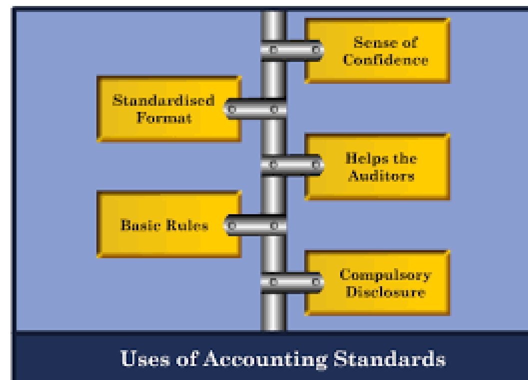
Accounting & Accounting Standards for Non-Corporate Entities in India



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Accounting is the language of a business. **Accounting** or **accountancy** is the measurement, processing and communication of financial information about economic entities. There are general rules and concepts that govern the field of accounting. These general rules are referred to as basic accounting principles**.** These basic principles or guidelines forms the base for more detailed, complicated and legalistic accounting rules often referred to as "generally accepted accounting principles" or GAAP. **Generally accepted accounting principles** (**GAAP**) are the standard framework of guidelines for financial accounting used in any given jurisdiction; generally known as **accounting standards**. These include the standards, conventions, and rules that accountants follow in recording and summarizing and in the preparation of financial statements. The phrase GAAP consists of three important sets of rules: (1) the basic accounting principles and guidelines, (2) the detailed rules and standards issued by the chief Accounting Body, and (3) the generally accepted industry practices. Accounting Standards describes the accounting principles, in relation to recognition, measurement, presentation and disclosure of various elements of accounts. They deal with the valuation technique, and the method of applying the principles of accountancy in preparation and presentation of financial position and performance of an entity so that they may present a true and fair view and make ample disclosure of required information in most appropriate manner. Pronouncement of accounting standards reduces/ eliminates variations in accounting treatment thereby ensuring consistency and comparability of statements prepared by same entity in different periods or by different entities even across sectors and political boundaries. Appreciating the need for uniform accounting standards, the Council of Institute of Chartered Accountants of India (ICAI), constituted Accounting Standards Board (ASB) on 21st April 1977 and started the process of pronouncing Accounting Standards in India.

Applicability of Various Accounting Standards in India

In India, currently there are multiple sets of accounting standards that are applicable to different forms and sizes of entities as 'one size fit all' approach is mot pragmatic. These frameworks can broadly be classified can be bifurcated into two: one for Governmental Accounting and other for non-governmental commercial profit seeking enterprises.

Governmental Accounting in India

The Government accounting system in India is rule based and follows primarily, cash basis accounting. The Comptroller and Auditor General of India (CAG) has constituted Government Accounting Standards Advisory Board (GASAB) with the support of Government of India (GoI) to formulate and recommend Indian Government Accounting Standards (IGASs) and 'Indian Government Financial Reporting Standards (IGFRSs)' with a view to improving standards of Governmental accounting and financial reporting. Where IGAS are based on Cash Basis of accounting as are currently in vogue in India, IGFRS are on accrual basis and futuristic in nature.

Indian Government Accounting Standards (IGASs)

So far, GASAB has approved 6 IGASs of which 3 has been implemented and other three are under consideration by the Government. These Standards are based on internationally recognized IPSAS standards for Cash basis of accounting (popularly known as Cash IPSAS) issued by the International Public Sector Accounting Board (IPSASB), constituted by the International Federation of Accountants (IFAC). The three IGASs notified by the GoI are:

IGAS 1: Guarantees given by Governments: Disclosure Requirements

IGAS 2: Accounting and classification of Grants-in-Aid; and

IGAS 3: Loans and Advances made by Governments

Following IGASs approved by GASAB are under consideration by GoI:

IGAS 7: Foreign Currency and Loss/ Gain by Exchange Rate Variations;

IGAS 9: Government Investments In Equity; and

IGAS 10: Public Debt and Other Liabilities of Governments: Disclosure Requirements.

'Indian Government Financial Reporting Standards (IGFRSs)

Though traditionally, cash based accounting system is followed in India for budgeting, accounting and financial reporting as cash based system is simple and recognizes a transaction when cash is paid or received. It requires less skilled personnel and is geared to cash management needs. It has also served the basic requirements of financial accountability of Government to Parliament. However, cash based system of accounting is not the most informative way of presenting government account and much need is being felt for accounting framework and accounting standards on accrual basis to keep in pace with the global best practices and to facilitate pilot studies and research efforts on migration to accrual accounting at Union and State level. GASAB has also taken a decision to develop accrual basis accounting standards alongside cash basis standards. The accrual basis standards are issued under the title 'Indian Government Financial Reporting Standards (IGFRSs)'. So far, GASAB has approved 5 IGFRS and all are under consideration of the Government. These are:

- IGFRS 1 : Presentation of Financial Statements
- IGFRS 2: Property, Plant & Equipment
- GFRS 3: Revenue from Government Exchange Transactions
- IGFRS 4: Inventories
- IGFRS 5: Contingent Liabilities (other than guarantees) and Contingent Assets: Disclosure Requirements

GASAB has also developed an operational framework of the accrual system that will prevail in Government. The operational framework would provide overall architecture of the accounting model that would prevail in Government while conforming to the national and constitutional reporting needs. This important document is also under consideration of the Government.

