

Accounting Updates and Year End Reminders



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Recent Media Headlines – Y.E March 31, 2013



1. Cairn India – Adjustment of Goodwill of Rs. 10,167 crores in Standalone and Consolidated Financial Statement

2. Tata Steel – Impairment of Rs. 8,356 crores



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Objective and overall background

The objective of this session is to share the key updates in Indian GAAP along with more common accounting issues that are may be considered in year-end closure of various financial statements for the year ending March 31, 2013/Quarter ending June 2014.

Status on Accounting Standards

Sources	Update and literature for 2013
Accounting Standards 1-32 (AS 8 withdrawn and AS 30, 31 and 32 is not mandatory)	None
Accounting Standards Interpretation ASI 1 – 29 (ASI 2, 3 and 11 withdrawn)	None
Limited Revision – Various in the text of the Standards	None
ICAI Announcements – Central Council Decisions	None
Guidance Notes	One (Oil and Gas)
Expert Advisory Opinions (EAO)	Various
FRRB Pronouncements	Various

FRRB Observations

FRRB – Observations Relating to Accounting Non-Compliance

	Observations
1	Timing of recognition of revenue is generally not described in accounting policies - AS 1
2	Depreciation is charged directly to revaluation reserve without routing it through P&L (Para 9 of Guidance Note on revaluation of fixed)
3	Excess Depreciation (for change in method) is withdrawn from general reserves.
4	Extraordinary items – Not meeting the test of the term “extraordinary” (AS 4 Definitions)
5	Dividend - Accrual of Income is not basis of AGM date
6.	Revaluation of Fixed assets added in total instead of individual item of FA
7.	Items covered under forward rate are not retranslated /restated - AS 11
8	No disclosure of exchange loss in P&L (AS 11 para 40 (a))
9	Inadequate disclosures are made with respect to classification of Investment. Neither Schedule VI nor AS 13 is fully complied. Typically trade & non-trade classification is not made.
10	Sale of investment – FIFO/LIFO method is applied which is not acceptable as only weighted average cost is allowed per Para 22 of AS 13.

FRRB – Observations Relating to Accounting Non-Compliance

	Observations
11	AS 15 – para 17 (1) – simple accrual at year end for eligible employees (as against actuarial valuation) is allowed only for company's employing very small number of employees
12	Contribution paid to LIC may not be an appropriate accrual.
13	Borrowing – General cost borrowing cost just expensed (contravened para 12) and the amount capitalized is just not disclose (contravened Para 23).
14	Segments – Business segments are evident from MD&A but not disclosed in Financial statement (AS 17)
15	Apparent inconsistencies in identifying primary & secondary segments (Para 19 contravened)
16	Lease rent is accounted as per terms of agreement (Para 25 of AS 19 contravened)
17	Convincing evidence for determining 'virtual certainty' is not disclosed (AS 22 disclosure requirement contravened)
18	DTA shall be recognized at least to the extent of DTL (AS 22 para 18 contravened)
19	Para 15 and 17 of AS 22 interpreted –Where the enterprise have unabsorbed losses or / and depreciation, DTA on all the items (not merely unabsorbed losses/depreciation) should be based on virtual certainty.

Accounting Standards Refresher – Beyond Basics

AS – 2: Beyond Basics

Cost Formulas v/s Techniques of Measurement

Specific Identification cost method shall be used for items

- that are not ordinarily interchangeable
- and goods or services produced and segregated for specific projects.

In all other cases the cost of inventories,

- first-in, first-out (FIFO), or
- weighted average cost formula.

Techniques for the Measurement of Cost

- Standard cost method or
- the retail method,

may be used for convenience if the results approximate the actual cost.

Questions

- Is technique of measurement an acceptable cost formula ?
- Is the list of permissible cost formula limited ?
- Is the management having discretion to adopt any of the permissible methods ?

Net Realisable Value

Definition: Net realisable value is the estimated selling price in the ordinary course of business less the estimated costs of completion and the estimated costs necessary to make the sale.

Implementation Issues

- Are NRV compared on item by Item basis or global basis ? (Refer para 21)
- What is the treatment of surplus inventory i.e. though not obsolete ? (*Refer EOA – VOL XIV Page 35*)
- Are committed contracts for sale to be taken into account in arriving NRV ? (Refer Para 22)
- How the NRV for Raw Material is computed. (Refer Para 24)
- Are subsequent prices taken into account while arriving at NRV. If so, to what extent or under what circumstances ? (Refer AS 4)
- Is Negative NRV Possible (e.g... Onerous contracts, Para 23)
- Where Inventory once written down to NRV can it be Written Back (Refer Indian GAAP Framework , IAS 2)

Special Treatments as stated in other Accounting Standards

Accounting Standard 11, *'Accounting for the Effects of Changes in Foreign Exchange Rates'*

