
# Research Report:

## Valuation and Accounting Estimates under Ind AS: Sector-Wise Analysis

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# FOREWORD

Most large Indian companies are currently applying Indian Accounting Standards (Ind AS)[1], financial reporting framework that is based on the globally followed financial reporting standards. Ind AS is extensively based on fair valuation measurement base. Financial instruments, such as, investment in equity instruments and mutual fund units are required to be remeasured at fair value at every balance sheet date. Further, disclosure of fair values of certain assets and liabilities, such as financial assets, financial liabilities and investment properties, are required in the notes to financial statements even though they are not measured at fair value. There are other accounting areas, such as, share-based payments, plan assets of defined benefit plan asset, property, plant & equipment that are measured under revaluation model and assets and liabilities acquired in a business combination.

Ind AS framework has extensive application of fair valuation, management judgements and accounting estimation, most of which will have a significant effect on the reported financial results and financial position. For instance, changes in the underlying cash flow projections or discount rate may change the fair valuation of investments in equity shares. Information about the valuation assumptions, key judgements and accounting estimates made is of value to investors as it assists them to assess the financial position and performance, benchmark with peer companies and understand the sensitivities to changes in assumptions. Good quality of the disclosures and financial information provided in the financial statement, such as, quantitative sensitivity analysis or a range of possible outcomes, on how a change to a key accounting estimate could potentially affect the following year's results would enable the shareholders / users of the financial statements to assess the impact of management's accounting policy decisions and the likelihood of future changes in a way that generic disclosures do not.

Often accounting estimates may have a sectorial essence – the future occupancy rate estimate would be a key aspect of valuation/ impairment testing for hospitality companies, whilst the future passenger traffic estimate would be vital for valuation/ impairment testing for aviation companies. In this context, this publication intends to bring out significant sector-wise analysis of key areas of valuation and accounting estimation under Ind AS that have emerged in practice. As the nature and extent of fair valuation and accounting estimation varies from sector to sector due to the specific scenario within the business sector, we have identified the major areas of valuation and accounting estimation across the sectors, the categorization of which we have explained later in the publication. It must be noted that, company-specific situations, such as, the group structure, financing structure and the extent of treasury activities may also call for specific accounting estimation and management judgement.

In separate chapters, this publication also covers the key requirement for valuation, accounting estimates and management judgement under Ind AS. Our approach is to go beyond the realms of theoretical or conceptual requirements under Ind AS and look into the practicalities of how the sample companies are complying with the requirements. We have also provided the relevant extracts from the disclosures in the published financial statements of leading companies.

[1] Prescribed under Section 133 of Companies Act, 2013 as notified under Companies (Indian Accounting Standards) Rules, 2015

This publication is not meant to deal with the quantitative impact that the valuation and estimates under Ind AS may have caused from a capital markets or market capitalization perspective. This publication aims to assess the accounting impact on the Ind AS valuation and estimation for a wide cross-section of sectors with an objective to assist companies leverage on the experiences, thereby, providing them with a cutting edge for their financial reporting process.

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# Chapter 1: Summary of Findings: Key Sector-Wise Areas of Valuation and Accounting Estimates

**The table below summaries the major areas of valuation, accounting estimates and management judgement and the sectors mainly impacted.**

| Major Area of Impact | Key Areas of Ind AS Valuation, Judgement and Estimation | Main Sectors Impacted |
|---|---|---|
| Property, Plant & Equipment and Intangible Assets | - Impairment Reviews of Property, Plant and Equipment<br>- Review of Useful Life and Residual Value<br>- Intangible assets with Indefinite Useful lives<br>- Goodwill impairment review | - Retail<br>- Hospitality & Leisure<br>- Infrastructure<br>- Automotive<br>- Power & Utilities<br>- Telecommunications<br>- Extraction<br>- Fast Moving Consumer Goods |
| Financial Instruments | - Impairment of Financial Assets based on Expected loss model<br>- Valuation of Investments<br>- Valuation of Derivatives and Hedge Accounting | - Non-Banking Finance Companies<br>- Automotive<br>- Fast Moving Consumer Goods |
| Revenue | - Timing of Recognition of Revenue<br>- Deferral of Revenue due to Slow Progress of Completion<br>- Increase in Estimated Sales Returns | - Real Estate & Construction<br>- Transportation & Logistics<br>- Hospitality & Leisure<br>- Pharmaceuticals & Life Sciences<br>- Telecommunication |
| Leases | - Assessment of Lease Liabilities<br>- Lease Concessions | - Retail<br>- Transportation & Logistics<br>- Hospitality & Leisure<br>- Non-Banking Finance Companies<br>- Telecommunication |
| Deferred Tax | - Recoverability of Deferred Tax Assets<br>- Uncertain Tax Position | - Pharmaceutical & Life Sciences<br>- Technology & ITES<br>- Real Estate & Construction |

| | | |
|---|---|---|
| Inventory | - Estimation of Net Realisable Value of Inventories | - Extraction<br>- Retail<br>- Real Estate & Construction |
| Going Concern | - Going Concern Analysis | - Transportation & Logistics<br>- Hospitality & Leisure<br>- Telecommunication |
| Employee Benefits and Share-based Payments | - Actuarial Assumptions<br>- Share-Based Payment Arrangements<br>- Employee Incentive Plans | - Transportation & Logistics<br>- Hospitality & Leisure<br>- Fast Moving Consumer Goods<br>- Technology & ITES |
| Provisions | - Provision for Litigation<br>- Onerous Contracts<br>- Decommissioning obligation<br>- Warranty Obligations | - Pharmaceutical & Life Sciences<br>- Transportation & Logistics<br>- Fast Moving Consumer Goods<br>- Extraction |
| Liquidity issues, Borrowings, Debt Covenants and Going Concern | - Going Concern Assessment<br>- Debt Covenants<br>- Liquidity Issues<br>- Impairment | - Telecommunication<br>- Hospitality & Leisure<br>- Transportation & Logistics |

## Key Areas of Valuation and Accounting Estimates by Sector

| Sector | Impairment | Income Taxes | PPE/ Intangible Assets | Share-based Payments | Employee Benefits | Provisions/ Contingent Liabilities | Inventory | Revenue | Business Combination/ Consolidation | Leases | Liquidity issues, Borrowings, Debt Covenants and Going Concern | Valuation of Financial Instruments |
|---|---|---|---|---|---|---|---|---|---|---|---|---|
| **Retail** | ✓ | ✓ | ✓ | ✓ | ✓ | | ✓ | ✓ | | ✓ | | ✓ |
| **Hospitality & Leisure** | ✓ | ✓ | ✓ | | ✓ | ✓ | | ✓ | | ✓ | ✓ | ✓ |
| **Infrastructure** | ✓ | ✓ | ✓ | | | ✓ | | ✓ | | | | ✓ |
| **Automotive** | ✓ | ✓ | ✓ | | ✓ | ✓ | | | | | ✓ | ✓ |
| **Power & Utilities** | ✓ | ✓ | | | ✓ | | | ✓ | | | ✓ | ✓ |
| **Non-Banking Finance Companies** | ✓ | ✓ | ✓ | ✓ | ✓ | | | | | | | ✓ |
| **Fast Moving Consumer Goods** | ✓ | ✓ | ✓ | | ✓ | ✓ | | ✓ | ✓ | ✓ | | |
| **Real Estate & Construction** | ✓ | ✓ | | | | | ✓ | ✓ | | | | ✓ |
| **Pharmaceuticals & Life Sciences** | ✓ | ✓ | ✓ | | ✓ | ✓ | | ✓ | ✓ | ✓ | | ✓ |
| **Jewelry & Gems** | | ✓ | | | ✓ | | ✓ | ✓ | | ✓ | | ✓ |
| **Technology & ITES** | ✓ | ✓ | | | ✓ | ✓ | | | | ✓ | | ✓ |
| **Extraction** | ✓ | ✓ | | | ✓ | ✓ | | | | ✓ | ✓ | |
| **Telecommunication** | ✓ | ✓ | ✓ | ✓ | ✓ | ✓ | | ✓ | | ✓ | ✓ | |

# Chapter 2: Methodology of Our Approach

## 2.1 Coverage

2.1.1 In this publication, we have perused the annual or latest available financial results announced by 43 companies across 13 sectors for the financial years ended 31 March 2021. The selection was based on market capitalization of the companies and does not find adequate representations of a few sectors, such as, real estate, retail, transportation and jewelry & gems. Therefore, we have expanded our samples and included leading companies in respective sectors, so as to have a sample size of at least 3 companies. Whilst banking and financial services sector is included in the research, it must be noted that banks are currently not allowed to apply Ind AS. Therefore, the analysis is based on the Ind AS financial results of non-banking finance companies.

## 2.2 Sectors covered

| Sr. No. | Sector categorization | Number of companies covered |
|---|---|---|
| 1 | Automotive & Auto Components | 4 |
| 2 | Fast Moving Consumer Goods | 3 |
| 3 | Hospitality & Leisure | 4 |
| 4 | Infrastructure | 3 |
| 5 | Jewelry & Gems | 3 |
| 6 | Financial Services | 4 |
| 7 | Oil & Gas | 3 |
| 8 | Power & Utilities | 3 |
| 9 | Pharmaceuticals & Life Sciences | 3 |
| 10 | Real estate & construction | 3 |
| 11 | Retail | 4 |
| 12 | Technology & IT Enabling Services | 3 |
| 13 | Transportation & Logistics | 3 |

## 2.3 Basis

2.3.1 The publication analysis are primarily based on the disclosures provided by the selected companies in their financial results.

