UNIT 7:
INVESTMENT IN ASSOCIATES & JOINT VENTURES

7.1 INTRODUCTION

Ind AS 28, Investments in Associates and Joint Ventures,
a) prescribes the accounting for investments in associates and
b) sets out the requirements for the application of the equity method when accounting for
investments in associates and joint ventures.

It is important to note here that Ind AS 111, describes joint arrangements including joint ventures
and prescribes equity method for joint ventures. But here, in Ind AS 28, the equity method is
described for both Associate and Joint Ventures.

7.2 SCOPE

This Standard shall be applied by all entities that are investors with joint control of, or significant
influence over, an investee.

7.3 SIGNIFICANT INFLUENCE

The concept of 'significant influence' signifies the close relationship between two entities where one
has the power to influence the decision making in the other entity. In today's business world, many
companies do not have actual control over other companies but hold significant ownership to influence
the decision making in such companies. Many such investments are in the form of joint ventures in
which two or more companies form a new entity to carry out a specified operating purpose.

For example, Microsoft and NBC formed MSNBC, a cable channel and online site to go with
NBC’s broadcast network. Each partner owns 50 percent of the joint venture. For each of these
investments, the investors do not possess absolute control because they hold less than a
majority of the voting stock. Thus, the preparation of consolidated financial statements is
inappropriate. However, the large percentage of ownership indicates that each investor
possesses some ability to affect the investee’s decision-making process.

Definition

Significant influence is the power to participate in the financial and operating policy decisions of
the investee but is not control or joint control of those policies.

Analysis

✓ HOLDING 20% OR MORE OF THE VOTING RIGHTS: If an entity holds, directly or indirectly
(eg through subsidiaries), 20 per cent or more of the voting power of the investee, it is
presumed that the entity has significant influence, unless it can be clearly demonstrated that this is not the case.

- **HOLDING LESS THAN 20% OF VOTING RIGHTS:** Also, in cases where the entity holds, directly or indirectly (eg through subsidiaries), less than 20 per cent of the voting power of the investee, it is presumed that the entity does not have significant influence, unless such influence can be clearly demonstrated.

**Illustration 1**

X Ltd. owns 20% of the voting rights in Y Ltd. and is entitled to appoint one director to the board, which consist of five members. The remaining 80% of the voting rights are held by two entities, each of which is entitled to appoint two directors.

A quorum of four directors and a majority of those present are required to make decisions. The other shareholders frequently call board meeting at the short notice and make decisions in the absence of X Ltd’s representative. X Ltd has requested financial information from Y Ltd, but this information has not been provided. X Ltd’s representative has attended board meetings, but suggestions for items to be included on the agenda have been ignored and the other directors oppose any suggestions made by X Ltd. Is Y Ltd an associate of X Ltd?

**Solution**

Despite the fact that the X Ltd owns 20% of the voting rights and has representations on the board, the existence of other shareholders holding a significant proportion of the voting rights prevent X Ltd. from exerting significant influence. Whilst it appears the X Ltd should have the power to participate in the financial and operating policy decision, the other shareholders prevent X Ltd’s efforts and stop X Ltd from actually having any influence.

In this situation, Y Ltd would not be an associate of X Ltd.

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Whether an investor has significant influence over the investee is a matter of judgment based on the nature of the relationship between the investor and the investee. Existence of significant influence may be judged by the following factors:

a) **Representation on the board of directors or equivalent governing body of the investee;**

**Illustration 2**

Kuku Ltd. holds 12% of the voting shares in Boho Ltd. Boho Ltd.‘s board comprise of eight members and two of these members are appointed by Kuku Ltd. Each board member has one vote at meeting. Is Boho Ltd an associate of Kuku Ltd?

**Solution**

Boho Ltd is an associate of Kuku Ltd as significant influence is demonstrated by the presence of directors on the board and the relative voting rights at meetings.

It is presumed that entity has significant influence where it holds 20% or more of the voting power of the investee, but it is not necessary to have 20% representation on the board to
demonstrate significant influence, as this will depend on all the facts and circumstances. One board member may represent significant influence even if that board member has less than 20% of the voting power. But for significant influence to exist it would be necessary to show based on specific facts and circumstances that this is the case, as significant influence would not be presumed.