Accounting Standard 14, *'Accounting for Amalgamations'*

Accounting Standard 16, *'Borrowing Cost'*

Accounting Standard 21, *'Consolidated Financial Statements'*

Special Treatments as stated in Expert Advisory Opinion

EOA – VOL VII Page 58 -

Determination of Normal Capacity

EOA – VOL XVI Page 34 & EOA -

Accounting for Waste Products

EOA – VOL XII Page 46 -

Goods in Transit

EOA – VOL XII Page 32 -

Accounting for Goods Sent on Approval

EOA – VOL XII Page 44 -

Materials Given on Loans

EOA – VOL IV Page 8 -

Valuation of Empties

EOA – VOL X Page 77 -

Valuation of rubber and tea

EOA – VOL XVI Page 41 -

Valuation of books by publishing company

EOA – VOL IX Page 88 -

Valuation of Inventories in an extractive industry

EOA – VOL XIV Page 35 -

Valuation of Spares

EOA – VOL XIII Page 77 -

Factory Administration Cost and Valuation of Inventory

AS - 6 : Beyond Basics

Solution:

(EAO – VOI XI Page 48)

- A payment is made for asset, the title is not transferred , expenditure is made on its improvement, should the expenditure be capitalized, depreciated and disclosed

Basis

- Substance over form
- Intended to be used for production
- Unclear title to be disclosed

Conclusion

- Yes.
- Capitalized and depreciated and disclose fact of unclear title

AS - 6 : Beyond Basics

Solution:

(EAO – VOL XVII 87)

- Depreciation of Helicopter whether on basis of schedule XIV rates or actual hours flown ?

Basis

- Schedule XIV rates are minimum rates
- Additional wear & tear for excess use

Conclusion

- Higher of Schedule XIV rates or Hours Flow to be determined for each year on cumulative basis

AS - 6 : Beyond Basics

Conclusions on Methods of Depreciation

- (EAO – VOL V page 47) – Adoption of Different methods of depreciation for different class of assets is Permitted
- (EAO – VOL VIII page 72) – Adoption of Different methods of depreciation for same class of assets is permitted (e.g. plants at different location)
- (EAO – XXI, page 224) – Adoption of Different methods of depreciation for same class of assets based on acquisition dates is not permitted.

Conclusions on Methods of Depreciation

- 100 % Rate v/s full write-off
- 10 % Criteria generally overlooked

Key Terms - Depreciation

Depreciation is a measure of

the wearing out, consumption or other loss of value of a depreciable asset arising from;

- use,
- efflux of time or
- obsolescence through technology and market changes.

Questions

- Is depreciation required to be provided for Idle Assets ?
- Is depreciation required to be provided on Asset held for Disposal ?

Key Terms – Depreciable Assets

Depreciable assets are assets which;

- are expected to be used during more than one accounting period; and
- have a limited useful life; and
- are held by an enterprise for use in the production or supply of goods and services, for rental to others, or for administrative purposes and not for the purpose of sale in the ordinary course of business.

Questions

- Is Goodwill Required to be depreciation ? (Para 1)

Key Terms – Useful Life and Depreciable Amount

Useful life is either

- (i) the period over which a depreciable asset is expected to be used by the enterprise; or
- (ii) the number of production or similar units expected to be obtained from the use of the asset by the enterprise.

Depreciable amount of a depreciable asset is its historical cost, or other amount substituted for historical cost in the financial statements, less the estimated residual value.

Comment

- Relationship between useful life and depreciable amount.

AS - 6 : Beyond Basics

- **Change in Estimate of Useful Life (Para 11)**
 - Whether effect to be given is prospective or retrospective ?
- **Effect of Change in Depreciation Method ? (Para 15)**
 - Retrospective or Prospective
- **Schedule XIV Rates v/s Useful life; higher or lower ? (Para 13)**
 - Circular n.o 2/89 of DCA focuses on “Minimum Rates”
- **Depreciation on any Addition or Extension (Para 9)**
 - Where integral Part
 - Where separate identity
- **Residual Value (Para 10)**
 - Whether 5 % to be retained or Nil value is allowed ?
- **Where Historical Cost has Undergone Change ? (Para 16)**
 - Retrospective or Prospective

AS - 10 : Beyond Basics

- Treatment of Forex Expenditure – AS 11
- Treatment of Trial Run Expenses – During Substandard Production Meant for Sale – EAO VOL VXII Page 63
- Treatment of Liquidated Damages Received – EAO VOL XIII Page 49
- Treatment of Time Barred Liabilities – EAO VOL XIV page 95
- Treatment of Replacement – Vol XIV page 75
- Treatment of Building purchased along with Land – EAO – VOL X page 10