# Chapter 3: Key Areas of Valuation and Estimation uncertainties under Ind AS

This chapter deals with the key areas of valuation and accounting estimates.

## 3.1 Impairment of Goodwill and Other Non-financial Assets

### 3.1.1 Key Ind AS Requirement

| | |
|---|---|
| **Impairment of Goodwill and Intangible assets with Indefinite Useful Lives** | • An entity is required to assess, at the end of each reporting period, whether there is any impairment for an entity's non-financial assets.<br>• Under Ind AS 36, cash-generating unit (CGU) to which goodwill is allocated are tested for impairment annually on each balance sheet date, or more frequently when there is an indication that the unit may be impaired.<br>• If the recoverable amount of the CGU is less than the carrying amount of the unit, the impairment loss is allocated first to reduce the carrying amount of any goodwill allocated to that unit and then to the other assets of the unit pro rata on the basis of carrying amount of each asset in the unit.<br>• Goodwill impairment loss recognized is not reversed in subsequent period. |
| **Impairment of Property, plant & Equipment (PPE) and Intangible assets with finite Useful Lives** | • On each balance sheet date, an entity assesses whether there is any indication that any PPE or intangible assets with finite lives may be impaired.<br>• If any such impairment exists, the recoverable amount of an asset is estimated to determine the extent of impairment, if any.<br>• Where it is not possible to estimate the recoverable amount of an individual asset, we estimate the recoverable amount of the CGU to which the asset belongs.<br>• Intangible assets with indefinite useful lives and intangible assets not yet available for use are tested for impairment annually on each balance sheet date, or earlier if there is an indication that the asset may be impaired. |
| **Impairment testing** | • The recoverable amount is the higher of fair value less costs to sell and value-in-use (VIU).<br>• In assessing VIU, the estimated future cash flows are discounted to their present value using a pre-tax discount rate that reflects current market assessments of the time value of money and the risks specific to the asset for which the estimates of future cash flows have not been adjusted.<br>• If the recoverable amount of an asset (or CGU) is estimated to be less than its carrying amount, the carrying amount of the asset (or CGU) is reduced to its recoverable amount.<br>• If this occurs, an impairment loss is recognized immediately in the profit and loss account. |

### 3.1.2 Key Disclosures

Where an impairment charge is recognised, Ind AS 36 requires disclosure of significant assumptions used in calculating the impairment, the events and circumstances that led to the impairment, and the composition of CGUs. Some points that may be considered while providing these disclosures are:

- The objective of this disclosure requirement is to convey how the impairment charge arose and how was the same determined. While providing this disclosure, entities may consider following points:
    - What sensitivity analysis or iterations of scenarios were considered by the management to estimate the recoverable amount?
    - What are the key assumptions used for each scenario in order to determine the impairment charge?
    - How were the alternative scenarios developed?
    - How much weightage of probabilities were assigned to each scenario and what was the basis of determining the same?
    - How was the WACC or the discount rate used determined?

When an impairment charge is reversed as per the requirements of Ind AS 36, there are different disclosures required. Also, it must be noted that when the recoverable amount exceeds the carrying amount of the asset/ CGU (there is no impairment charge), but there is only a 'thin' headroom or the recoverable amount is dependent on a significant assumption for its support, it would be expected that the entity provides appropriate disclosures about the key judgments and estimates. Further, in such a case, if a reasonably possible change in a key assumption would result in the carrying amount of the asset or CGU exceeding its recoverable amount, there are additional disclosures are required by Ind AS 36.

### 3.1.3 Key Assumptions

- Forecast cash flows including assumptions on growth rates
- Discount rates
- Terminal growth rate
- Economic and entity specific factors incorporated in the valuation.

### 3.1.4 Discount rate

Under Ind AS 36, the discount rate used for the purpose of impairment testing shall be a pre-tax rate that reflects the current market assessments of:

- the time value of money and
- the risks specific to the asset for which the future cash flow estimates have not been adjusted

Following the onset of the COVID-19 outbreak, for financial year ended March 31, 2020 many companies concluded that while determining the discount rate, using spot country risk premiums would not give a discount rate that a market participant would expect at the balance Sheet date in determining the present value of cash flows over a long term period. For financial year ended March 31, 2021, due to reduction in the market volatility many companies reverted to using a spot rate.

Discount rate range observed amongst sample companies:

| Sector | Discount Rate |
|---|---|
| Automotive | 12.00% - 25.00% |
| Extraction | 9.60% - 14.29% |
| Consumer Goods | 8.90% - 14.40% |
| Hospitality & Leisure | 11.00% - 12.50% |
| Power & Utilities | 8.86% - 14.50% |
| Real Estate & Construction | 11.90% - 12.75% |
| Steel | 8.00% - 10.00% |
| Telecommunications | 10.00% - 11.48% |

### 3.1.5 Terminal Growth rate

Under Ind AS 36, impairment testing requires estimation of cash flow projections beyond the period covered by the most recent budgets/forecasts by extrapolating them using a steady or declining growth rate for subsequent years, unless an increasing rate can be justified. This growth rate must not exceed the long-term average growth rate for the products, industries, or country or countries in which the entity operates, or for the market in which the asset is used, unless a higher rate can be justified.

Growth rate range observed amongst sample companies:

| Sector | Growth Rate |
|---|---|
| Automotive | 2.00% - 7.00% |
| Extraction | 0.30% - 2.00% |
| Consumer Goods | 3.50% - 6.00% |
| Hospitality & Leisure | 3.00% - 3.50% |
| Steel | 0% - 1.25% |
| Telecommunications | 2.51% - 5.11% |

## 3.2 Impairment of Financial Assets

### 3.2.1 Key Estimation Uncertainties

Ind AS 109 *Financial Instruments* requires an entity to incorporate reasonable and supportable information about past events, current conditions and the forecast of future economic conditions into the assessment of expected credit losses (ECL) for financial assets not measured at fair value through profit or loss. ECL is a probability weighted amount that is determined by evaluating a range of possible outcomes.

ECL is a probability weighted amount that is determined by evaluating a range of possible outcomes. The impact from the outbreak may vary depending on an entity's specific situation and its methodology in assessing ECL. Accordingly, management should ensure that there is reasonable and supportable consideration of past events, current conditions and forecast of future economic conditions when making that assessment.

When considering the Ind AS 109 requirements to incorporate the forecast of future economic conditions on a probability weighted basis, from a technical standpoint, an entity should evaluate the likelihood of the occurrence of an event (i.e., in this case its severity and the potential impact leading to an epidemic) if this would significantly affect the estimation of expected losses of financial assets. In assessing the expected credit loss, management should consider reasonable and supportable information at the reporting date.

The implications could vary depending on an entity's specific situation and its methodology in assessing ECL. For example, financial institutions may incorporate estimates of forward-looking macro-economic factors into multiple scenarios about the future economy.

ECL may increase due to an increase in both the probability of default ('PD') and the loss given default ('LGD') for financial assets. 12- month PD is required to be estimated for all ECL calculations.

### 3.2.2 Relevant Extracts of Credit Risk Management/ Expected Credit Loss Disclosures from Published Financial Statements

**(i) Extracts from Disclosures provided by certain non-NBFC companies**

***Extract from Company 1***

*Our historical experience of collecting receivables indicate a low credit risk. Hence, trade receivables are considered to be a single class of financial assets.*

***Extract from Company 2***

*The Company has established a credit policy under which each new customer is analysed individually for creditworthiness before entering into contract. Sale limits are established for each customer, reviewed regularly and any sales exceeding* *those limits require approval from the appropriate authority. There are no significant concentrations of credit risk within the Group.*

*The average credit period ranges from 30 to 45 days on sales of products. Credit risk arising from trade receivables is managed in accordance with the Company's established policy, procedures and control relating to customer credit risk management. Credit quality of a customer is assessed based on a detailed study of credit worthiness and accordingly individual credit limits are defined/modified. The concentration of credit risk is limited due to the fact that the customer base is large. There is no customer representing more than 5% of the total balance of trade receivables*

| ***Net Outstanding > 365 days*** | ***% Collection to gross outstanding in current year*** | ***Credit loss allowance*** |
|---|---|---|
| *Yes* | *< 25%* | *Yes, to the extent of lifetime expected credit losses outstanding as at reporting date.* |
| *Yes* | *> 25%* | *Yes, to the extent of lifetime expected credit losses pertaining to balances outstanding for more than one year* |

***Extract from Company 3***

*Company's deployment in debt instruments are primarily in fixed deposits with highly rated banks and companies, bonds issued by government institutions, public sector undertakings and certificate of deposits issued by highly rated banks and financial institutions. Of this, investments that are held at amortised cost stood at …. With respect to the Company's investing activities, counter parties are shortlisted and exposure limits determined on the basis of their credit rating (by independent agencies), financial statements and other relevant information. As these counter parties are Government institutions /public sector undertakings with investment grade credit ratings and taking into account the experience of the Company over time, the counter party risk attached to such assets is considered to be insignificant. The Company's customer base is large and diverse limiting the risk arising out of credit concentration. Further, credit is extended in business interest in accordance with guidelines issued centrally and business-specific credit policies that are consistent with such guidelines. Exceptions are managed and approved by appropriate authorities, after due consideration of the counterparty's credentials and financial capacity, trade practices and prevailing business and economic conditions.*