Accounting Standards for Local Bodies (ASLB)

Accounting Standards issued by GASAB are applicable to accounting by central and state governments. They do not deal with accounting aspects of Local Bodies. The term 'Local Body' may be defined as a local self-government at the third tier of governance in an administrative and geographical vicinity, e.g., a municipal corporation, a municipality or a panchayat. In many cases, the Local Bodies delegate their functions such as building of schools, city roads, parks, running transport services, providing water supply etc., to some other bodies that may or may not be controlled by the Local Bodies, e.g. development authorities, boards, parastatals. Such bodies may be constituted, in partnership with private sector or otherwise, directly or indirectly by or on behalf of a Local Body to promote or carry out some specific objective(s) or function(s) of the Local Bodies. Such bodies may be constituted under a statute. The term 'Local Body' would also encompass such bodies too.

The Committee on Accounting Standards for Local Bodies (CASLB) set up by Council of the Institute of Chartered Accountants of India issues Accounting Standards for Local Bodies (ASLB) to fill this gap. These Standards are based on IPASAS. So far it has issued the following:

- The Conceptual Framework for General Purpose Financial Reporting by Local Bodies
- Preface to the Accounting standard for Local Bodies
- Accounting Standard for Local Bodies (ASLB) 1, *'Presentation of Financial Statements'*
- Accounting Standard for Local Bodies (ASLB) 2, 'Cash Flow Statements'
- Accounting Standards for Local Bodies (ASLB) 3, *'Accounting Policies, changes in Accounting Estimates and Errors"*
- Accounting Standards for Local Bodies (ASLB) 4, *'The Effects of Changes in Foreign Exchange Rates'*
- Accounting Standard for Local Bodies (ASLB) 5, *'Borrowing Costs'*

- Accounting Standard for Local Bodies (ASLB)9, *‘Revenue from Exchange Transactions’*
- Accounting standard for Local Bodies (ASLB) 11, *“Construction Contracts”*
- Accounting Standard for Local Bodies (ASLB) 12, *'Inventories'*
- Accounting Standards for Local Bodies (ASLB) 13, *‘Leases’*
- Accounting Standard for Local Bodies (ASLB) 14, *‘Events After the Reporting Date’*
- Accounting Standards for Local Bodies (ASLB) 16, *‘Investment Property’*
- Accounting Standard for Local Bodies (ASLB) 17, *‘Property, Plant and Equipment’*
- Accounting Standard for Local Bodies (ASLB) 18, *‘Segment Reporting’*
- Accounting Standards for Local Bodies (ASLB) 19, *‘Provision, Contingent Liabilities and Contingent Assets’*
- Accounting Standard for Local Bodies (ASLB) 20, *‘Related Party Disclosures’*
- Accounting Standards for Local Bodies (ASLB) 21, *‘Impairment of Non-Cash-Generating Assets’*
- Accounting Standards for Local Bodies (ASLB) 23, *‘Revenue from Non-Exchange Transaction (Taxes and Transfers)’*
- Accounting Standard for Local Bodies (ASLB) 24, *‘Presentation of Budget Information in Financial Statements’*
- Accounting Standards for Local Bodies (ASLB) 26, *‘Impairment of Cash-Generating Assets’*
- Accounting Standards for Local Bodies (ASLB) 31, *‘Intangible Assets’*
- Accounting Standards for Local Bodies (ASLB) 32, *‘Service Concession Arrangements: Grantor’*
- Accounting Standards for Local Bodies (ASLB) 33, *‘First-Time Adoption of Accrual Basis Accounting Standards for Local Bodies (ASLBs)’*
- Accounting Standards for Local Bodies (ASLB) 34, *‘Separate Financial Statements’*
- Accounting Standards for Local Bodies (ASLB) 36, *‘Investment in Associates and Joint Ventures’*
- Accounting Standards for Local Bodies (ASLB) 39, *‘Employee Benefits’*
- Accounting Standards for Local Bodies (ASLB) 42, *‘Social Benefits’*
- Accounting Standards for Local Bodies (ASLB), *‘Financial Reporting under Cash Basis of Accounting’*