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b) Participation in policy-making processes, including participation in decisions about dividends or other distributions;

Example:
X Ltd creates a separate legal entity in which it holds less than 20% of the voting interests but however controls that entity through contracts that ensures that decision-making power and the distribution of profits and losses lies with X Ltd. In such cases the investor is able to exercise significant influence over its investee.

Example:
Info Ltd owns 9% equity in Sync Ltd. However, it has the approval or veto rights over critical decisions of compensation, hiring, termination, and other operating and capital spending decisions of Sync Ltd. The non-controlling rights are so restrictive that it is appropriate to infer that control rests with the Info Ltd for all major decisions.

c) Material transactions between the entity and its investee;

Illustration 3
Q Ltd manufactures shoes for a leading retailer P Ltd. P Ltd provides all designs for the shoes and participates in scheduling, timing and quantity of the production. The majority (i.e. 90%) of Q Ltd.’s sales are made to the retailer, P Ltd. P Ltd. has 10% shareholding in the Q Ltd. It acquired this interest many years ago at the start of their relationship. Does significant influence exist?

Solution
Q Ltd is highly dependent on the retailer for the continued existence of the business. Despite having only a 10% interest in Q Ltd, P Ltd has significant influence

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Illustration 4
X Ltd owns 15% of the voting rights of Y Ltd., and the remainder are widely dispersed among the public.

X Ltd also is the only supplier of crucial raw materials to Y Ltd., further it provides certain expertise guidance regarding the maintenance of Y Ltd.’s factory.

Discuss the relationship between X Ltd. and Y Ltd.
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Solution

Y Ltd. is effectively functioning because of the participation of X Ltd. in the Y Ltd.'s factory despite having 15% interest in Y Ltd., X Ltd. has significant influence.

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d) Interchange of managerial personnel; or

Illustration 5

Entity X and entity Y, operate in the same industry, but in different geographical regions. Entity X acquires a 10% shareholding in entity Y as a part of a strategic agreement. A new production process is key to serve a fundamental change in the strategic direction of entity Y. The terms of agreement provide for entity Y to start a new production process under the supervision of two managers from entity X. The managers seconded from entity X, one of whom is on entity X's board, will oversee the selection and recruitment of new staff, the purchase of new equipment, the training of the workforce and the negotiation of new purchase contracts for raw materials. The two managers will report directly to entity Y's board as well as to entity X's. Analyse.

Solution

The secondment of the board member and a senior manager from entity X to entity Y gives entity X, a range of power over a new production process and may evidence that entity X has significant influence over entity Y. This assessment takes into the account what are the key financial and operating policies of entity Y and the influence this gives entity X over those policies.

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e) Provision of essential technical information.

Illustration 6

Soul Ltd has 18% interest in God Ltd. Soul Ltd manufacture mobile telephone handsets using technology developed by God Ltd. God Ltd licenses the technology to Soul Ltd and updates the license agreement for new technology on a regular basis. The handsets are sold by Soul Ltd and represent substantially Soul Ltd's entire sale. Analyse.

Solution

Soul Ltd is dependent on the technology that God Ltd supplies since a high proportion of Soul Ltd’s sales are based on that technology. Therefore, Soul Ltd is likely to be an associate of God Ltd because of the provision of essential technical information.

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7.4 POTENTIAL VOTING RIGHTS

An investor may hold any instrument (such as share warrants, share call options, debt or equity instruments) issued by an associate and terms of the instrument is that a holder will get an equity
rights on the expiry of the term i.e. they are convertible into ordinary shares, to give the entity additional voting power or to reduce another party's voting power over the financial and operating policies of another entity (ie potential voting rights). Only an existing right will be considered for determining the Significant influence. Any potential voting rights that will arise in future will not be considered while determining Significant influence.

It is worth noting that a substantial or majority ownership by another investor does not necessarily preclude an entity from having significant influence

### 7.5 EQUITY METHOD

**a) On the date of acquisition:**

Under the equity method, on initial recognition the investment in an associate or a joint venture is recognised at cost.