AS – 9: Beyond Basics

Select Examples; Recognition of Revenue from Sale Transactions (Ref. Appendix A)

Sr No	Situations	Basis
1	Delivery is delayed at buyer's request and buyer takes title and accepts billing	When identified item is ready for delivery
2	Delivered subject to conditions	
	(a) installation and inspection	On Installation unless it is just a too simple
	(b) on approval	On acceptance or act of acceptance or after reasonable time
	(c) guaranteed sales	Depending on nature like retail sales or to distributor
	(d) consignment sales	On sales to Third Party
	(e) Cash on delivery	On Receipt of Cash
3	Sales to intermediate parties	Based on transfer of risk and rewards criterion
4	Subscriptions for publications	on time/value proportion
5	Instalment sales	Recognise except interest which shall be on effective yield
6	Trade discounts and volume rebates	Not a revenue
7	Sale/repurchase agreements	Not a revenue

Select Examples; Basis of Sales Criterion (Ref. Expert Advisory Opinions)

Sr No	References	Basis
1	EAO – Volume XVII Page 42	Revenue recognition in case of sale of goods on Documents against payment basis
2	EAO VOL XIX page 99	Treatment of Loan restructuring and interest waived in the books of the borrower
3	CA Journal, October 2001	Accounting treatment of Recovery of Income Tax from Customers
4	EAO – Volume XV Page 2 & EAO VOL XIX page 159	Accruing of Interest on outstanding from Customers

Select Examples; Revenue Recognition from Rendering Services (Ref. Appendix B)

Sr No	Situations	Basis
1	Installation Fees	On installation
2	Advertising agency commissions	On publication date
3	Insurance agency commissions	On Commencement or renewals
4	Financial service commissions for arranging loans	Binding Agreement
5	Financial service commissions for Commitments	Over the life of the commitment facility
6	Admission fees for events	When the event takes place
7	Tuition fees	Over the period of instruction
8	Membership fees with no privileges	When due
9	Membership fees entailing the user subsidies services	On systematic and rational basis

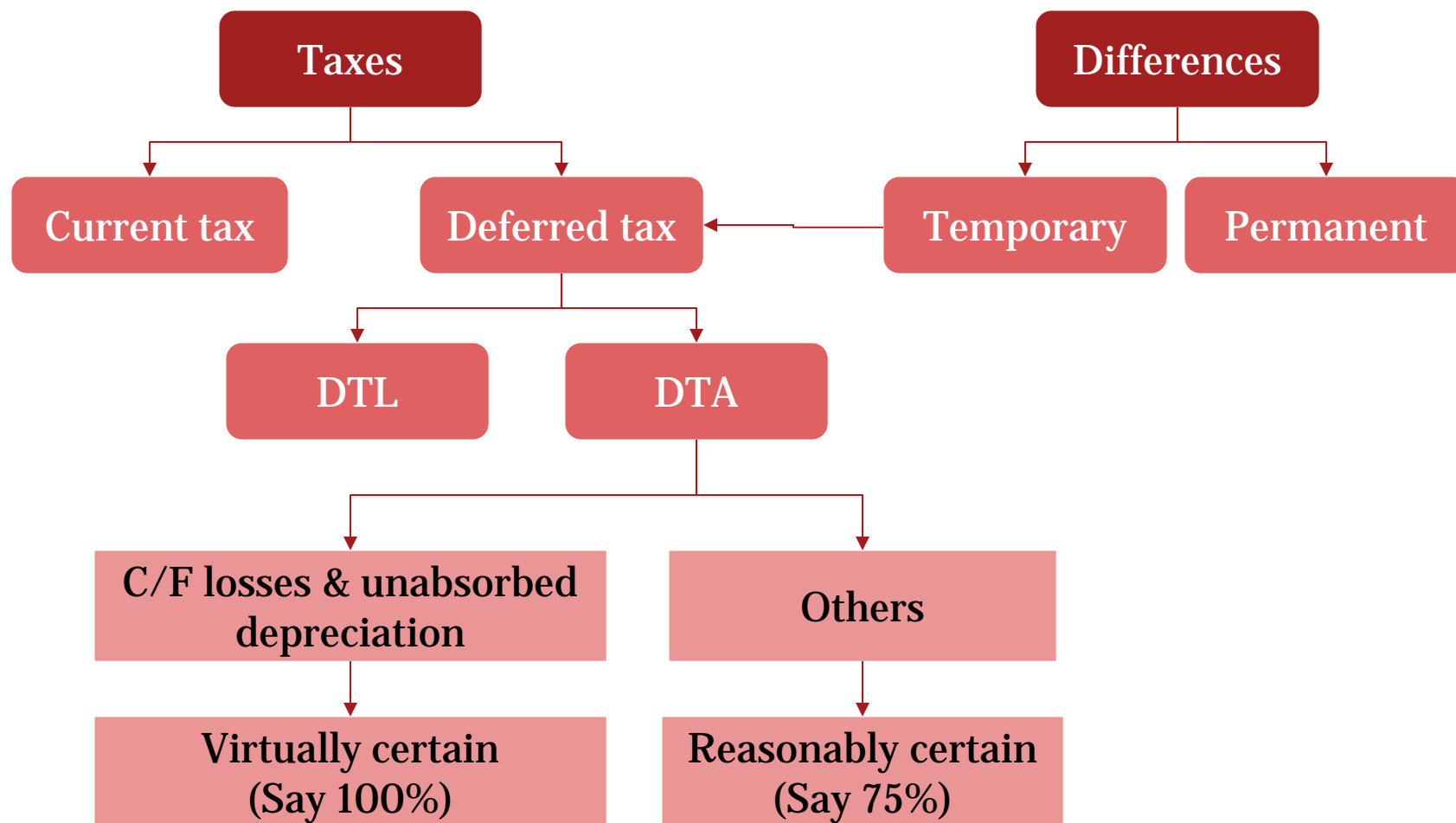
Criteria: Use by others ...resources of entity