***Extract from Company 4***

*The Company has used practical expedient by computing expected credit loss allowance for trade receivable by taking into consideration payment profiles of sales over a period of 36 months before the reporting date and the corresponding historical credit loss experiences within this period. The historical loss rates are adjusted to reflect current and forward looking information on macro economic factors affecting the ability of the customers to settle the receivables. The expected credit loss is based on the ageing of the days, the receivables due and the expected credit loss* *rate. In addition, in case of event driven situation as litigations, disputes, change in customer's credit risk history, specific provisions are made after evaluating the relevant facts and expected recovery. Refer Note No…. for ECL provisioning and its movement on financial assets carried at amortised cost. Concentration risk: As at the year ending March 31, 2021, two customers are exceeding 10% of the Company's total trade receivables, which was nil as at March 31, 2020. However, these customers do not contribute to more than 10% of the revenue of the Company.*

*In addition the Company is exposed to credit risk in relation to financial guarantees given by the Company on behalf of its subsidiaries and joint operations (net of Company's share). The Company's maximum exposure in this respect is the maximum amount the Company could have to pay if the guarantee is called on (net of Company's share in joint operations), as at March 31, 2021 …. These financial guarantees have been issued to the banks / customers on behalf of the subsidiaries and joint operations under the agreements entered into by the subsidiaries/ Joint operations with the banks / customers. Based on management's assessment as at the end of the reporting period, the Company considers the likelihood of any claim under the guarantee is remote.*

*The company catogarises financial assets based on the assumptions, inputs and factors specific to the class of financial assets into High-quality assets, negligible credit risk; Quality assets, low credit risk; Standard assets, moderate credit risk; Substandard assets, relatively high credit risk; Low quality assets, very high credit risk; Doubtful assets, credit-impaired. Financial assets are written off when there is no reasonable expectations of recovery, such as a debtor failing to engage in a repayment plan with the Company. The Company categorises a loan or receivable for write off when a debtor fails to make contractual payments greater than one year past due. Where loans or receivables have been written off, the Company continues engage in enforcement activity to attempt to recover the receivable due. Where recoveries are made, these are recognized in profit or loss.*

***Provision for expected credit losses:***

| ***Description of category*** | ***Category*** | ***Basis for recognition of expected credit loss provision*** | | |
|---|---|---|---|---|
| | | ***Investments*** | ***Loans and deposits*** | ***Trade Receivables*** |
| *Assets where the counter-party has strong capacity to meet the obligations and where the risk of default is negligible or nil* | *High-quality assets, negligible credit risk* | *12 month expected credit losses* | *12 month expected credit losses* | |
| *Assets where there is low risk of default and where the counter-party has sufficient capacity to meet the obligations and where there has been low frequency of defaults in the past* | *Quality assets, low credit risk* | | | |

<table>
<tr><td>Assets where the probability of default is considered moderate, counter-party where the capacity to meet the obligations is not strong</td><td>Standard assets, moderate credit risk</td><td></td><td></td><td rowspan="3">Life time expected credit losses (simplified approach)</td></tr>
<tr><td>Assets where there has been a significant increase in credit risk since initial recognition. Assets where the payments are more than 180 days past due</td><td>Substandard assets, relatively high credit risk</td><td rowspan="2">Life-time expected credit losses</td><td rowspan="2">Life-time expected credit losses</td></tr>
<tr><td>Assets where there is a high probability of default. In general, assets where contractual payments are more than 180 days past due are categorised as low quality assets. Also includes assets where the credit risk of counter-party has increased significantly though payments may not be more than 180 days past due</td><td>Low quality assets, very high credit risk</td></tr>
<tr><td>Assets are written off when there is no reasonable expectation of recovery, such as a debtor declaring bankruptcy or failing to engage in a repayment plan with the company. The company categorises a loan or receivable for write off when a debtor fails to make contractual payments greater than 365 days past due. Where loans or receivables have been written off, the company continues to engage in enforcement activity to attempt to recover the receivable due. Where recoveries are made, these are recognised in profit or loss.</td><td>Doubtful assets, credit-impaired</td><td colspan="3">Asset is written off</td></tr>
</table>

## (ii) Extracts from Disclosures provided by an NBFC

*Inputs considered in the ECL model*

*In assessing the impairment of financial loans under Expected Credit Loss (ECL) Model, the assets have been segmented into three stages. The three stages reflect the general pattern of credit deterioration of a financial instrument. The differences in accounting between stages, relate to the recognition of expected credit losses and the measurement of interest income. The Company categorises loan assets into stages primarily based on the Months Past Due status.*

*Stage 1: 0-30 days past due*

*Stage 2: 31-90 days past due*

*Stage 3: More than 90 days past due*

*The Company applies the simplified approach to providing for expected credit losses prescribed by Ind AS 109, which permits the use of the lifetime expected loss provision for trade advances. The Company has computed expected credit losses based on a provision matrix which uses historical credit loss experience of the Company.*

*(i) Definition of default The Company considers a financial asset to be in "default" and therefore Stage 3 (credit impaired) for ECL calculations when the borrower becomes 90 days past due on its contractual payments.*

*(ii) Exposure at default "Exposure at Default" (EAD) represents the gross carrying amount of the assets subject to impairment calculation. Future Expected Cash flows (Principal and Interest) for future years has been used as exposure for Stage 2.*

*(iii) Estimations and assumptions considered in the ECL model*

*The Company has made the following assumptions in the ECL Model:*

*a. "Loss given default" (LGD) is common for all three Stages and is based on loss in past portfolio. Actual cashflows on the past portfolio are discounted at portfolio EIR rate for arriving loss rate.*

*b. "Probability of Default" (PD) is applied on Stage 1 and Stage 2 on portfolio basis and for Stage 3 PD at 100%. This is calculated as an average of the last 60 months yearly movement of default rates and future adjustment for macro-economic factor*

*(iv) Measurement of ECL: ECL is measured as follows:*

*- financial assets that are not credit impaired at the reporting date: for Stage 1, gross exposure is multiplied by PD and LGD percentage to arrive at the ECL. For Stage 2, future Expected Cash flows (Principal and Interest) for respective future years is multiplied by respective years Marginal PDs and LGD percentage and thus arrived ECL is then discounted with the respective loan EIR to calculate the present value of ECL. In addition, in case of Bills discounting and Channel finance, as the average lifetime is of 90 days, a time to maturity factor of 0.25 is used in the ECL computation.*

*- financial assets that are credit impaired at the reporting date: the difference between the gross exposure at reporting date and computed carrying amount considering EAD net of LGD and actual cash flows till reporting date;*

*- undrawn loan commitments: as the present value of the difference between the contractual cash flows that are due to the Company if the commitment is drawn down and the cash flows that the Company expects to receive.*

*(v) Forward Looking Information Historical PDs has been converted into forward looking PD which incorporates the forward-looking economic outlook. Considering that major chunk of borrowers in the retail portfolio is from rural area, Agriculture (real change % p.a.) is used as a macroeconomic variable. Agriculture (real change % p.a.) stands for Percentage change in real agricultural value-added, including livestock, forestry and fishing, over previous year. In case of SME and Bills Discounting portfolio, Real GDP (% change p.a.) is used as the macroeconomic variable. The macroeconomic variables considered by the Company are robust reflections of the state of economy which result into systematic risk for the respective portfolio segments. Additionally, three different scenarios have been considered for ECL calculation. Along with the actual numbers (considered for Base case scenario), other scenarios take care of the worsening as well as improving forward looking economic outlook.*

*(vi) Assessment of significant increase in credit risk When determining whether the credit risk has increased significantly since initial recognition, the Company considers both quantitative and qualitative information and analysis based on the Company's historical experience, including forward-looking information. The Company considers reasonable and supportable information that is relevant and available without undue cost and effort. The Company's accounting policy is not to use the practical expedient that the financial assets with 'low' credit risk at the reporting date are deemed not to have had a significant increase in credit risk.*

*As a result, the Company monitors all financial assets and loan commitments that are subject to impairment for significant increase in credit risk. As a part of the qualitative assessment of whether a customer is in default, the Company also considers a variety of instances that may indicate unlikeliness to pay. In such instances, the Company treats the customer at default and therefore assesses such loans as Stage 3 for ECL calculations, following are such instances:*

*- A Stage 3 customer having other loans which are in Stage 1 or 2.*

*- Customers who have failed to pay their first EMI.*

*- Physical verification status of the repossessed asset related to the loan.*

*- Cases where Company suspects fraud and legal proceedings are initiated.*

## 3.3 Income Taxes

### 3.3.1 Key Estimation Uncertainties


Under Ind AS 12, a deferred tax asset shall be recognised for the carry forward of unused tax losses and unused tax credits to the extent that it is probable that future taxable profit will be available against which the unused tax losses and unused tax credits can be utilised. With some exceptions, deferred tax assets arising from deductible temporary differences and carry forward of unused tax losses and credits are recognised to the extent that sufficient future taxable profit will be available against which the deductible temporary differences will be utilised. With regard to probability of taxable profit in future, Ind AS 12 identifies the sources of taxable profits against which an entity can utilise deductible temporary differences. They include:

- future reversal of existing taxable temporary differences;

- taxable profit in future periods; and

- tax planning opportunities.