<table>
<thead>
<tr>
<th>Investment in Associate A/c</th>
<th>Dr.</th>
</tr>
</thead>
<tbody>
<tr>
<td>To Cash A/c</td>
<td></td>
</tr>
</tbody>
</table>

**b) Recognizing the share in Profit or loss:**

Since the investor has the significant influence over the investee, the investor has an interest in the performance of the investee. It can influence the dividend to be distributed irrespective of the actual profits made by the investee. Here the recognition of income based on profit distributed may not be a true measure of the income earned by an investor on an investment in an associate or a joint venture. The distributions made may bear little relation to the actual performance of the associate or joint venture. Hence recognizing actual profit or loss (irrespective of the amount of dividend distributed) is more reflective of the actual value of the investment.
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(i) If Associate or joint venture makes profit

<table>
<thead>
<tr>
<th>Investment in Associate A/c</th>
<th>Dr.</th>
</tr>
</thead>
<tbody>
<tr>
<td>To Share in Profit from Associate A/c</td>
<td></td>
</tr>
</tbody>
</table>

(ii) If Associate or joint venture makes losses

<table>
<thead>
<tr>
<th>Share in Losses from Associate A/c</th>
<th>Dr.</th>
</tr>
</thead>
<tbody>
<tr>
<td>To Investment in Associate A/c</td>
<td></td>
</tr>
</tbody>
</table>

(iii) Cash dividend received: Any distribution of dividend in the form of cash received from the associate reduces the carrying amount of the investment.

<table>
<thead>
<tr>
<th>Cash A/c</th>
<th>Dr.</th>
</tr>
</thead>
<tbody>
<tr>
<td>To Investment in Associate A/c</td>
<td></td>
</tr>
</tbody>
</table>

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### Application of Equity Method

<table>
<thead>
<tr>
<th>Investee Event</th>
<th>Books of Investor</th>
</tr>
</thead>
<tbody>
<tr>
<td>Income earned</td>
<td>Proportionate share of income is recognized by investor</td>
</tr>
<tr>
<td>Dividends distributed</td>
<td>Investor’s share in dividends reduces the investment account</td>
</tr>
</tbody>
</table>

### Illustration 7

*Amar Ltd. acquires 40% shares of Ram Ltd. On 1 April, 20X1, the price paid is ₹10,00,000. Ram Ltd has reported a profit of ₹2,00,000 and paid dividend of ₹1,00,000. Calculate Carrying Amount of Investment as per Equity Method?*

#### Solution

<p>| | |</p>
<table>
<thead>
<tr>
<th></th>
<th></th>
</tr>
</thead>
<tbody>
<tr>
<td>Cost</td>
<td>10,00,000</td>
</tr>
<tr>
<td>Add: Share in Post-Acquisition Profits (2,00,000 x 40%)</td>
<td>80,000</td>
</tr>
<tr>
<td>Less: Distribution of Dividend (1,00,000 x 40%)</td>
<td>(40,000)</td>
</tr>
<tr>
<td><strong>Total</strong></td>
<td><strong>10,40,000</strong></td>
</tr>
</tbody>
</table>

Adjustments to the carrying amount may also be necessary for a change in the investor’s proportionate interest in the investee arising from changes in the investee’s other comprehensive income. Such changes include those arising from the revaluation of property, plant and equipment and from foreign exchange translation differences. The investor’s share of those changes is recognised in other comprehensive income of the investor.

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7.6 APPLICATION OF EQUITY METHOD

The investor needs to apply equity method of accounting when it has joint control or significant influence over the investee.

The rationale behind the application of the equity method is that in case of an associate or a joint venture, an investor commences to gain the ability to influence the decision-making process of an investee as the level of ownership rises. The investor, hence, has the ability to exercise significant influence over operating and financial policies of an investee even though the investor holds 50 percent or less of the voting rights. Clearly, this is a subject of judgments and interpretations in practice. Also, it is important to note that ‘significant influence’ is required to be present but there is no requirement that any actual influence must have ever been applied.

However, the investor is exempt from the application of Equity Method under certain circumstances.