Transactions	Basis
(i) Interest	on a time proportion basis taking into account the amount outstanding and the rate applicable.
(ii) Royalties	on an accrual basis in accordance with the terms of the relevant agreement.
(iii) Dividends from investments in shares	when the owner's right to receive payment is established.
Provided no significant uncertainty as to measurability or collectability exists	

Accounting Standards – Select Aspects tested in a stressed economy

AS – 22: Beyond Basics

Accounting for Taxes on Income Commentary on Issues in Basic Framework

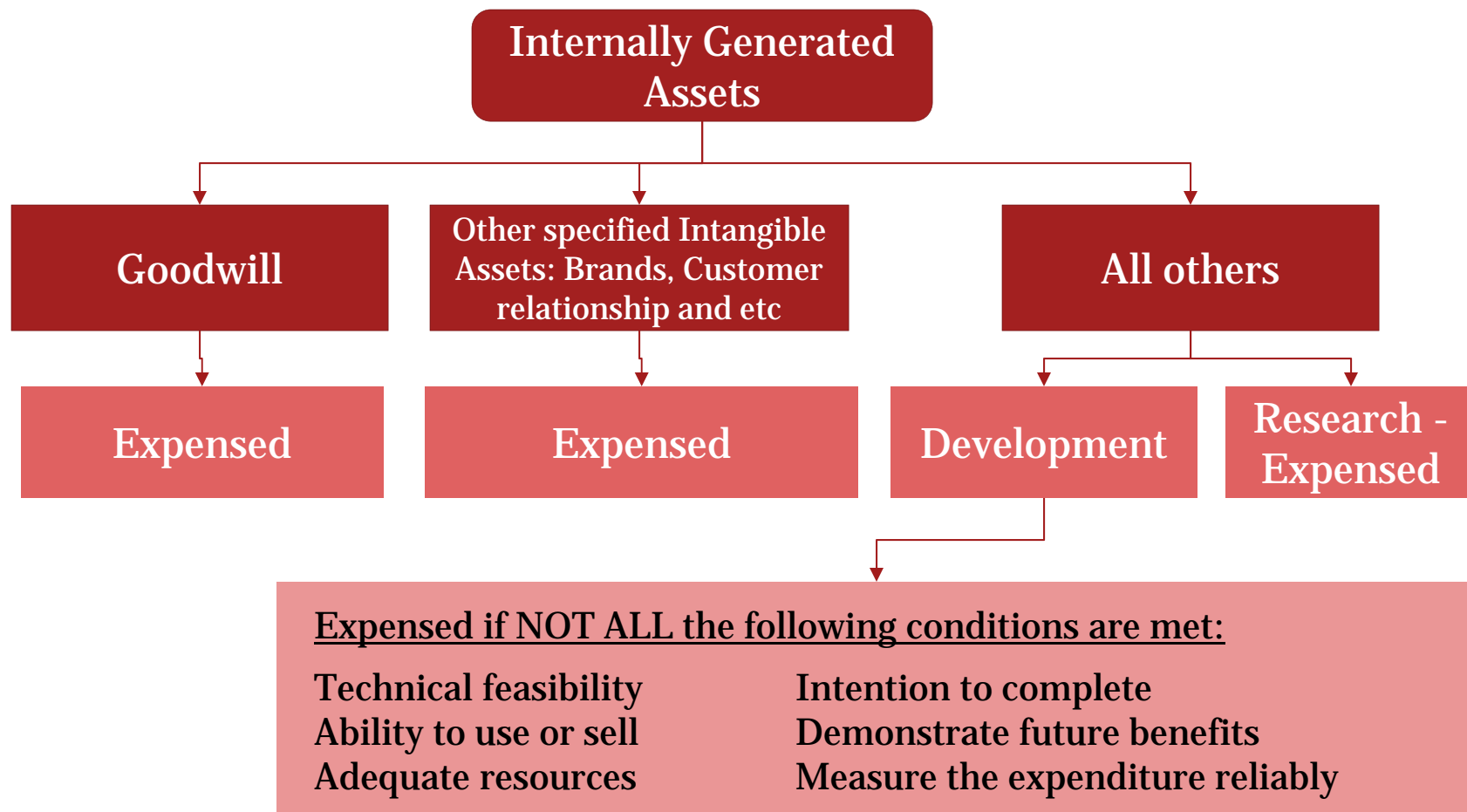