Accounting Standards for Non-Governmental Commercial Enterprises

Even if we leave aside non-commercial & governmental organizations, there are three sets of Accounting Standards applicable to non –governmental profit seeking commercial enterprises. These are:

a) Accounting Standards as pronounced by MCA under ***Companies (Indian Accounting Standards) Rules, 2015*** *[As amended on June 18, 2021]**.*** These are popularly known as Ind AS and are converged with International Financial Reporting Standards (IFRS) and applicable for specified class of companies as per MCA notification dated 16 February 2015;

b) Accounting Standards as pronounced by the Ministry of Corporate Affairs (MCA) under ***Companies (Accounting Standards) Rules, 2021*** [superseding Companies (Accounting Standards) Rules, 2006, as amended from time to time] pronounced on *June 23,* 2021. The Accounting Standards shall come into effect in respect of accounting periods commencing on or after the April 1, 2021. These Standards are applicable for companies other than those following Ind AS; and

c) Accounting Standards as prescribed by the Institute of Chartered Accountants of India (ICAI) similar to those mentioned in (b) above with minor differences regarding presentation, disclosures etc. for entities other than companies.

Accounting Standards prescribed by MCA are applicable only to Corporate Entities (Both private limited as well as public limited) whereas those pronounced by ICAI are applicable to all other form of business entities like individuals, partnerships, etc. Besides, there are certain other levels of applicability within each of these standards depending upon the size of the entity. The applicability of these accounting standards are discussed below.

Accounting Standards as prescribed by the Institute of Chartered Accountants of India (ICAI)

The Accounting Standards by ICAI are the original accounting standards of India and are also popularly known as Indian GAAP. However, the accounting standards prepared and issued by

the ICAI were mandatory only for its members, who, while discharging their audit function, were required to examine whether the said standards of accounting were complied with. With the amendment of the Companies Act, 1956 through the Companies (Amendment) Act, 1999, accounting standards as well as the manner in which they were to be prescribed, were provided a statutory backing at least for corporate entities. Ever since pronouncement of Companies (Accounting Standards) Rules 2006, ICAI standards are applicable only for non-corporate entities. Till date 32 standards have been issued by ICAI. However, AS 8 *Research & Development* had been withdrawn since pronouncement of AS 26 *Intangible Assets* in 2002. Moreover, ICAI had issued Accounting Standard (AS) 30, *Financial Instruments: Recognition and Measurement*, Accounting Standard (AS) 31, *and Financial Instruments: Presentation* in year 2007 and Accounting Standard (AS) 32*, Financial Instruments: Disclosures* in year 2008. These Accounting Standards were based on related IFRSs and were to come into effect in respect of accounting periods commencing on or after April 1, 2009, and were to be recommendatory in nature for an initial period of two years, thereafter, these were to become mandatory in respect of accounting periods commencing on or after April 1, 2011. However owing to financial crisis which raised issues regarding accounting treatment of financial instruments, the ICAI withdrew the recommendatory as well as mandatory status of AS 30, AS 31 and AS 32 in March 2011.

The Accounting Standards by ICAI has seen improvement time and again. Earlier in 2017, ICAI had decided to make changes in standards notified by it, in order to harmonise them with amendments made by the Central Government by Companies (Accounting Standards) (Amendment) Rules, 2016 . In view of the above, it released a new compendium and following changes were made in **Accounting Standards issued by the ICAI for non-corporate entities:**

i. AS 6, *Depreciation Accounting* stood withdrawn.
ii. The following Accounting Standards were amended:
    a. AS 2, *Inventories*
    b. AS 4, *Contingencies and Events Occurring After the Balance Sheet Date*
    c. AS 10, *Property, Plant and Equipment*
    d. AS 13, *Accounting for Investments*
    e. AS 14, *Accounting for Amalgamations*
    f. AS 21, *Consolidated Financial Statements*

g. AS 29, *Provisions, Contingent Liabilities and Contingent Assets*

After these amendments 27 standards as issued by ICAI are applicable to non-corporate entities (AS 1-5, 7 & 9-29). The above amendments came into effect prospectively in respect of accounting periods commencing on or after April 1, 2017. However, early application of the aforementioned amendments was permitted.

Categorization of entities for applicability of various Standards

The Council, at its 236th meeting, held on September 16-18, 2003, considered the matter relating to applicability of Accounting Standards to Small and Medium Sized Enterprises (SMEs). The Council decided that for the purpose of applicability of Accounting Standards, enterprises were classified into three categories, viz., Level I, Level II and Level III. Level II and Level III enterprises were considered as SMEs. These criteria were further revised in 2013.