7.6.1 Exemptions from applying the equity method

An entity need not apply the equity method to its investment in an associate or a joint venture if the entity is a parent that is exempt from preparing consolidated financial statements by the scope exception in paragraph 4(a) of Ind AS 110 or if all the following apply:

(a) The entity is a wholly-owned subsidiary, or is a partially-owned subsidiary of another entity and its other owners, including those not otherwise entitled to vote, have been informed about, and do not object to, the entity not applying the equity method.

(b) The entity’s debt or equity instruments are not traded in a public market (a domestic or foreign stock exchange or an over-the-counter market, including local and regional markets).

(c) The entity did not file, nor is it in the process of filing, its financial statements with a securities commission or other regulatory organisation, for the purpose of issuing any class of instruments in a public market.

(d) The ultimate or any intermediate parent of the entity produces consolidated financial statements available for public use that comply with Ind AS.

When an investment in an associate or a joint venture is held by, or is held indirectly through, an entity that is a venture capital organisation, or a mutual fund, unit trust and similar entities including investment-linked insurance funds, the entity may elect to measure investments in those associates and joint ventures at fair value through profit or loss in accordance with Ind AS 109.

When an entity has an investment in an associate, a portion of which is held indirectly through a venture capital organisation, or a mutual fund, unit trust and similar entities including investment-linked insurance funds, the entity may elect to measure that portion of the investment in the associate at fair value through profit or loss in accordance with Ind AS 109 regardless of whether
the venture capital organisation has significant influence over that portion of the investment. If the entity makes that election, the entity shall apply the equity method to any remaining portion of its investment in an associate that is not held through a venture capital organisation.

An entity’s net investment in associate or joint venture includes investment in ordinary shares, other interests that are accounted using the equity method, and other long-term interests, such as preference shares and long-term receivables or loans, the settlement of which is neither planned nor likely to occur in the foreseeable future. These long-term interests are not accounted for in accordance with Ind AS 28, instead they are governed by the principles of Ind AS 109.

As per para 10 of Ind AS 28, the carrying amount of entity’s investment in its associate and joint venture increases or decreases (as per equity method) to recognise the entity’s share of profit or loss of its investee associate and joint venture.

Para 38 of Ind AS 38 further states that the losses that exceed the entity’s investment in ordinary shares are applied to other components of the entity’s interest in the associate or joint venture in the reverse order of their superiority.

In this context, the amendments to Ind AS 28 clarify that the accounting for losses allocated to long-term interests would involve the dual application of Ind AS 28 and Ind AS 109. The annual sequence in which both standards are to be applied can be explained in a three-step process:

**Step 1: Apply Ind AS 109 independently**

Apply Ind AS 109 (such as impairment, fair value adjustments etc.) ignoring any adjustments to carrying amount of long-term interests under Ind AS 28 (such as allocation of losses, impairment etc.)

**Step 2: True-up past allocations**

If necessary, prior years’ Ind AS 28 loss allocation is trued up in the current year, because Ind AS 109 carrying value may have changed. This may involve recognizing more prior year’s losses, reversing these losses or re-allocating them between different long-term interests.

**Step 3: Book current year equity share**

Any current year Ind AS 28 losses are allocated to the extent that the remaining long-term interest balance allows. Any current year Ind AS 28 profits reverse any unrecognized prior years’ losses and then allocations are made against long-term interests.
7.6.2 Discontinuing of equity Method

The investor should discontinue the use of Equity Method from the date the significant influence or joint control ceases.

7.6.3 Equity method procedures

While preparing the consolidated financial statements, an investor applies equity method of accounting for investments in associates and joint ventures. It includes the aggregate of the holdings in that associate or joint venture by the parent and its subsidiaries taken together. The holdings of the group’s other associates or joint ventures are ignored for this purpose.

When an associate or a joint venture has subsidiaries, associates or joint ventures, the profit or loss, other comprehensive income and net assets taken into account in applying the equity method are those recognised in the associate’s or joint venture’s financial statements (including the associate’s or joint venture’s share of the profit or loss, other comprehensive income and net assets of its associates and joint ventures), after any adjustments necessary to give effect to uniform accounting policies.