AS - 26: Beyond Basics

Intangible Assets: Meaning - Commentary on Issues in Basic Definition

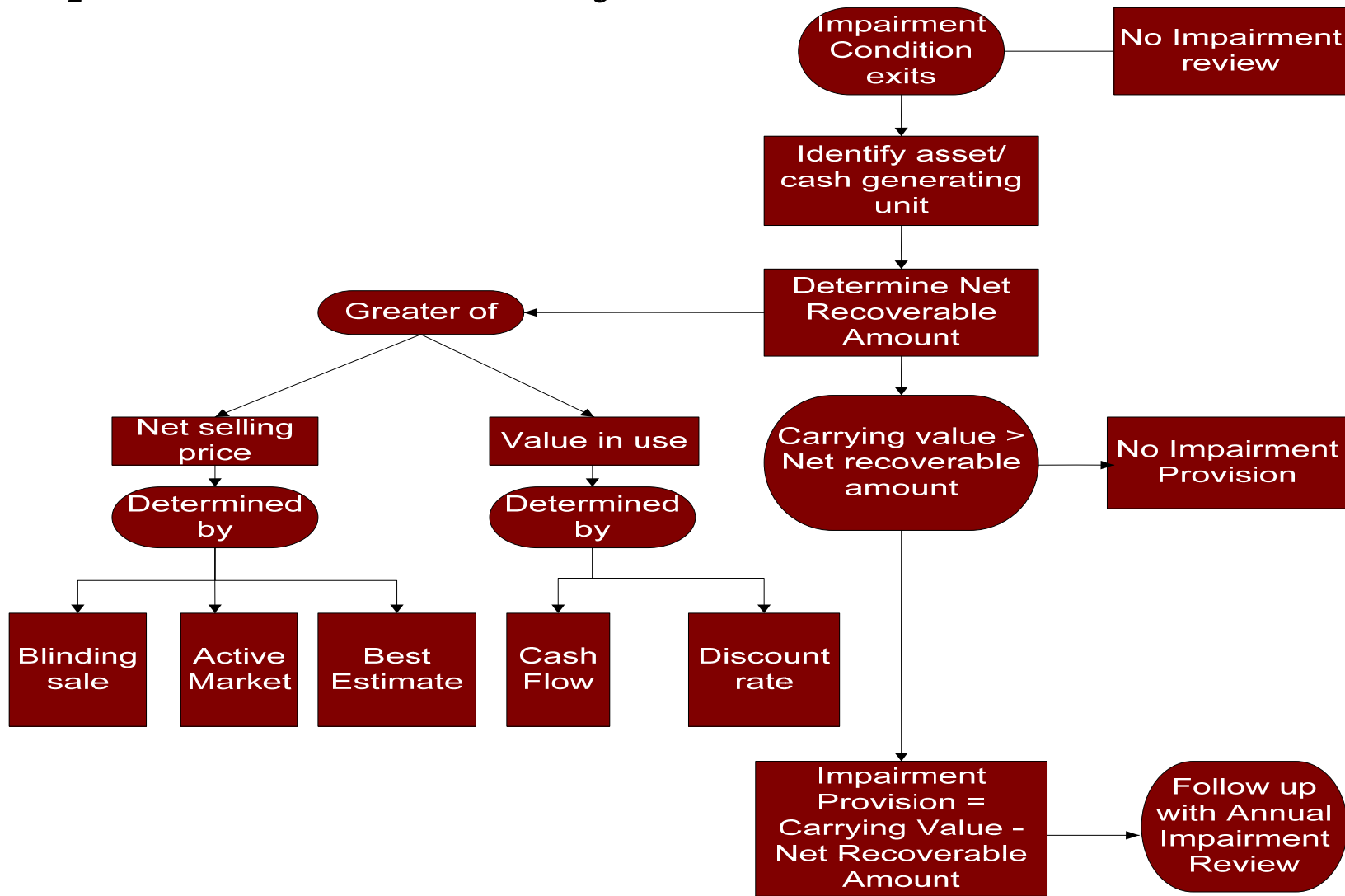
- ***An intangible asset is an identifiable non-monetary asset, without physical substance, held for use in the production or supply of goods or services, for rental to others, or for administrative purposes.***
- Analysis of Definition (read with definition of Asset)
 1. Identifiability
 2. Control by enterprise
 3. Expectation of future economic benefits
- Any expenditure not meeting definition of intangible asset, are ***expensed*** when incurred.