One of major changes has been made recently when the Accounting Standards board of ICAI, at its 400th meeting, held on March 18-19, 2021, which has significantly simplified the accounting standards applicability criteria for Micro and small size non-company entities. This Announcement supersedes the earlier Announcement of the ICAI on 'Harmonisation of various differences between the Accounting Standards issued by the ICAI and the Accounting Standards notified by the Central Government' issued in February 2008, to the extent it prescribes the criteria for classification of Non-company entities (Non-corporate entities) and applicability of Accounting Standards to non-company entities, and the Announcement 'Revision in the criteria for classifying Level II non-corporate entities' issued in January 2013." It should be noted that Announcement is not relevant for Non-company entities who may be required to follow Ind AS as per relevant regulatory requirements applicable to such entities like in case an entity is subsidiary of a parent which is required to follow Ind AS.

The most significant change is the introduction of a new category (Level IV) which has been created for micro-enterprises. Thus, for the purpose of applicability of accounting standards, non-company entities have been now classified into four categories viz. Level-I, Level-II, Level-III and Level-IV. Further the ICAI has also revised the turnover and borrowing limits for deciding the criteria for classification of non-company entities for the applicability of accounting

standards. The scheme for applicability of Accounting Standards to Non-corporate entities shall come into effect in respect of accounting periods commencing on or after April 1, 2020.

The following table summarizes criteria for classification of Non-Corporate Entities.

Criteria	**Level – I** **(Large)**	**Level – II** **(Medium)**	**Level - III** **(Small)**	**Level – IV** **(Micro)**
Turnover (Excluding Other Income) in preceding accounting year	> 250 Crore	> 50 Crore but < 250 Crore	> 10 Crore but < 50 Crore	Non-corporate entities which are not covered under Level I, Level II and Level III are considered as Level IV entities
Borrowings (Including Public Deposits) at any time during preceding accounting year	> 50 Crore	> 10 Crore but < 50 Crore	> 2 Crore but < 10 Crore	

Besides, all entities whose shares are Listed or are under the Process of Listing in the stock exchange of India or any other country, Banks (including cooperative banks), Financial Institutes or entities carrying on Insurance Business are regarded as Level-I entity irrespective of turnover and borrowing limits. Further, the holding and subsidiary entities of entities in each category also fall in that category or superior category. There are very few non-corporate entities which may be eligible for listing like in case of non-corporate units in Special Economic Zones (SEZ) who issues Foreign Currency Convertible Bonds (FCCB) may be listed on foreign stock exchanges. A new concept of Social Stock Exchange is brewing in India. It would be interesting to figure out if For Profit Enterprises (FPE) listed on such exchanges will be mandatorily required to prepare accounts using Accounting Standards.

Level I entities are large size entities, Level II entities are medium size entities, Level III entities are small size entities and Level IV entities are micro entities. Level IV, Level III and Level II entities are collectively called referred to as Micro, Small and Medium size entities (MSMEs). As a consequence to recent amendment, the terms 'Small and Medium Enterprise' or 'SME'

used in Accounting Standards is to be read as 'Micro, Small and Medium size entity' or 'MSME'.

Level I entities have to comply with the complete set of Accounting Standards. However, certain exemptions are available to other entities. These exemptions are summarized in table below.

Accounting Standard	**Applicability to**		
	Level II (Small)	**Level III (Medium)**	**Level IV (Micro)**
AS 1 Disclosure of Accounting Policies	Yes	Yes	Yes
AS 2 Valuation of Inventories	Yes	Yes	Yes
AS 3 Cash Flow Statements	No	No	No
AS 4 Contingencies and Events Occurring After the Balance Sheet Date	Yes	Yes	Yes
AS 5 Net Profit or Loss for the Period, Prior Period Items and Changes in Accounting Policies	Yes	Yes	Yes
AS 7 Construction Contracts	Yes	Yes	Yes
AS 9 Revenue Recognition	Yes	Yes	Yes
AS 10 Property, Plant and Equipment	Yes	Applicable with Disclosures Exemption	Applicable with Disclosures Exemption
AS 11 The Effects of Changes in Foreign Exchange Rates	Yes	Applicable with Disclosures Exemption	Applicable with Disclosures Exemption
AS 12 Accounting for Government Grants	Yes	Yes	Yes
AS 13 Accounting for Investment	Yes	Yes	Applicable with Disclosures Exemption
AS 14 Accounting for Amalgamations	Yes	Yes	No

AS 15 Employee Benefits	Applicable with Exemptions	Applicable with Exemptions	Applicable with Exemptions
AS 16 Borrowing Costs	Yes	Yes	Yes
AS 17 Segment Reporting	No	No	No
AS 18 Related Party Disclosures	Yes	No	No
AS 19 Leases	Applicable with Disclosures Exemption	Applicable with Disclosures Exemption	Applicable with Disclosures Exemption
AS 20 Earnings Per Share	No	No	No
AS 21 Consolidated Financial Statements	No	No	No
AS 22 Accounting for Taxes on Income	Yes	Yes	Applicable Only for Current Tax Related Provisions
AS 23 Accounting for Investments in Associates in Consolidated Financial Statements	No	No	No
AS 24 Discontinuing Operations	No	No	No
AS 25 Interim Financial Reporting	No	No	No
AS 26 Intangible Assets	Yes	Yes	Applicable with Disclosures Exemption
AS 27 Financial Reporting of Interests in Joint Ventures	No	No	No
AS 28 Impairment of Assets	Applicable with Disclosures	Applicable with Disclosures Exemption	No