In accounting, transactions between related companies are identified as either downstream or upstream. Downstream transfers include investor’s sale of an item to investee. Conversely, a downstream transfer means sales made by investee to investor. These two types of intra-entity transactions are examined separately.

Gains and losses resulting from ‘upstream’ and ‘downstream’ transactions between an entity (including its consolidated subsidiaries) and its associate or joint venture are recognised in the entity’s financial statements only to the extent of unrelated investors’ interests in the associate or joint venture. The investor’s share in the associate’s or joint venture’s gains or losses resulting from these transactions is eliminated.

Example:

Assume that Babu Ltd owns a 40% share of Sahu Ltd and accounts for this investment through the equity method. In 20X1, Babu Ltd sells inventory to Sahu Ltd at a price of 50,000. This figure includes a gross profit of 30%.

By the end of 20X1, Sahu Ltd has sold 40,000 of these goods to outside parties while retaining 10,000 in inventory for sale during the subsequent year.

The investor has made downstream sales to the investee. In applying the equity method, recognition of the related profit must be delayed until the buyer disposes of these goods.

Although total intra-entity transfers amounted to 50,000, only 40,000 of this merchandise has already been resold to outsiders, thereby justifying the normal reporting of profits.

For the 10,000 still in the investee’s inventory, the earning process is not finished. In computing equity income, this portion of the intra-entity profit must be deferred until Sahu Ltd. disposes of the goods.

The gross profit on the original sale was 30% of the transfer price; therefore, Sahu Ltd.’s profit associated with these remaining items is 3,000 (10,000 * 30%). However, because only 40%
of the investee’s stock is held by Babu Ltd., just 1,200 (3,000 * 40%) of this profit is unearned. Babu Ltd’s ownership percentage reflects the intra-entity portion of the profit. The total 3,000 gross profit within the ending inventory balance is not the amount deferred. Rather, 40% of that gross profit is viewed as the currently unrealized figure.

After calculating the appropriate deferral, the investor decreases current equity income by 1,200 to reflect the unearned portion of the intra-entity profit. This procedure temporarily removes this portion of the profit from the investor’s books in 20X1 until the investee disposes of the inventory in 20X2.

In the subsequent year, when this inventory is eventually consumed by Sahu Ltd. or sold to unrelated parties, the deferral is no longer needed. The earning process is complete, and Babu Ltd. should recognize the 1,200.

**Example: Equity method accounting**

B Ltd acquired a 30% interest in D Ltd and achieved significant influence. The cost of the investment was ₹ 2,50,000. The associate has net assets of ₹ 5,00,000 at the date of acquisition. The fair value of those net assets is ₹ 6,00,000 as a fair value of property, plant & equipment is ₹ 1,00,000 higher than its book value. This property, plant & equipment has a remaining useful life of 10 years.

After acquisition D Ltd recognize profit after tax of ₹ 1,00,000 and paid a dividend out of these profits of ₹ 9,000. D Ltd has also recognized exchange losses of ₹ 20,000 directly in other comprehensive income.

B Ltd’s interest in D Ltd at the end the year is calculated as follows:

<table>
<thead>
<tr>
<th>Description</th>
<th>Amount (₹)</th>
</tr>
</thead>
<tbody>
<tr>
<td>Balance on requisition under the equity method (including goodwill of ₹ 70,000)</td>
<td>2,50,000</td>
</tr>
<tr>
<td>B Ltd’s share of D Ltd’s after tax profit (30% x ₹1,00,000)</td>
<td>30,000</td>
</tr>
<tr>
<td>Elimination of dividend received by B Ltd from D Ltd (30% x ₹9,000)</td>
<td>(2,700)</td>
</tr>
<tr>
<td>B Ltd’s share of D Ltd’s exchange differences (30% x ₹20,000)</td>
<td>(6,000)</td>
</tr>
<tr>
<td>B Ltd’s share of amortisation of fair value uplift (30% x ₹10,000)</td>
<td>(3,000)</td>
</tr>
<tr>
<td>B Ltd’s interest in D Ltd at the end of the year under the equity method</td>
<td>2,68,300</td>
</tr>
<tr>
<td>(including goodwill)</td>
<td></td>
</tr>
<tr>
<td>D Ltd has net assets at the end of the year of ₹ 5,71,000 (that is, net assets at the start of the year of ₹ 5,00,000, plus profit during the year of ₹ 1,00,000, less dividend of ₹ 9,000, less foreign exchange losses of ₹ 20,000).</td>
<td></td>
</tr>
<tr>
<td>B Ltd’s interest in D Ltd at the end of the year is made up of:</td>
<td></td>
</tr>
<tr>
<td>B Ltd’s share of D Ltd.’s net assets (30% x ₹ 5,71,000)</td>
<td>1,71,300</td>
</tr>
<tr>
<td>Goodwill</td>
<td>70,000</td>
</tr>
<tr>
<td>B Ltd’s share of D Ltd’s fair value adjustments (the initial fair value</td>
<td></td>
</tr>
</tbody>
</table>
**Illustration 8**

Entity A holds a 20% equity interest in Entity B (an associate) that in turn has a 100% equity interest in Entity C. Entity B recognised net assets relating to Entity C of ₹1,000 in its consolidated financial statements. Entity B sells 20% of its interest in Entity C to a third party (a non-controlling shareholder) for ₹300 and recognises this transaction as an equity transaction in accordance with paragraph 23 of Ind AS 110, resulting in a credit in Entity B’s equity of ₹100.

The financial statements of Entity A and Entity B are summarised as follows before and after the transaction:

### Before

<table>
<thead>
<tr>
<th></th>
<th>₹</th>
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<th>₹</th>
</tr>
</thead>
<tbody>
<tr>
<td><strong>A’s consolidated financial statements</strong></td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>Assets</td>
<td></td>
<td>₹Liabilities</td>
<td></td>
</tr>
<tr>
<td>Investment in B</td>
<td>200</td>
<td>Equity</td>
<td>200</td>
</tr>
<tr>
<td>Total</td>
<td>200</td>
<td>Total</td>
<td>200</td>
</tr>
</tbody>
</table>

<table>
<thead>
<tr>
<th></th>
<th>₹</th>
<th></th>
<th>₹</th>
</tr>
</thead>
<tbody>
<tr>
<td><strong>B’s consolidated financial statements</strong></td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>Assets</td>
<td></td>
<td>₹Liabilities</td>
<td></td>
</tr>
<tr>
<td>Assets (from C)</td>
<td>1000</td>
<td>Equity</td>
<td>1000</td>
</tr>
<tr>
<td>Total</td>
<td>1000</td>
<td>Total</td>
<td>1000</td>
</tr>
</tbody>
</table>

The financial statements of B after the transaction are summarised below:

### After

<table>
<thead>
<tr>
<th></th>
<th>₹</th>
<th></th>
<th>₹</th>
</tr>
</thead>
<tbody>
<tr>
<td><strong>B’s consolidated financial statements</strong></td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>Assets</td>
<td></td>
<td>₹Liabilities</td>
<td></td>
</tr>
<tr>
<td>Assets (from C)</td>
<td>1000</td>
<td>Equity</td>
<td>1000</td>
</tr>
<tr>
<td>Cash</td>
<td>300</td>
<td>Equity transaction with non-controlling interest</td>
<td>100</td>
</tr>
<tr>
<td></td>
<td></td>
<td>Equity attributable to owners</td>
<td>1100</td>
</tr>
<tr>
<td></td>
<td></td>
<td>Non-controlling interest</td>
<td>200</td>
</tr>
<tr>
<td>Total</td>
<td>1300</td>
<td>Total</td>
<td>1300</td>
</tr>
</tbody>
</table>
Although Entity A did not participate in the transaction, Entity A’s share of net assets in Entity B increased as a result of the sale of B's 20% interest in C. Effectively, A’s share in B’s net assets is now ₹220 (20% of ₹1,100) i.e., ₹20 in addition to its previous share.

How is an equity transaction that is recognised in the financial statements of Entity B reflected in the consolidated financial statements of Entity A that uses the equity method to account for its investment in Entity B?