Summary: Accounting Treatment Internally Generated Assets - Commentary on Issues in Basic Framework



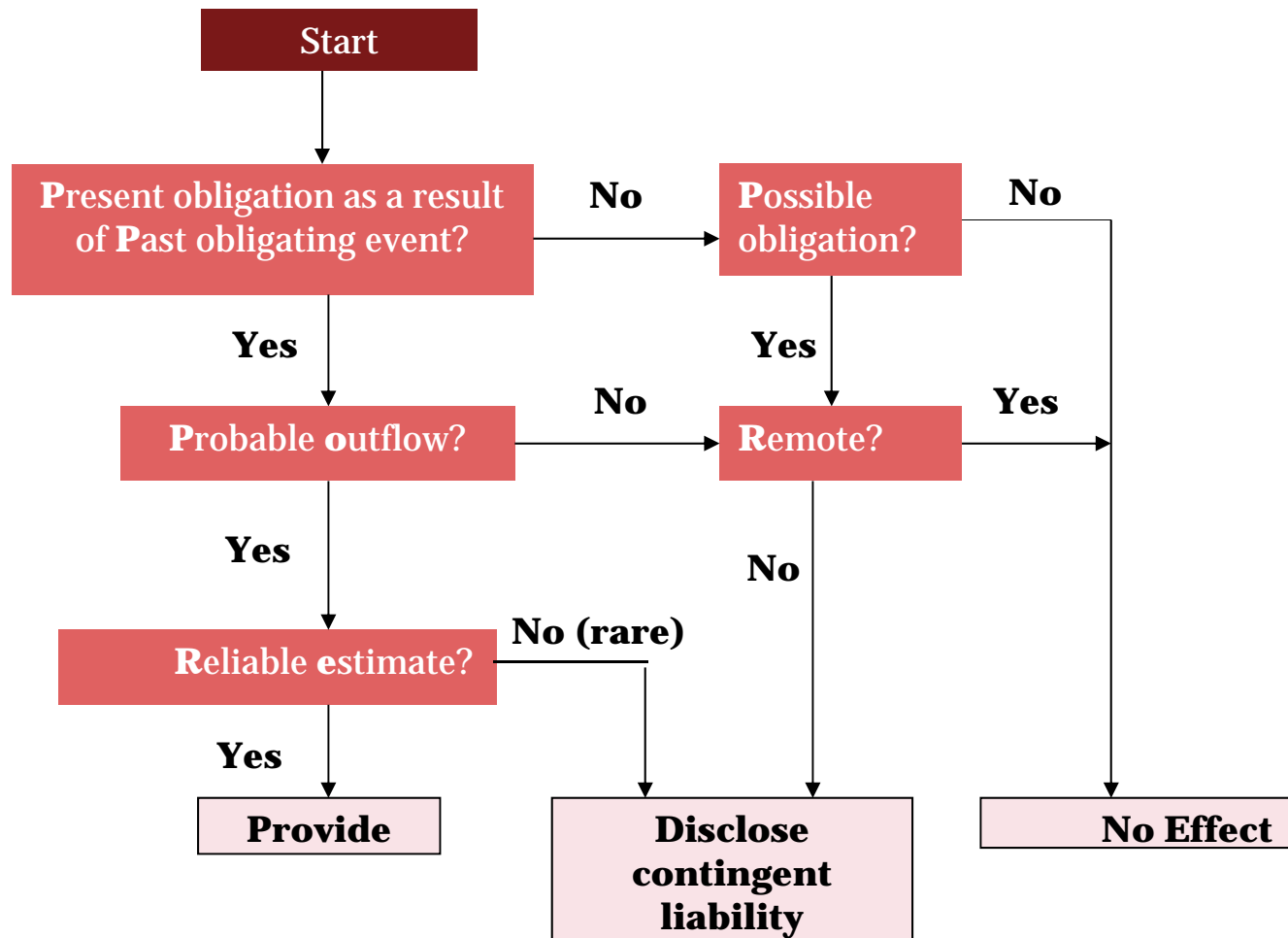
AS – 28: Beyond Basics

Impairment - Commentary on Issues in Basic Framework



AS – 29: Beyond Basics

Recognition of Provision - Commentary on Issues in Basic Framework



Other Accounting Standards in stressed economy

Name of AS	Events of Stress
Revenue Recognition	Condition of reasonable certainty or realisation
Construction Contracts	In most case application of % completion method can only be measured on basis of cost as against physical units
Borrowing Costs	Delay in capitalisation and ready for intended use.
Amalgamation	Court asks auditors certificate of compliance with framework
Employee Benefits	Application of discount rate
Investments	Impairment testing on item by item basis