Recoverability of deferred tax asset is an accounting estimate which is generally based on management's assumptions relating to projections of future taxable profits which are in turn driven by forecast sales, cost incurred, cash flows, impairment assessments, future recoverability or settlement of an asset and liability etc.

Further, under Ind AS 12, an entity is required to periodically evaluate positions taken in its tax returns with respect to situations in which applicable tax regulations are subject to interpretation and consider whether it is probable that a taxation authority will accept an uncertain tax treatment. The entity should reflect the effect of uncertainty for each uncertain tax treatment by using either most likely method or expected value method, depending on which method predicts better resolution of the treatment.

### 3.3.2 Relevant Extracts from Published Financial Statements of Sample Companies

***Extract from Company 1***

*MAT Credit not recognised as at March 31, 2021 is INR …. The Company continues not to recognise such MAT credit as a component of deferred tax asset in the balance sheet, on the basis of the assessment made by the Company's management of the profitability and operational plans in the foreseeable future, the Company's management is of the view that presently, there is no convincing evidence supporting the probability that the Company would be liable to pay income tax under the normal provisions of the Income-*

*tax Act for the periods up to which the Company is eligible to utilise the unused MAT credit, specifically considering the available deductions/ benefits etc. under the normal provisions under the Income Tax Act. Further, and notwithstanding the foregoing, the Company can elect to exercise the option permitted u/s 115BAA of the Income- tax Act, 1961 consequent to which the entire MAT credit would no longer be allowed for utilisation.*

*However, during the year, the Company was in a situation where it ended up utilising unrecognised MAT credit of INR … Million as it had to pay income tax under the normal provisions under the Income Tax Act despite the availability of the deductions/ benefits as the actual profits far exceeded the estimates made in the previous year in view of unanticipated increase in sales of certain products during the year where the probability of recurrence in the foreseeable future cannot be determined at present.*

***Extract from Company 2***

*The Company has carry forward tax losses, unabsorbed depreciation and MAT credit that are available for offset against future taxable profit. Deferred tax assets are recognised only to the extent that it is probable that taxable profit will be available against which the unused tax losses or tax credits can be utilized. This involves an assessment of when those assets are likely to reverse, and a judgement as to whether or not there will be sufficient taxable profits available to offset the assets. This requires assumptions regarding future profitability, which is inherently uncertain. To the extent assumptions regarding future profitability change, there can be an increase or decrease in the amounts recognised in respect of deferred tax assets and consequential impact in the statement of profit and loss.*

*The total deferred tax assets recognised in these financial statement …includes MAT credit entitlements of ….(31 March 2020: ….), of which ….is expected to be utilised in the fourteenth year (FY 19-20: … was expected to be utilised in fourteenth and fifteenth year), fifteen years being the maximum permissible time period to utilise the MAT credits.*

*Additionally, the Company has tax receivables on account of refund arising on account of past amalgamation and relating to various tax disputes. The recoverability of these receivables involve application of judgement as to the ultimate outcome of the tax assessment and litigations. This pertains to the application of the legislation, which in certain cases is based upon management's interpretation of country specific tax law, in particular India, and the likelihood of settlement. Management uses in-house and external legal professionals to make informed decision.*

***Extract from Company 3***

*In the absence of reasonable certainty, the Company has not recognised deferred tax assets (DTA) on mark to market loss on equity shares of ….*

## 3.4 Revenue

| Key Area of Estimation | Ind AS 115 Requirement |
|---|---|
| Discounts and Rebates to customers | Under Ind AS 115, revenue is measured on the basis of contracted price, after deduction of any trade discounts, volume rebates and any taxes or duties. An entity is required to estimate the provision for such discounts and rebates. Revenue is only recognised to the extent that it is highly probable a significant reversal will not occur. |

***Extract from Company 1***

*Revenue is measured based on the transaction price, which is the consideration, adjusted for volume discounts, rebates, scheme allowances, price concessions, incentives, and returns, if any, as specified in the contracts with the customers. …Accruals for discounts/incentives and returns are estimated (using the most likely method) based on accumulated experience and underlying schemes and agreements with customers. Due to the short nature of credit period given to customers, there is no financing component in the contract.*

| Key Area of Estimation | Ind AS 115 Requirement |
|---|---|
| Customers' Right to Returns | When a customer has a right to return the product within a given period, an entity is requited to recognise a provision for sales return. This is measured on the basis of average past trend of sales return as a percentage of sales. Revenue is adjusted for the expected value of the returns and cost of sales are adjusted for the value of the corresponding goods to be returned. |

***Extract from Company 1***

*Revenue is recognised net of accrual for chargeback, rebates, sales returns and discounts, etc. The estimates relating to the accruals are important given the significance of revenue and also considering the distinctive terms of arrangement with customers. These estimates are complex and require significant judgement and estimation by the Company for establishing an appropriate accrual. Accuracy of revenues may deviate on account of change in judgements and estimates.*

| Key Area of Estimation | Ind AS 115 Requirement |
|---|---|
| Revenue under Percentage of Completion method | • When an entity recognises revenue on the basis of stage of completion in proportion of the contract costs incurred at balance sheet date, relative to the total estimated costs of the contract at completion, there are estimates in relation to total estimated costs of each such contract. Significant judgements are also involved in determining the expected losses, when such losses become probable based on the expected total contract cost.<br><br>• Cost contingencies may include in these estimates to take into account specific risks of uncertainties or disputed claims arising within each contract. These contingencies are required to be reviewed by the entity on a regular basis throughout the life of the contract and adjusted where appropriate.<br><br>• The revenue on contracts may also include variable consideration (variations and claims). Variable consideration is recognised when the recovery of such consideration is highly probable |

***Extract from Company 1***

*The percentage-of-completion (POC) method places considerable importance on accurate estimates to the extent of progress towards completion and may involve estimates on the scope of deliveries and services required for fulfilling the contractually defined obligations. These significant estimates include total contract costs, total contract revenues, contract risks, including technical, political and regulatory risks, and other judgments. The Company re-assesses these estimates on periodic basis and makes appropriate revisions accordingly.*

*Provision for liquidated damages*

*Liquidated damages are provided based on contractual terms when the delivery / commissioning dates of an individual project have exceeded or are likely to exceed the delivery / commissioning dates as per the respective contracts. This expenditure is expected to be incurred over the respective contractual terms up to closure of the contract (including warranty period). Provision for loss orders A provision for expected loss on construction contracts is recognised when it is probable that the contract costs will exceed total contract revenue. For all other contracts, loss order provisions are made when the unavoidable costs of meeting the obligation under the contract exceed the currently estimated economic benefits.*

## 3.5 Leases

| Key Area of Estimation | Ind AS 116 Requirement |
|---|---|
| Determining the lease term | Under Ind AS 116, an entity being a lessee is required to determine the lease term as the non-cancellable period of a lease adjusted with any option to extend or terminate the lease, if the use of such option is reasonably certain. If it is reasonably certain that a lease will be extended / will not be early terminated, an entity is required to estimate the expected lease period which may be different from the contractual tenure.<br>An entity may have various lease agreements with a right to extend / renew / terminate wherein it considers the nature of the contractual terms and economic factors to determine the lease term. |

***Extract from Company 1***

*Leases under Ind AS 116*

*Termination options*

*Termination options are included in a number of property and equipment leases across the Company, where the Company is a lessee. These terms are used to maximise operational flexibility in terms of managing contracts. The majority of termination options held are exercisable only by the Company and not by the respective lessor. In determining the lease term, management considers all facts and circumstances that create an economic incentive not to exercise a termination option. Periods after termination options are only included in the lease term if the lease is reasonably certain to be not terminated by the Company. The assessment is reviewed if a significant event or a significant change in circumstances occurs which affects this assessment and that is within the control of the lessee*

***Extract from Company 2***

*Critical Judgements in determining the Lease Term: Ind AS 116 requires lessees to determine the lease term as the non-cancellable period of a lease adjusted with any option to extend or terminate the lease, if the use of such option is reasonably certain. The Company makes an assessment on the expected lease term on a lease-by-lease basis and thereby assesses whether it is reasonably certain that any options to extend or terminate the contract will be exercised. In evaluating the lease term, the Company considers factors such as any significant leasehold improvements undertaken over the lease term, costs relating to the termination of the lease and the importance of the underlying asset to Company's operations taking into account the location of the underlying asset and the availability of suitable alternatives. The lease term in future periods is reassessed to ensure that the lease term reflects the current economic circumstances.*

| Key Area of Estimation | Ind AS 116 Requirement |
| --- | --- |
| Determining the incremental borrowing rate for lease contracts | The initial recognition of lease liabilities at present value requires the identification of an appropriate discount rate. An entity has to determine the incremental borrowing rate based on considerations specific to the leases by taking consideration of the risk free borrowing rates as adjusted for country / company specific risk premiums (basis the readily available data points). |

***Extract from Company 1***

*The Company cannot readily determine the interest rate implicit in the lease, therefore, it uses its incremental borrowing rate (IBR) to measure lease liabilities. The IBR is the rate of interest that the Company would have to pay to borrow over a similar term, and with a similar security, the funds necessary to obtain an asset of a similar value to the right-of-use asset in a similar economic environment. The Company estimates the IBR using observable inputs (such as market interest rates) when available and is required to make certain specific estimates such as Company's credit rating.*

## 3.6 Valuation of Financial Instruments

### 3.6.1 Key Requirements

Ind AS 109 requires investments in equity instruments to be fair valued, with the exception of investments in subsidiaries, associates and joint venture in separate financial statements of parent or investor which are accounted for either at cost or at fair value. If an equity investment is not held for trading, an entity can make an irrevocable election at initial recognition to measure it fair value through other comprehensive income (FVOCI) rather than at FVPL.