**Solution**

Ind AS 28 defines the equity method as “a method of accounting whereby the investment is initially recognised at cost and adjusted thereafter for the post-acquisition change in the investor’s share of the investee’s net assets. The investor’s profit or loss includes its share of the investee’s profit or loss and the investor’s other comprehensive income includes its share of the investee’s other comprehensive income.”

Paragraph 27 of Ind AS 28, states, inter alia, that when an associate or joint venture has subsidiaries, associates or joint ventures, the profit or loss, other comprehensive income, and net assets taken into account in applying the equity method are those recognised in the associate’s or joint venture’s financial statements (including the associate’s or joint venture’s share of the profit or loss, other comprehensive income and net assets of its associates and joint ventures), after any adjustments necessary to give effect to uniform accounting policies.

The change of interest in the net assets / equity of the associate as a result of the investee’s equity transaction is reflected in the investor’s financial statements as ‘share of other changes in equity of investee’ (in the statement of changes in equity) instead of gain in Statement of profit and loss, since it reflects the post-acquisition change in the net assets of the investee as per paragraph 3 of Ind AS 28 and also faithfully reflects the investor’s share of the associate’s transaction as presented in the associate’s consolidated financial statements.

Thus, in the given case, Entity A recognises ₹20 as change in other equity instead of in statement of profit and loss and maintains the same classification as of its associate, Entity B, i.e., a direct credit to equity as in its consolidated financial statements.

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**7.6.4 Impairment losses**

After application of the equity method, it is necessary to recognise any additional impairment loss with respect to Investor’s net investment in the associate or joint venture. There has to be substantial objective evidence of impairment as a result of one or more events that occurred after the initial recognition of the net investment (a ‘loss event’) and that loss event (or events) has an impact on the estimated future cash flows from the net investment that can be reliably estimated. There may be combined multiple events that may result in impairment. It is important to note that any losses expected from future events, no matter how likely, are not recognized. Objective evidences may include

(a) significant financial difficulty of the associate or joint venture;
(b) a breach of contract, such as a default or delinquency in payments by the associate or joint venture;
(c) the entity, for economic or legal reasons relating to its associate’s or joint venture’s financial difficulty, granting to the associate or joint venture a concession that the entity would not otherwise consider;
(d) it becoming probable that the associate or joint venture will enter bankruptcy or other financial reorganisation; or
(e) the disappearance of an active market for the net investment because of financial difficulties of the associate or joint venture.

**Example:**
X Ltd, an associate of Y Ltd, disappears from the active market as its financial instruments are no longer publicly traded. However, this is not evidence of impairment. It has to supported by other evidences.

**Example:**
There is a downgrade of an associate’s or joint venture’s credit rating. This, however, is not an evidence of impairment, although it may be evidence of impairment when considered with other available information.

**Example:**
There are significant changes with an adverse effect that have taken place in the technological, market, economic or legal environment in which the associate or joint venture operates, and indicates that the cost of the investment in the equity instrument may not be recovered. A significant or prolonged decline in the fair value of an investment in an equity instrument below its cost is also objective evidence of impairment.

Goodwill that forms part of the carrying amount of the net investment in an associate or a joint venture is not separately recognized. Therefore, it is not tested for impairment separately by applying the requirements for impairment testing goodwill in Ind AS 36, Impairment of Assets. Instead, the entire carrying amount of the investment is tested for impairment in accordance with Ind AS 36 as a single asset, by comparing its recoverable amount (higher of value in use and fair value less costs to sell) with its carrying amount. Accordingly, any reversal of that impairment loss is recognised in accordance with Ind AS 36 to the extent that the recoverable amount of the net investment subsequently increases.

In determining the value in use of the net investment, an entity estimates:

(a) its share of the present value of the estimated future cash flows expected to be generated by the associate or joint venture, including the cash flows from the operations of the associate or joint venture and the proceeds from the ultimate disposal of the investment;

or

(b) the present value of the estimated future cash flows expected to arise from dividends to be received from the investment and from its ultimate disposal.

Using appropriate assumptions, both methods give the same result.