	Exemption		
AS 29 Provisions, Contingent Liabilities and Contingent Assets	Applicable with Disclosures Exemption	Applicable with Disclosures Exemption	Applicable with Disclosures Exemption

Beside the above Standards the Compendium of Accounting Standard also provides a *Preface to the Statements of Accounting Standards* and *Framework for the Preparation and Presentation of Financial Statements.*

Condition for Availing Benefits of MSME

- An MSME which avails the exemptions or relaxations must disclose by way of a note to its financial statements the fact that it is an MSME, the Level of MSME and that it has complied with the Accounting Standards insofar as they are applicable to entities falling in Level II or Level III or Level IV, as the case may be.
- Where an entity, being covered in Level II or Level III or Level IV, had qualified for any exemption or relaxation previously but no longer qualifies for the relevant exemption or relaxation in the current accounting period, the relevant standards or requirements become applicable from the current period and the figures for the corresponding period of the previous accounting period need not be revised merely by reason of its having ceased to be covered in Level II or Level III or Level IV, as the case may be. The fact that the entity was covered in Level II or Level III or Level IV, as the case may be, in the previous period and it had availed of the exemptions or relaxations available to that Level of entities shall be disclosed in the notes to the financial statements. The fact that previous period figures have not been revised shall also be disclosed in the notes to the financial statements.

- Where an entity has been covered in Level I and subsequently, ceases to be so covered and gets covered in Level II or Level III or Level IV, the entity will not qualify for exemption/relaxation available to that Level, until the entity ceases to be covered in Level I for two consecutive years. Similar is the case in respect of an entity, which has been covered in Level II or Level III and subsequently, gets covered under Level III or Level IV.

- If an entity covered in Level II or Level III or Level IV opts not to avail of the exemptions or relaxations available to that Level of entities in respect of any but not all of the Accounting Standards, it shall disclose the Standard(s) in respect of which it has availed the exemption or relaxation.
- If an entity covered in Level II or Level III or Level IV opts not to avail any one or more of the exemptions or relaxations available to that Level of entities, it shall comply with the relevant requirements of the Accounting Standard.
- An entity covered in Level II or Level III or Level IV may opt for availing certain exemptions or relaxations from compliance with the requirements prescribed in an Accounting Standard: provided that such a partial exemption or relaxation and disclosure shall not be permitted to mislead any person or public.
- In respect of Accounting Standard (AS) 15, Employee Benefits, Level II and Level III entities whose average number of persons employed during the year is less than 50 would enjoy greater exemption similar to that enjoyed by level IV entities. Others will have limited exemptions/ relaxations.

The relaxations/exemptions in each Standard are detailed below

LEVELS	
LEVEL I (large)	All 29 AS applicable in full.
LEVEL II [Medium]	**AS not applicable:** AS 3 – Cash Flow Statements; AS 17 – Segment Reporting; AS 20 – Earnings Per Share **AS applicable with exemptions:** AS 15 – Employee Benefits **Accounting Standard(s) applicable with Note:** [following AS, being related to CFS, the same is not applicable to Level II, III, IV entities unless they voluntary decide to consolidate the financial statements] AS 21 – Consolidated Financial Statements

	AS 23 – Accounting for Investments in Associates in Consolidated Financial Statements AS 25 – Interim Financial Reporting AS 27 – Financial Reporting of Interests in Joint Ventures (to the extent of requirements relating to Consolidated Financial Statements)
LEVEL III [Small]	All exemptions provided to Level II shall be applicable; In addition: **AS not applicable:** AS 18 – Related Party Disclosures, AS 24 – Discontinuing Operations **Partial disclosure exemption:** AS 10 – Property, Plant and Equipment AS 11 – The Effects of Changes in Foreign Exchange Rates
Level IV [Micro]	All exemptions provided to Level III shall be applicable. In addition: **AS not applicable** AS 14 – Accounting for Amalgamations AS 28 – Impairment of Assets AS 22 is applicable only for current tax related provisions **Partial disclosure exemption:** AS 13 – Accounting for Investments