There is no exception for investment in unquoted equity investments and, therefore, an entity can not measure its investments in unquoted equity investments (except in subsidiary, joint venture or associate company) at cost. This is practically challenging for many companies as there may be several practical challenges such as, lack of availability of relevant financial information such as, cash flow projections, appropriate peer company, lack of reliable valuation inputs, etc.

### 3.6.2 Relevant Extracts with respect to Valuation assumption/ inputs used for Investment in Unquoted Equity Investments

***Extract from Company 1***

*Fair valuation of Unquoted Equity Investments*

*The Investments measured at fair value (FVTOCI) and falling under fair value hierarchy Level 3 are valued on the basis of valuation reports provided by external valuers with the exception of certain investments, where cost has been considered as an appropriate* *estimate of fair value because of a wide range of possible fair value measurements and cost represents the best estimate of fair values within that range. The Company considers Comparable Companies Method (CCM) method and the illiquidity discount based on its assessment of the judgement that market participants would apply for measurement of fair value of unquoted investments. In the CCM method, the Company would find comparable listed entities in the market and use the same PE multiple (ranging from 8.8 to 19.4) for determining the fair value of the investment.*

***Extract from Company 2***

*Costs of certain unquoted equity instruments have been considered as an appropriate estimate of fair value because these investments are subject to a wide range of possible fair value measurements and cost represents the best estimate of fair value within that range. These investments in equity instruments are not held for trading. Instead, they are held for medium or long term strategic purpose. Upon the application of Ind AS 109, the Company has chosen to designate these investments in equity instruments at FVTOCI as the directors believes this provides a more meaningful presentation for medium or long term strategic investments, than reflecting changes in fair value in profit or loss.*

***Extract from Company 3***

*Cost of unquoted equity instruments has been considered as an appropriate estimate of fair value because of a wide range of possible fair value measurements and cost represents the best estimate of fair value within that range.*

***Extract from Company 4***

*Certain unquoted investments are not held for trading, instead they are held for medium or long term strategic purpose. Upon the application of Ind AS 109 'Financial Instruments', the Company has chosen to designate these investments in equity instruments as at FVTOCI as the management believe this provides more meaningful presentation for medium and long term strategic investments, then reflecting changes in fair value immediately in profit or loss.*

*The cost of certain unquoted investments approximate their fair value because there is a wide range of possible fair value measurements and the cost represents the best estimate of fair value within that range.*

*Ind AS 109 also requires investments in mutual funds and derivative contracts held by an entity to be measured at fair value through profit and loss account, except if certain criteria for hedge accounting are met.*

### 3.6.3 Relevant Extracts with respect to Valuation assumption/ inputs used for other Financial Instruments

***Extract from Company 1***

*To provide a meaningful assessment of the foreign currency risk associated with the Group's foreign currency derivative positions against off-balance sheet exposures and unhedged portion of on-balance sheet financial assets and liabilities, the Group uses a multi-currency correlated value-at-risk ("VAR") model. The VAR model uses a Monte*

*Carlo simulation to generate thousands of random market price paths for foreign currencies against Indian Rupee taking into account the correlations between them. The VAR is the expected loss in value of the exposures due to overnight movement in spot exchange rates, at 95% confidence interval. The VAR model is not intended to represent actual losses but is used as a risk estimation tool. The model assumes normal market conditions and is a historical best fit model. Because the Group uses foreign currency instruments for hedging purposes, the loss in fair value incurred on those instruments are generally offset by increase in the fair value of the underlying exposures for on-balance sheet exposures. The overnight VAR for the Group at 95% confidence level is R 203.08 crore as at March 31, 2021 and R 111.39 crore as at March 31, 2020. Actual future gains and losses associated with the Group's investment portfolio and derivative positions may differ materially from the sensitivity analysis performed as at March 31, 2021 due to the inherent limitations associated with predicting the timing and amount of changes in foreign currency exchange rates and the Group's actual exposures and position.*

***Extract from Company 2***

*The fair value of liquid mutual funds and long term equity investment is based on active market. Fair values of certain non-current investment are valued based on discounted cash flow/book value/EBITDA multiple approach. Derivative financial instruments are generally valued based on Black-Scholes-Merton approach/ Dollar offset principles.*

***Extract from Company 3***

*Fair value of the government securities are based on the price quotations near the reporting date. Fair value of the unquoted equity shares have been estimated using market comparable method. The valuation requires management to make certain assumptions about the marketability, active market price, discount rate, credit risk and volatility. The probabilities of the various estimates within the range can be reasonably assessed and are used in management's estimate of fair value for those unquoted equity investments.*

*The fair value of debentures is determined by using the quoted prices. The own non-performance risk as on 31st March, 2021 was assessed to be insignificant.*

***Extract from Company 4***

*Fair value of investment in preference shares is estimated through a valuation model incorporating assumptions which includes unobservable market data and by discounting the expected future cash flows using a discount rate equivalent to the expected rate of return for a similar instrument and maturity as on the reporting date. Key inputs to the valuation model are expected cash flows and discount rate expected for an instrument with similar terms and maturity as on the reporting date.*

*Fair value of investments in preference share of XXX is dependent on its profitability and cash flows available for distribution. The expected cash flows have been discounted considering a pre-tax discount rate of 13.84% (March 31, 2020: 11.90%). The fair value is sensitive to changes in discount rate and profitability. An increase in cash flow by 1% would lead to an increase in fair value of preference shares by ₹… crore (March 31, 2020: ₹… crore) and increase in discount rate by 1% would lead to decrease in fair value by ₹… crore (March 31, 2020: ₹….crore).*

## 3.7 Business Combinations

### 3.7.1 Key Requirements

Under Ind AS 103, acquisition of a subsidiary that constitutes a business to be accounted using purchase price allocation method, irrespective of their legal form. This involves all identifiable assets and liabilities of the acquired entity would be recorded in the acquirer's books at fair values as on the acquisition date. Purchase consideration payable is also measured at fair value. Any excess consideration paid/payable over the fair value of the identifiable net assets is recorded as goodwill. In case the fair value of the identifiable net assets is higher than the consideration, the gain is recorded as capital reserve.

***Extract from Company 1***

*The carrying amount of all assets and liabilities within the working capital equals their fair value. None of the Trade receivables was impaired and the full contractual amount were expected to be realised. Mining Rights have been valued considering the With or Without method, i.e. based on the cost savings resulting from the usage of the mines vis a vis procurement of raw material (chrome ore) from external vendors. Land has been valued based on the Right to Fair Compensation and Transparency in Land Acquisition, Rehabilitation and Resettlement Act. Buildings, Plant & Machinery, Other Tangible Assets, Capital Work-in-Progress and Capital Advances pertaining to the Tangible Assets together have been estimated based on the Value in Use of … (acquired company) under the Income Approach.*

*Non-controlling interest has been measured at the non-controlling interest's proportionate share of FPL's identifiable net assets.*

***Extract from Company 2***

*Deferred contingent consideration*

*Based on actual performance in financial year 2020-21, contingent consideration paid and current view of future projections for the brand, the Company has reviewed and fair valued the deferred contingent consideration so payable. As at 31st March, 2021, the fair value of the contingent consideration is … crores which is classified as other financial liability. The determination of the fair value as at Balance Sheet date is based on discounted cash flow method. The key input used in determining the fair value of deferred contingent consideration were domestic turnover projection of the brand.*

*Determination of the fair value as at balance sheet date is based on discounted cash flow method. Contingent consideration is arrived basis weighted average probability approach of achieving various financial and non-financial performance targets.*

*The main assets acquired were Right to use XXX brand which were valued using the income approach model by estimating future cashflows generated by these assets and* *discounting them to present value using rates in line with a market participant expectation.*

*In addition, as applicable, Property plant & equipment have been valued using the market comparison technique and replacement cost method.*

*The gross contractual value and fair value of trade and other receivables as at the dates of acquisition amounted to … crores which is expected to be fully recoverable.*

## 3.8 Inventories

### 3.8.1 Key Requirements

Under Ind AS 2, inventories are valued at lower of cost and net realizable value. Cost of inventories, comprise costs of purchase and other costs incurred in bringing the inventories to their present condition and location. Net realizable value is the estimated selling price in the ordinary course of business less the estimated costs of completion and the estimated cost necessary to make the sale.

***Extract from Company 1***

*The company has calculated the provision for inventory basis the percentage as per historical experience for inventory lying from the last inventory count date to the reporting date.*

***Extract from Company 2***

*Evaluation of Net realisable Value of Inventories Inventories comprising of finished goods and construction-work-in progress are valued at lower of cost and net realisable value. Net Realisable value is based upon the estimates of the management. The effect of changes, if any, to the estimates is recognised in the Standalone Financial Statements for the period in which such changes are determined.*

## 3.9 Property, Plant & Equipment and Intangible Assets

### 3.9.1 Key Requirements

Ind AS 16 requires depreciation to be based on the estimated useful life of assets. Also, it is required to estimate the residual value, useful life and depreciation method to be reviewed at least at the end of each financial year. Any changes to these estimates are required to be accounted on a prospective basis.