Commentary on schedule VI and Other Disclosure practices

	Observations
1	Notes in financial statements such as “Debtors are subject to confirmation” are absurd and should be avoided at all cost.
2	General weakness in classifying provision and liabilities. Often provision are classified as liability.
3	Restatement (which is not permitted in India) is generally treated as regrouping.
4	Rounding off in excess of rupees thousand and approval by the DCA has been approved by some companies. Larger number of companies had rounded off beyond thousand and without approval from DCA.

Year End Updates and developments

Year End Updates

Question 1

Capitalisation of interest during pre-operative period in Cable and Telecommunication Industry.

The querist has sought the opinion of the Expert Advisory Committee that considering the nature of the business and assets of the company, whether (i) the company ought to capitalise borrowing cost for the period when commercial operation is not feasible for certain period initially for want of customers, and (ii) charging off fully the interest to the profit and loss account will not be proper in view of applicability of AS 16.

Answer

No.

The time taken for getting sizeable number of customers cannot be considered in the instant case as “Substantial period of time”

Year End Updates

Question 2

Accounting treatment of Minimum Alternative Tax (MAT) Credit in case of carried forward losses.

The querist has sought the opinion of the Expert Advisory Committee as to whether recognition of MAT credit entitlement is necessary in the year 2009-10 even with the presence of huge carried forward losses of Rs. 92,048 lakh at the beginning of the year and uncertainty in profitability due to upcoming events, like implementation of IFRS and Direct Tax Code from 1 st April, 2011 or whether the company should create MAT credit as an asset in the year when there is virtual certainty that computation of income tax as per normal provisions of Income-tax Act, 1961 shall arise or earlier to that.

Answer

Yes.

The criteria for Virtual Certainty is not stipulated in guidance note on accounting of MAT.

Year End Updates

Question 3

Depreciation on freehold land having mineral reserves and the internal roads constructed in the premises of the company

The querist has sought the opinion of the Expert Advisory Committee on the following issues:

- (i) whether accounting treatment given by the company for amortisation of the land (over the period of extraction of mineral) is in order or not . If not, whether the company should charge depreciation on the basis of mineral actually excavated with respect to the estimated reserves of lignite. Further, in case amortisation of the land is to be done on the basis of quantity of lignite excavated, whether the same is to be done retrospectively.
- (ii) whether depreciation on the road constructed on such land should be charged on the same basis as that of the land or as per Schedule XIV to the Companies Act, 1956.

Answer

- i) No. Depreciation shall on units of production method**
- ii) No. Depreciation of roads shall be on basis of its own useful life.**

Year End Updates

Question 4

Accounting for the share of expenditure incurred by the company on development of power sub-station and for obtaining power connection.

The querist has sought the opinion of the Expert Advisory Committee on the following issues:

- (i) Whether the expenditure of Rs. 62.70 lakh to be paid to Developer and subsequent payments to SPCL for getting the power connection is capital or revenue in nature. If it is classified as capital expenditure, then the class of asset in which the expenditure should be booked may be clarified.
- (ii) Whether such expenditure creates an intangible asset as defined and governed by Accounting Standard (AS) 26, 'Intangible Assets'.

Answer

- i) Revenue in nature as the power station shall be owned by SPCL. For an item to be recognised as asset, the criteria of “control” needs to be met which has not been met.**
- ii) No. In view of above**

Year End Updates

Question 5

Revenue recognition in case of construction contracts.

The querist has sought the opinion of the Expert Advisory Committee on the issue:

In the case of erection sites, whether the cost of cement and steel procured and delivered at the project site, specific to the project, in respect of which billing has been done as per the BBU agreed with the customer can be considered as 'cost incurred' in working out the percentage of completion as per AS 7 (revised 2002) and whether the same is in line with the revenue recognition principle as per AS 7 (revised 2002).

Answer

No. Revenue shall be recognised based on performance of the contract as against billing schedule/ delivery or dispatched agreed with / made to customer

Year End Updates

Question 6

Revenue recognition in case of project managers.

The querist has sought the opinion of the Expert Advisory Committee on the following issues:

- (i) Whether or not the company is required to follow proportionate completion method prescribed for a 'cost plus contract' method, in accordance with AS 7.

- (ii) Whether the existing accounting treatment followed by the company of recognising only the service charges, i.e., professional fee, as its revenue is in order.