Para 87 of Accounting Standard (AS) 10, Property, Plant and Equipment

Accounting Standard	***Relaxations/Exemptions***	**To whom**
AS 10, Property, Plant and equipment (Paragraph 87)	An enterprise is encouraged to disclose the following: (a) the carrying amount of temporarily idle PPE; (b) the gross carrying amount of any fully depreciated PPE that is still in use; (c) for each revalued class of PPE, the carrying amount that would have been recognized had the assets been carried under the cost model; (d) The carrying amount of PPE retired from active use and not held for disposal.	Level III & IV
AS 11, The Effects of Changes in Foreign Exchange Rates (Paragraph 44)	Disclosure is also encouraged of an enterprise's foreign currency risk management policy	Level III & IV
AS 13, Accounting for Investments (Paragraph 35(f))	The information should be disclosed in the financial statements for the amounts included in profit and loss statement for other disclosures as specifically required by the relevant statute governing the enterprise.	Level IV
AS 15, Employee Benefits	a. Clauses relating to recognition and measurement of short -term accumulating compensated absences which are non-vesting b. Clauses which deal with discounting of amounts that fall due more than 12 months	Level II and Level III entities whose average number of persons employed

	after the balance sheet date; c. Recognition, measurement, presentation and disclosure principles in respect of accounting for defined benefit plans. However, such entities should actuarially determine and provide for the accrued liability in respect of defined benefit plans by using the Projected Unit Credit Method and the discount rate used should be determined by reference to market yields at the balance sheet date on government bonds as per and disclose actuarial assumptions; and d. Recognition and measurement principles in respect of accounting for other long-term employee benefits However, such entities should actuarially determine and provide for the accrued liability in respect of other long-term employee benefits by using the Projected Unit Credit Method and the discount rate used should be determined by reference to market yields at the balance sheet date on government bonds	during the year is 50 or more
	a. Clauses relating to recognition and measurement of short -term accumulating compensated absences which are non-vesting b. Clauses which deal with discounting of amounts that fall due more than 12 months after the balance sheet date;	Level II and Level III Non-company entities with average number of persons employed

	c. Recognition, measurement, presentation and disclosure principles in respect of accounting for defined benefit plans. However, such entities may calculate and account for the accrued liability under the defined benefit plans by reference to some other rational method d. Recognition and measurement principles in respect of accounting for other long-term employee benefits Such entities may calculate and account for the accrued liability under the other long-term employee benefits by reference to some other rational method,	during the year is less than 50 and Level IV
AS 19, Leases	Disclosures for finance leases by lessee: [P22(c.e.f)] • the total of minimum lease payments at and their present value at the balance sheet date, and their present value, periods: (i) not later than one year; (ii) later than one year and not later than five years; (iii) later than five years; and reconciliation between two at balance sheet date • the total of future minimum sublease payments expected to be received under non-cancellable subleases at the balance sheet date; and • a general description of the lessee's significant leasing arrangements	Level II, Level III, Level IV

	The lessee should make the following disclosures for operating leases: [P25(a,b,e)] (a) the total of future minimum lease payments under non-cancellable operating leases for each of the following periods: (i) not later than one year; (ii) later than one year and not later than five years; (iii) later than five years; (b) the total of future minimum sublease payments expected to be received under non-cancellable subleases at the balance sheet date; (e) a general description of the lessee's significant leasing arrangements including, but not limited to, the following: (i) the basis on which contingent rent payments are determined; (ii) the existence and terms of renewal or purchase options and escalation clauses; and (iii) restrictions imposed by lease arrangements, such as those concerning dividends, additional debt, and further leasing. The lessor should make the following disclosures for finance leases:[P37(a,f)] • An enterprise should disclose the total gross investment in the lease and the present value of minimum lease payments receivable at the balance sheet date, for each of the following periods: (i) not later than one year; (ii) later than one year and not later than five years; (iii) later than five years. And a reconciliation between the two	

	at balance sheet date. • a general description of the significant leasing arrangements of the lessor The lessor should make the following disclosures for operating leases:[P46(b,d)] • the future minimum lease payments under non-cancellable operating leases in the aggregate and for each of the following periods: (i) not later than one year; (ii) later than one year and not later than five years; (iii) later than five years; a general description of the lessor's significant leasing arrangements	
	The lessor should make the following disclosures for finance leases:[37(g)] • Accounting policy adopted in respect of initial direct costs. The lessor should make the following disclosures for operating leases:[P46(e)] • Accounting policy adopted in respect of initial direct costs.	Additional exemption for Level III & IV
AS 22, Accounting for Taxes on Income	All provisions of the standards other than those for Current tax	Level-IV
AS 26, Intangible Assets	Disclose for each class of intangible assets a reconciliation of the carrying amount at the beginning and end of the period showing [P	Level-IV