Ind AS 38 states that the useful life of an intangible can be assessed as finite or indefinite. Useful lives of intangible assets with finite useful life are determined based on management's estimate which is reviewed at least annually. An intangible can be assessed to have an indefinite useful life if there is no foreseeable limit over which it is expected to generate economic benefits for the company. Generally, brands with certain attributes may qualify for assessment as with indefinite lives.

***Extract from Company 1***

*The estimated useful lives, residual values and depreciation method are reviewed at the end of each reporting period and the effect of any changes in estimate is accounted for prospectively.*

*In F.Y.2019-20, effective 1 Jan 2020, the Company has reviewed the estimated economic useful lives of all components within the broad category of Leasehold improvements as specified in the above table and Electrical Equipments as specified in the above table of its property, plant and equipment, based on the combination of evaluation conducted by an independent consultants and management estimate.*

*Effective 1 Jan 2020, the Company has reviewed the estimated economic useful lives of all components within the broad category of Leasehold improvements and Electrical Equipments of its property, plant and equipment, based on the combination of evaluation conducted by an independent consultants and management estimate*

***Extract from Company 2***

*Changes in useful life*

*During the year ended March 31, 2021, the Company has reassessed useful life of certain categories of network assets due to technological developments and accordingly has revised the estimate of its useful life in respect of those assets. The impact of above change on the depreciation charge for the current and future years are as follows:*

| | ***For the year ending*** | | | | ***Future period till end of life*** |
|---|---|---|---|---|---|
| | ***March 31, 2021*** | ***March 31, 2022*** | ***March 31, 2023*** | ***March 31, 2024*** | |
| *Impact on depreciation charge* | *8,107* | *(730)* | *(2,353)* | *(2,820)* | *(2,204)* |

***Extract from Company 3***

*Indefinite-life intangible assets comprises of trademarks and brands, for which there is no foreseeable limit to the period over which they are expected to generate net cash inflows. These are considered to have an indefinite life, given the strength and durability of the brands and the level of marketing support.*

*Brands amounting to XX crore (31-Mar-20 XX crore) that have an indefinite life and are tested for impairment at every year end. Based on analysis of all relevant factors (brand establishment, stability, types of obsolescence etc.), there is no foreseeable limit to the period over which the assets are expected to generate net cash inflows for the Company.*

***Extract from Company 4***

*Brands/trademark with indefinite useful lives are also tested for impairment annually either individually or, if the intangible asset does not generate cash flows that are largely independent of those from other assets or groups of assets, as part of the cash-generating unit to which it belongs. Such intangibles are not amortised. The useful life of a brand with an indefinite life is reviewed annually to determine whether indefinite life assessment continues to be supportable. If not, the change in the useful life assessment from indefinite to finite is made on a prospective basis.*

*Brands of Rs. … Crores which has been categorised as brand with indefinite life and will be annually tested for impairment. Based on analysis of all relevant factors such as market share, stability, potential obsolescence, profitability, etc., the brand is expected to provide cash inflows to the Company over an indefinite period.*

## 3.10 Employee Benefits

### 3.10.1 Key Requirements

Under Ind AS 19, actuarial remeasurement gains and losses with respect to defined benefit plans such as, gratuity benefits, are recognised in other comprehensive income. Ind AS 19 requires discounting of defined benefit obligations based on yields on government bonds.

Defined employee benefit costs and obligations are dependent on assumptions used in calculating such amounts. These assumptions include salary increases, discount rates, health care cost trend rates, benefits earned, interest costs, expected return on plan assets, mortality rates and other factors. While we believe that the assumptions used are appropriate, differences in actual experience or changes in assumptions may affect our employee benefit costs and obligations.

### 3.10.2 Key Actuarial Estimates

- Salary increases
- Discount rates
- Health care cost trend rates
- Benefits earned
- Interest costs

- Expected return on plan assets
- Mortality rates

### 3.10.3 Key assumptions observed amongst sample companies

| Sector | Discount Rate | Salary Increase |
|---|---|---|
| Retail | 5.40% - 6.26% | 4.50% - 8.00% |
| Hospitality & Leisure | 6.80% - 7.95% | 8.00% - 9.00% |
| Infrastructure | 6.50% -7.00% | 8.50% |
| Automotive and Auto- Components | 6.10% - 6.90% | 5.75% - 10.00% |
| Power & Utilities | 6.50% - 6.75% | 5.00% - 7.00% |
| Non-Banking Financing Companies | 6.50% - 6.90% | 6.00% - 10.00% |
| Fast Moving Consumer Goods | 6.25% - 6.87% | 2.50%- 10.00% |
| Real Estate & Construction | 6.30% - 6.50% | 6.00% - 7.00% |
| Pharmaceuticals & Life Sciences | 6.50% - 6.75% | 7.00% - 7.50% |
| Technology & ITES | 6.65% - 6.85% | 6.00% - 7.00% |
| Extraction | 6.75% - 6.95% | 2.00% -15.00% |
| Telecommunication | 6.65% - 7.00% | 6.00% - 10.00% |
| Steel | 6.50% - 6.75% | 6.00% - 7.50% |

## 3.11 Share-Based Payment Arrangements

### 3.11.1 Key Requirements

Under Ind AS 102, subject to some very limited exceptions, share-based payment arrangements are measured using the fair value method. Under this approach, the share-based equity instrument is generally measured using option pricing models.

In practice, the Black-Scholes-Merton and Binomial models are two commonly used methods for estimating the fair value of share options. Share-based payment arrangements that include a market condition or the market value of the entity's equity in a performance condition, the valuation technique such as Monte Carlo Simulation are additionally used to estimate the likelihood that a market condition will be reached. Ind AS 102 requires that, the entity must at least use the following six inputs in whichever model is selected.

| Impact of increase in an input into a valuation method | | |
|---|---|---|
| | **Fair Value increase** | **Fair Value decrease** |
| Exercise price of the option | | ✓ |
| Expected life of the option | ✓ | |
| Expected volatility | ✓ | |
| Current equity share price | ✓ | |
| Expected dividend yield | | ✓ |
| Risk-free interest rate | ✓ | |

Determination of the exercise price of the option and the current equity share price is straight-forward and does not involve much management judgment. However, estimating the other four assumptions can be quite subjective.

Estimating the expected life of the option would involve evaluating factors such as, the vesting period, past history of the employee's exercise, the employee's organisational designation and the expected volatility.

Estimating the expected volatility would involve determination of the historical volatility over the same period as the expected life of the share option, long-term average volatility level and the length of time an entity's shares have been publicly traded.

Expected dividend yield would involve estimating the expectation for the entity's dividend policy, and whether an employee is entitled to dividends on the underlying shares while holding the share option. Determining the risk-free interest rate would entail estimating the implied yield currently available on zero-coupon government bonds denominated in the currency of the market in which the underlying shares primarily trade.

*Majority of our sample companies followed the Black-Scholes-Merton method for estimating the fair value of the share-based payment arrangements.*

## 3.12 Liquidity issues, Borrowings, Debt Covenants and Going Concern

### 3.12.1 Key Requirements

Financial statements are generally prepared using going concern assumption. An entity is no longer a going concern if management either intends to liquidate the entity or to cease trading or has no realistic alternative but to do so. If management has significant doubt of the entity's ability to continue as a going concern, the uncertainties should be disclosed. In case the financial statements are not prepared on a going concern basis, the entity should disclose the basis of preparation of financial statements and also the reason why the entity is not regarded as a going concern. Companies need to carefully assess the implications of the COVID relief packages provided by government and moratorium provided by banks for the purpose of going concern assessment.

Business uncertainties, particularly, in certain sectors such as, hospitality, aviation and real estate may lead to material uncertainties related to events or conditions that may cast significant doubt upon the entity's ability to continue as a going concern.

***Extract from Company 1***

*Some of the Company's loans are subjected to covenant clauses, whereby the Company is required to meet certain specified financial ratios. The Company has not met certain financial ratios for some of these arrangements, the gross outstanding amount for which as at March 31, 2020 was … Mn (March 31, 2019: … Mn). Waivers for loans of ` Nil (March 31, 2019: …. Mn) has been received as of reporting date. Accordingly … Mn (includes …. Mn reclassified as on March 31, 2019) has been re-classified from non-current borrowings to current maturities of long term debt (refer note 4(B)). The unamortised arrangement fees on such borrowings of … Mn (March 31, 2019: … Mn) has been charged in statement of profit and loss. As on the reporting date, none of the banks have approached for early repayment.*

*The Company has classified … Mn (includes … Mn reclassified as at March 31, 2019) from non-current borrowings to current maturities of long-term debt for not meeting certain covenant clauses under the financial agreements for specified financial ratios as at March 31, 2020 (refer note 21(b)). The Company had exchanged correspondences/ been in discussions with these lenders for the next steps/waivers. During the year, the credit rating of certain borrowings have been revised to BB-. As a result, certain lenders have asked for increase of interest rates, for which the Company is in discussion with such lenders. Further, guarantees amounting to … Mn are due to expire during the next twelve months. The above factors indicate that material uncertainty exists that cast significant doubt on the Company's ability to continue as a going concern and its ability to generate the cash flow that it needs to settle/refinance its liabilities and guarantees as they fall due. The Company's ability to continue as a going concern is essentially dependent on a positive outcome of the application before the Hon'ble Supreme Court for the payment in installments and successful negotiations with lenders. Pending the outcome of the above matters, these financial results have been prepared on a going concern basis.*