Answer

- i) No. These shall be accounted under AS 9 as rendering of services.**
- ii) Yes.**

Year End Updates

Question 7

Accounting for sales returns

The querist has sought the opinion of the Expert Advisory Committee on the following issues:

- (i) Whether the present policy of the company regarding recognition of sales returns after the date of the balance sheet in the books of account only upon the physical receipt of goods from the franchisees is correct.

- (ii) If the company records the sales returns received after the date of the balance sheet on estimated basis taking into account the past trend, whether it will be proper accounting to prepare financial statements of the company on estimation basis.

Answer

- i) No. It shall be based on estimates of sales return.**
- ii) Yes.**

Year End Updates

Question 8

Accounting for book value of fixed assets demolished for expansion purpose.

The querist has sought the opinion of the Expert Advisory Committee with respect to capitalisation of book value of assets demolished along with the new assets in the books of the company.

Answer

Yes

The Committee is of the opinion that on disposal/demolition of the existing fixed assets, the carrying amount of the portion/items of the fixed assets demolished/disposed off should be eliminated from the financial statements and the gain or loss on derecognition should be recognised in the statement of profit and loss,

Developments - Recent Guidance Notes

Name of GN	Effective Date	Key Points
Accounting for Oil and Gas Producing Activities	1 st April, 2013	Changes/reiterations 1. Applicability to Shale Gas 2. Under FCM, the cost centre not normally smaller than a country
Accounting for Real Estate Transactions	1 st April, 2012	Changes 1. Wider applicability 2. 25% of construction cost criteria 3. Receipt of 10% of the consideration
Accounting for Self-generated Certified Emission Reductions (CERs)	1 st April, 2012	1. Carried at cost or NRV whichever is lower 2. Grant of CER certificate from UNFCC
Rate Regulated Activities	1 st April, 2012	Introduces concept of recognising regulatory assets/liability

What is coming

Companies Bill

Definitions	Consolidated Financial Statement	Restatement	Financial Year
<ul style="list-style-type: none">• Differences exists between Definition as per AS and in the bill w.r.t. (a) Associated Company and (b) Control and thus Subsidiary company	<ul style="list-style-type: none">• Consolidation is made mandatory• Manner of consolidation is yet to be notified (This is already there in AS)• Disclosure of salient features of financial statement of its subsidiaries in a form as may be prescribed shall be required to be made.• Filing of accounts of subsidiaries outside India along with financial statement is required.	<ul style="list-style-type: none">• The company would be able to reopen the accounts and recast its financial statements after the necessary approvals.	<ul style="list-style-type: none">• Financial year shall mean the period ending on the 31st day of March every year.

Tax Accounting Standards

TAS	Particulars
AS 4	<ul style="list-style-type: none">• Under TAS adjustments for events after balance sheet date are allowed only when Material whereas under AS there is no such requirement of materiality
AS 5	<ul style="list-style-type: none">• There is no concept of Prior Period Item under TAS
AS 7	<ul style="list-style-type: none">• Anticipated losses are not allowable under TAS but in AS.• Contract cost relating to future activity shall be treated as asset and later shall be considered allowable expense under the provisions of the act. Typically these are expensed under AS.
AS 10	<ul style="list-style-type: none">• Under TAS exchange of assets shall be recorded at lower of asset given up or assets acquired
AS 11	<ul style="list-style-type: none">• Under TAS exchange losses /forward premium are recorded in financial statement only on settlement
AS 16	<ul style="list-style-type: none">• Income on temporary investment of funds shall be considered as income in TAS whereas it is reduced from borrowing cost eligible for capitalization under AS.• Under TAS, apportionment of general borrowing shall be based on ratio of qualifying assets to total assets whereas it for entire qualifying asset under AS.
AS 19	<ul style="list-style-type: none">• Uniformity of classification between lessor and lessee has to be ensured by joint confirmation. There is no such requirement under AS
AS 29	<ul style="list-style-type: none">• Contingent asset are recognized when it is reasonably certain as against virtually certain in AS.

Ind – AS

Deloitte.

Indian GAAP, IFRS and Ind AS
A Comparison

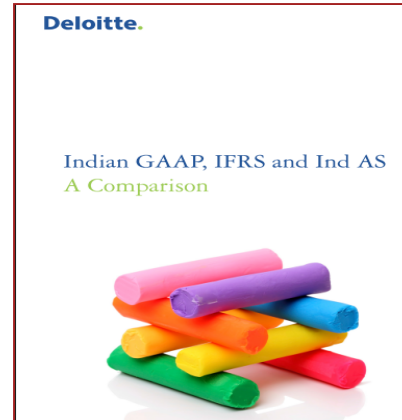


Tools & Template

Tools & Template



A study on Compliance of Financial Reporting Requirements



Comparison of Indian GAAP, IFRS and Ind AS



Illustrative financial statement as per Indian GAAP



Report issued by Accounting Standards Committee of CBDT