	(d(iii),(iv))] • impairment losses recognized in the statement of profit and loss during the period (if any); and • impairment losses reversed in the statement of profit and loss during the period (if any); An enterprise is encouraged, but not required, to give a description of any fully amortized intangible asset that is still in use. [P 98]	
AS 28, Impairment of Assets	If Level II or Level III Non-company entity chooses to measure the 'value in use' by not using the present value technique, the relevant provisions of AS 28, such as discount rate etc., would not be applicable to such an entity. If an impairment loss for an individual asset or a cash-generating unit is recognised or reversed during the period and is material to the financial statements of the reporting enterprise as a whole, an enterprise should disclose if recoverable amount is value in use, the discount rate(s) used in the current estimate and previous estimate (if any) of value in use [121(g)]	Level II, III *Note: Level IV fully exempted From AS 8
	If an impairment loss for an individual asset or a cash-generating unit is recognised or reversed during the period and is material to the financial statements of the reporting enterprise as a whole, an enterprise should disclose[121(c(ii), d(i),(ii))] • for an individual asset the reportable	Additional Exemption for Level III

	segment to which the asset belongs, based on the enterprise's primary format • for a cash-generating unit: (i) a description of the cash-generating unit (such as whether it is a product line, a plant, a business operation, a geographical area, a reportable segment (ii) the amount of the impairment loss recognised or reversed by class of assets and by reportable segment based on the enterprise's primary format • An enterprise is encouraged to disclose key assumptions used to determine the recoverable amount of assets (cash-generating units) during the period.	

Principles in Accounting

An **account** (in book-keeping) refers to assets, liabilities, income, expenses, and equity, as represented by individual ledger pages, to which changes in value are chronologically recorded with debit and credit entries. These entries, referred to as postings, become part of a *book of final entry* or ledger. Examples of common financial accounts are sales, accounts receivable, mortgages, loans, Property, Plant & Equipment, wages, etc.

Classification of Accounts

Based on the nature of accounts, they may be classified in the following three categories:

- **Real Accounts:** All assets of a firm, which are tangible or intangible, fall under this category. A few examples of tangible real accounts are building, machinery, stock, land, goodwill, patents, trademarks, etc.
- **Personal Accounts**: These accounts are related to individuals, firms, companies, etc. A few examples of personal accounts include debtors, creditors, banks, outstanding/prepaid accounts, accounts of credit customers, accounts of goods suppliers, capital, drawings, etc.
- **Nominal Accounts**: Accounts which are related to expenses, losses, incomes or gains are called Nominal accounts. The dictionary meaning of the word "nominal" is "*existing in name only*" and the meaning remains absolutely true in accounting sense too, because nominal accounts do not really exist in physical form, but behind every nominal account money is involved. E.g. Purchase A/C, Salary A/C, Sales A/C, Commission received A/C, etc.

Golden Rules of Accounting

This classification of accounts is important to understand the three golden rules of accountancy which are pillars on which any financial reporting stands. These rules are as follows:

For Real Accounts*: Debit what comes in, credit what goes out.*

For Personal Accounts: *Debit the receiver, credit the giver.*

For Nominal Accounts: *Debit all expenses and losses, credit all income and gains.*

Basic Principles of Accounting

There is no single list of accounting policies which are applicable to all circumstances. The differing circumstances in which enterprises operate in a situation of diverse and complex economic activity make alternative accounting principles and methods of applying those principles acceptable. The choice of the appropriate accounting principles and the methods of applying those principles in the specific circumstances of each enterprise calls for considerable judgement by the management of the enterprise. The following are examples of the areas in which different accounting policies may be adopted by different enterprises:

(a) Methods of depreciation, depletion and amortisation

(b) Treatment of expenditure during construction

(c) Conversion or translation of foreign currency items

(d) Valuation of inventories

(e) Treatment of goodwill

(f) Valuation of investments

(g) Treatment of retirement benefits

(h) Recognition of profit on long-term contracts

(i) Valuation of fixed assets

(j) Treatment of contingent liabilities.

The following is a list of the ten main accounting principles and guidelines together with a highly condensed explanation of each.

1. Economic Entity Assumption

The accountant keeps all of the business transactions of a sole proprietorship separate from the business owner's personal transactions. For legal purposes, a sole proprietorship and its owner are considered to be one entity, but for accounting purposes they are considered to be two separate entities.

2. Monetary Unit Assumption

Economic activity is measured in Rupees or any other currency, and only transactions that can be expressed in such monetary unit are recorded.

3. Time Period Assumption

This accounting principle assumes that it is possible to report the complex and ongoing activities of a business in relatively short, distinct time intervals such as annually, semi-annually, etc. It is *imperative* that the time interval (or period of time) be shown in the heading of each statement of profit & loss, statement of changes in equity, and statement of cash flows. Labelling one of these financial statements with "December 31" is not good enough–the reader needs to know if the statement covers the *one week* ended December 31, 2015 the *month* ended December 31, 2015 the *three months* ended December 31, 2015 or the *year ended* December 31, 2015.

4. Cost Principle

From an accountant's point of view, the term "cost" refers to the amount spent (cash or the cash equivalent) when an item was *originally* obtained, whether that purchase happened last year or thirty years ago. Traditionally, accounts were completely based on *historical* costs. However there has been a gradual shift towards fair value accounting which we will discuss in forthcoming chapters.