***Extract from Company 2***

*Going Concern - Negative working capital: As at the year end, the Company's current liabilities have exceeded its current assets by … crores primarily on account of current maturities of long term borrowings aggregating ` … crores and liability on derivative and other contracts aggregating … crores falling due within 12 months following the balance sheet date. Management is confident of its ability to generate adequate cash inflows from operations and also utilise long term funds available to meet its obligations on due date.*

*Impact of COVID-19: The Company is facing significant uncertainties due to COVID-19 which has impacted the operations of the Company adversely throughout the year. Management has assessed the impact of existing and anticipated effects of COVID-19* *on the future cash flow projections and has prepared a range of scenarios to estimate future financing requirements.*

*As on the reporting date, the Company has undrawn sanctioned lines of credit aggregating … crores which is estimated as sufficient to meet the estimated cash requirements during the next twelve months and the Company is current on all its Debt obligations. However as the COVID-19 situation still continues, as an abundant precaution, the Management is exploring means to secure additional financing to fulfil its long-term/ working capital requirements. Also refer note 2 (d) Estimation uncertainty relating to the global health pandemic on COVID-19.*

*Based on aforesaid assessment, management believes that as per estimates made conservatively, the Company will continue as a going concern and will be able to discharge its liabilities and realise the carrying amount of its assets as on March 31, 2021.*

***Extract from Company 3***

*The Group has assessed the ability of … Limited …, a subsidiary of the Company held through … to continue as going concern and meet its liquidity requirements. Given the improvement in outlook for European steel market, the directors of … observed that while there is a reasonable expectation that … has adequate resources to continue operating for the foreseeable future and that the going concern basis for the preparation of its financial statements remains appropriate, there exists a material uncertainty in respect of …. The financial statements of … are prepared on a going concern basis and do not include any adjustment regarding going concern of …. The Group has assessed its ability to meet any liquidity requirements at …, if required, and concluded that its cashflow and liquidity position remains strong. The net worth of …, an associate of the Company, has been fully eroded. The carrying value of the share of investment in the consolidated financial statements is Nil. The financial statements of … have been prepared on a going concern basis as it expects to generate cash flow from improvements in its operations, increased business from the Company, increased efficiencies in the project activities, proceeds from restructuring of its subsidiaries, facilities from banks as required and the Company is expected to provide the necessary financial support to …, if required, to meet its future obligations.*

## 3.13 Provisions and Contingent Liabilities

| Key Areas of Estimation | Ind AS Requirement | Key Estimates |
|---|---|---|
| Provision for Litigations | When an entity is involved in disputes, lawsuits, claims, anti-trust, governmental and / or regulatory inspections, inquiries, investigations and proceedings, including patent, tax and commercial matters in the ordinary course of business, Ind AS 37 is required to assess the probability, possibility or remoteness | Such claims may involve complex issues. An entity may need assistance from external legal counsel to assess the need to make provision or disclose a contingency on a case- to-case basis considering the underlying facts of each litigation. Legal and tax disputes can be complex and judgmental due to the difficulty in predicting the outcome of the |

| | | |
|---|---|---|
| | of the claim. If it is assessed that the claim is probable, the entity is required to provide for the estimated claim. | matter and estimating the potential impact if the outcome is unfavourable. |
| Decommissioning obligations | Ind AS 37 requires that the cost of dismantling or removal of the asset or restoration of the site to be included as part of the initial cost of the asset. A provision equivalent to the present value of such costs is recognised, with an equivalent amount capitalised as an additional cost component. Imputed interest would subsequently be recognised through the profit and loss account. Any changes in the obligation, other than that arising on efflux of time, are added or deducted from the cost of the asset and depreciated prospectively over balance useful life. | Estimating the cost of fulfilling the decommissioning obligation, the timing of the obligation and determining the appropriate discount rate may involve considerable judgement. |
| Warranty provisions | When an entity gives warranties on its products and services, undertaking to repair or replace the items that fail to perform satisfactorily during the warranty period, Ind AS 37 requires a provision to be made based on the estimated amount of the expected cost of meeting such obligations of rectification / replacement. | Estimating the cost of repair / replacement, the timing of the obligation and determining the appropriate discount rate may involve considerable judgement. |

***Extract from Company 1***

*Contingent liabilities (claims against the Company not acknowledged as debts)*

*Product and patent related matters*

*Matters relating to National Pharmaceutical Pricing Authority The Company manufactures and distributes … a formulations product, and in limited quantities, the active pharmaceutical ingredient …. Under the Drugs (Prices Control) Order (the “DPCO”), the National Pharmaceutical Pricing Authority (the “NPPA”) established by the Government of India had the authority to designate a pharmaceutical product as a “specified product” and the maximum selling price for such product. In 1995, the NPPA issued a notification and designated … as a “specified product” and fixed the maximum selling price. In 1996, the Company filed a statutory form III before the NPPA for the upward revision of the maximum selling price and a writ petition in the …. High Court* *(the "High Court") challenging the validity of the designation on the grounds that the applicable rules of the DPCO were not complied with while fixing the maximum selling price.*

*Although there can be no assurance regarding the outcome of any of the legal proceedings or investigations referred to in this Note, the Company does not expect them to have a materially adverse effect on its financial position, as it believes that the likelihood of loss in excess of amounts accrued (if any) is not probable. However, if one or more of such proceedings were to result in judgements against the Company, such judgements could be material to its results of operations in a given period.*

***Extract from Company 2***

*Product warranties: The Company gives warranties on certain products and services, undertaking to repair or replace the items that fail to perform satisfactorily during the warranty period. Provision made as at March 31, 2021 represents the amount of the expected cost of meeting such obligations of rectification/replacement. The timing of the outflows is expected to be within a period of 1 to 3 years from the date of Balance Sheet.*

*Expected tax liability in respect of indirect taxes represents mainly the differential sales tax liability on account of non-collection of declaration forms.*

*Provision for litigation-related obligations represents liabilities that are expected to materialise in respect of matters in appeal.*

*Contractual rectification cost represents the estimated cost the Company is likely to incur during defect liability period as per the contract obligations in respect of completed construction contracts accounted under Ind AS 115 "Revenue from Contracts with customers".*

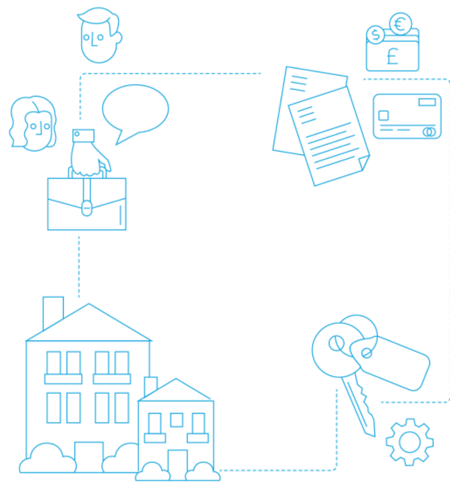
***Extract from Company 3***

*Warranty and product liability expenses represented 3.0% and 4.2% of our total revenues in FY 2020-21 and FY 2019- 20, respectively. The warranty expenses at Jaguar Land Rover decreased to GB£706 million (3.6% of the revenue) in FY 2020- 21, compared to GB£1,131 million (4.9% of revenue) in FY 2019- 20, mainly due to increased retailer guidance, guided diagnostics enhancement, proactive issue detection, prioritisation and resolution coming from charge+ initiatives, significant quality improvements in vehicles and the implementation of other business enhancement activities. For Tata Motors' Indian operations, these represent 0.9% and 1.2% of the revenue for FY 2020-21 and FY 2019-20, respectively, due to quality improvements and product mix.*

*Vehicle warranties are provided for a specified period of time. Our vehicle warranty obligations vary depending upon the type of the product, geographical location of its sale and other factors. The estimated liability for vehicle warranties is recorded when the products are sold or when new warranty programs are initiated. These estimates are established using historical information on the nature, frequency and average cost of warranty claims and management estimates regarding possible future warranty claims, customer goodwill and recall complains. The timing of outflows will vary depending on when warranty claim will arise, being typically up to six years and for batteries in Electric Vehicles warranty period is typically up to eight years. We also have back-to-back* *contractual arrangements with our suppliers in the event that a vehicle fault is proven to be a supplier's fault. Estimates are made of the expected reimbursement claims based upon historical levels of recoveries from supplier, adjusted for inflation and applied to the population of vehicles under warranty as on balance sheet date. Estimated supplier reimbursements are recognized as separate asset. Actual claims incurred in the future may differ from our original estimates, which may materially affect warranty expenses.*

## 3.14 Fair Valuation of Investment Properties

### 3.14.1 Key Requirements



Under Ind AS 40, investment properties comprise of land or building held for earning rentals or for capital appreciation or both. Land and building used in the production or supply of goods or services, or for administrative purposes is classified as property, plant and equipment and not investment property. Investment properties are measured at cost less depreciation and impairment, if any. Ind AS 40 requires the fair value of the investment properties to be disclosed in the annual financial statements.

| Incremental Fair Value as a percentage of Net Book Value | Fair Valuation Basis (Relevant Extracts from Financial Statements) |
|---|---|
| 62% | *Fair value of investment property as at March 31, 2021 is Rs.5918.31 crore. The fair values of investment property have been determined by internal architectural department or independent valuer, as appropriate. Fair value of property that are evaluated by independent valuers amounted to Rs.1616.64 crore. Valuation is based on government rates, market research, market trend and comparable values as considered appropriate.* |
| 129% | *The fair value of the investment property is Rs.861.00 crores, which has been determined on the basis of valuation carried out at the reporting date by independent valuer. The fair value measurement for investment property has been categorised as Level 2 based on the valuation techniques used and inputs applied. The main inputs considered by the valuer are government rates, property location, market research, market trend, contracted rentals, terminal yields, discount rates and comparable values, as appropriate.* |

| | |
|---|---|
| 4500% | *The Company obtains Independent Valuations of its investment property. The fair value of the investment property have been derived using the Direct Comparison Method. The direct comparison approach involves a comparison of the investment property to similar properties that have actually been sold in arms-length distance from investment property or are offered for sale in the same region. This approach demonstrates what buyers have historically been willing to pay (and sellers willing to accept) for similar properties in an open and competitive market, and is particularly useful in estimating the value of the land and properties that are typically traded on a unit basis. This approach leads to a reasonable estimation of the prevailing price. Given that the comparable instances are located in close proximity to the investment property; these instances have been assessed for their locational comparative advantages and disadvantages while arriving at the indicative price assessment for investment property.* |
| 48200% | *The valuation of investment properties is in accordance with the Ready Reckoner rates prescribed for the purpose of levying stamp duty. The Company has referred to the publications and government website for Ready Reckoner rates. Further, the fair value of certain investment property has been determined with the help of Independent valuer.* |
| 153% | *The fair value of investment property has been determined by external independent property valuers, having appropriate recognised professional qualification and recent experience in the location and category of the property being valued. The fair value measurement for all of the investment property has been categorised as a level 3 fair value based on the inputs to the valuation techniques used. The Company obtains independent valuations of its investment property after every three years. The fair value of the investment property have been derived using the Direct Comparison Method. The direct comparison approach involves a comparison of the investment property to similar properties that have actually been sold in arms-length distance from investment property or are offered for sale in the same region. This approach demonstrates what buyers have historically been willing to pay (and sellers willing to accept) for similar properties in an open and competitive market, and is particularly useful in estimating the value of the land and properties that are typically traded on a unit basis. This approach leads to a reasonable estimation of the prevailing price. Given that the comparable instances are located in close proximity to the investment property; these instances have been assessed for their locational comparative advantages and disadvantages while arriving at the indicative price assessment for investment property.* |

# Chapter 4: Key Valuation and Estimation Disclosures

## 4.1 Estimation Uncertainties and Management Judgement

4.1.1 Ind AS 1 requires following disclosures for key estimation uncertainties and management judgement:

Ind AS 1 paragraph 122 requires disclosure of the management judgements made in the process of applying the entity's accounting policies having the most significant impact on the amounts recognized in the financial statements.

Ind AS 1 paragraph 125 requires disclosure of financial information relating to the assumptions made about the future estimates and other significant sources of estimation uncertainties at the balance sheet date that have a significant risk of resulting in a material adjustment to the carrying amounts of assets and liabilities within the next financial year. Specifically, the disclosure about the nature and carrying amount at the end of the reporting period is required.

## 4.2 Fair Valuation

4.2.1 Ind AS 113 paragraph 91 requires disclosure information that helps users of its financial statements assess the following:

- for assets and liabilities that are measured at fair value on a recurring or non-recurring basis in the statement of financial position after initial recognition, the valuation techniques and inputs used to develop those measurements
- for fair value measurements using significant unobservable inputs (Level 3), the effect of the measurements on profit or loss or other comprehensive income for the period.

4.2.2 Ind AS 113 differentiates the extent of disclosures depending on whether the measurements are recurring or non-recurring.

- Recurring fair value measurements – fair value measurements required or permitted by other IFRSs to be recognised in the statement of financial position at the end of each reporting period
- Non-recurring fair value measurements are fair value measurements that are required or permitted by other IFRSs to be measured in the statement of financial position in particular circumstances.

4.2.3 Ind AS 113 paragraph 93 requires following minimum disclosures are required for each class of assets and liabilities measured at fair value in the balance sheet after initial recognition:

- the fair value measurement at the end of the reporting period

- for non-recurring fair value measurements, the reasons for the measurement
- level of the fair value hierarchy within which the fair value measurements are categorized in their entirety (i.e. Level 1, 2 or 3)
- for assets and liabilities held at the reporting date that are measured at fair value on a recurring basis, the amounts of any transfers between Level 1 and Level 2 of the fair value hierarchy, the reasons for those transfers and the entity's policy for determining when transfers between levels are deemed to have occurred, separately disclosing and discussing transfers into and out of each level
- for Level 2 and Level 3 fair value measurements, a description of the valuation technique and the inputs used in the fair value measurement, any change in the valuation techniques and the reason for making such change (there are certain exceptions)
- for Level 3 fair value measurements, the quantitative information about the significant unobservable inputs used in the fair value measurement (with some exceptions)
- total gains or losses for the period recognised in other comprehensive income, and the line items in other comprehensive income in which those gains or losses are recognized
- purchases, sales, issues and settlements (each of those types of changes disclosed separately)
- the amounts of any transfers into or out of Level 3 of the fair value hierarchy, the reasons for those transfers and the entity's policy for determining when transfers between levels are deemed to have occurred. Transfers into Level 3 shall be disclosed and discussed separately from transfers out of Level 3
- for Level 3 fair value measurements, a description of the valuation processes used by the entity
- for Level 3 recurring fair value measurements, a description of the sensitivity of the fair value measurement to changes in unobservable inputs if a change in those inputs to a different amount might result in a significantly higher or lower fair value measurement
- for financial assets and financial liabilities, if changing one or more of the unobservable inputs to reflect reasonably possible alternative assumptions would

change fair value significantly, an entity shall state that fact and disclose the effect of those changes

- if the highest and best use of a non-financial asset differs from its current use, disclosure of that fact and why the non-financial asset is being used in a manner that differs from its highest and best use

4.2.4 Ind AS 113 paragraph 99 states that quantitative disclosures are required to be presented in a tabular format unless another format is more appropriate.

# RSM India


**Mumbai**
8th Floor, Bakhtawar
229, Nariman Point
Mumbai – 400 021

3rd Floor, A Wing,
Technopolis Knowledge Park
Mahakali Caves Road, Andheri (E)
Mumbai – 400 093

201, Shree Padmini
Rajashree Sahu Marg
Teli Galli Junction
Andheri (E), Mumbai 400 069

**New Delhi – NCR**
2nd Floor, Tower – B
B-37, Sector – 1, Noida
New Delhi – NCR – 201 301

**Chennai**
Apex Towers, 2nd Floor, No.54
II Main Road, R. A. Puram
Chennai – 600 028

1A, Chamiers Apartments
62/121, Chamiers Road
R. A. Puram, Chennai – 600 028

**Kolkata**
A-6, 12th Floor
Chatterjee International Centre
33A, Jawaharlal Nehru Road
Kolkata – 700 071

**Bengaluru**
3rd Floor, B Wing
Jubilee Building, 45, Museum
Road, Bengaluru – 560 025

**Surat**
DTA-2, G-02 to G-05 Plot
Gujarat Hira Bourse
Ichhapore-2
Surat – 394 510

T-720, Belgium Tower
Opp. Linear Bus Stop
Ring Road, Surat – 395 002

B/604-605, Tirupati Plaza
Athwa Gate, Nanpura
Surat – 395 001

**Hyderabad**
217, Maruthi Corporate Point
Swapnalok Complex
92, Sarojini Devi Road
Secunderabad – 500 003

**Ahmedabad**
B/708, Mondeal Heights
Near Novotel Hotel
Opp. Karnavati Club, S.G.Highway
Ahmedabad – 380 015

**Pune**
102, 1st Floor
Shree Residency
Baner Balewadi Road
Balewadi, Pune – 411 045

**Gandhidham**
206, Sunshine Arcade II
Plot No. 37, Sector 8
Near D-Mart
Gandhidham – 370 201

**Jaipur**
346, 3rd Floor
Ganpati Plaza, M.I. Road
Jaipur – 302 001

For further information please contact:

RSM Astute Consulting Pvt. Ltd. |

8th Floor, Bakhtawar, 229, Nariman Point, Mumbai - 400021.

T: (91-22) 6108 5555/ 6121 4444
F: (91-22) 6108 5556/ 2287 5771

**E:** emails@rsmindia.in

**W:** www.rsmindia.in

Offices: Mumbai, New Delhi - NCR, Chennai, Kolkata, Bengaluru, Surat, Hyderabad, Ahmedabad, Pune, Gandhidham, and Jaipur.

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This Research Report provides a brief overview of fair valuation and accounting estimates under Ind AS. The Report is prepared for general use and our views as stated above would be required to be revalidated vis-à-vis the facts of each case. It may be noted that nothing contained in this Research report should be regarded as our opinion and facts of each case will need to be analyzed to ascertain applicability or otherwise of the said notification and appropriate professional advice should be sought for applicability of legal provisions based on specific facts. We are not responsible for any liability arising from any statements or errors contained in this Report.

24 September 2021