5. Full Disclosure Principle

If certain information is important to an investor or lender using the financial statements, that information should be disclosed within the statement or in the notes to the statement. It is because of this basic accounting principle that numerous pages of schedules and annexure are often attached to financial statements. A company usually lists its significant accounting policies as the first note to its financial statements.

6. Going Concern Principle

This accounting principle assumes that a company will continue to exist long enough to carry out its objectives and commitments and will not liquidate in the foreseeable future. If the company's financial situation is such that the accountant believes the company will *not* be able to continue on, the accountant is required to disclose this assessment. The going concern principle allows the company to defer some of its prepaid expenses until future accounting periods.

7. Matching Principle

This accounting principle requires companies to use the accrual basis of accounting. The matching principle requires that expenses be matched with revenues. For example, sales commission's expense should be reported in the period when the sales were made (and not reported in the period when the commissions were paid). Wages to employees are reported as an expense in the week when the employees worked and not in the week when the employees are paid.

8. Revenue Recognition Principle

Under the accrual basis of accounting (as opposed to the cash basis of accounting), revenues are recognized as soon as a product has been sold or a service has been performed, regardless of when the money is actually received.

9. Materiality

Because of this basic accounting principle or guideline, an accountant might be allowed to violate another accounting principle if an amount is insignificant. Professional judgement is needed to decide whether an amount is insignificant or immaterial.

10. Conservatism

If a situation arises where there are two acceptable alternatives for reporting an item, conservatism directs the accountant to choose the alternative that will result in less net income and/or less asset amount. Accountants are expected to be unbiased and objective. The basic accounting principle of conservatism leads accountants to anticipate or disclose losses, but it

does not allow a similar action for gains. For example, *potential* losses from lawsuits will be reported on the financial statements or in the notes, but *potential* gains will not be reported.

The Conceptual Framework for Financial Reporting

The Framework deals with:

- **(a)** The objective of financial reporting;
- **(b)** The qualitative characteristics of useful financial information;
- **(c)** The definition, recognition and measurement of the elements from which financial statements are constructed;
- **(d)** Concepts of capital and capital maintenance.

Elements of Financial Statements include Assets, Liabilities, Equity, Income and Expenses.

Recognition of the Elements of Financial Statements

The recognition is based on the probability of the future economic benefits and reliability of measurement. It involves the recognition of assets, liabilities, income and expense.

Measurement of the Elements of Financial Statements

Measurement involves assigning monetary amounts at which the elements of the financial statements are to be recognised and reported. The Framework acknowledges that a variety of measurement bases are used today to different degrees and in varying combinations in financial statements, including: Historical cost; Current cost; Net realisable (settlement) value and Present value (discounted)

Historical cost is the measurement basis most commonly used today, but it is usually combined with other measurement bases. The Framework does not include concepts or principles for selecting which measurement basis should be used for particular elements of financial statements or in particular circumstances. The qualitative characteristics do provide some guidance, however.

(d) Concepts of capital and capital maintenance.

The concept of capital maintenance is concerned with how an entity defines the capital that it seeks to maintain. It provides the linkage between the concepts of capital and the concepts of profit because it provides the point of reference by which profit is measured; it is a prerequisite for distinguishing between an entity's return on capital and its return of capital; only inflows of assets in excess of amounts needed to maintain capital may be regarded as profit and therefore as a return on capital. Hence, profit is the residual amount that remains after expenses (including capital maintenance adjustments, where appropriate) have been deducted from income. If expenses exceed income the residual amount is a loss.

Users of financial statement and their information needs

The Framework notes that financial statements cannot provide all the information that users may need to make economic decisions. For one thing, financial statements show the financial effects of past events and transactions, whereas the decisions that most users of financial statements have to make relate to the future. Further, financial statements provide only a limited amount of the non-financial information needed by users of financial statements. While all of the information needs of these user groups cannot be met by financial statements, there are information needs that are common to all users, and general purpose financial statements focus on meeting these needs.

Responsibility for Financial Statements

The management of an enterprise has the primary responsibility for preparing and presenting the enterprise's financial statements.

The Cost Constraint on useful Financial Reporting

Cost is a pervasive constraint on the information that can be provided by financial reporting. Reporting financial information imposes cost, and it is important that those costs are justified by the benefits of reporting that information. There are several types of costs and benefits to consider.

Elements of Financial Statements

a. Assets:

- **Definition**: An asset is a resource controlled by the entity as a result of past events and from which future economic benefits are expected to flow to the entity.
- **Recognition:** When it is probable that future economic benefits will flow to and the asset has cost or value that can be reliably measured.

b. Liabilities:

- **Definition**: It is the present obligation of an entity arising from past events, the settlement of which is expected to result in an outflow from the entity of resources embodying economic benefits.
- **Recognition:** When it is probable that an outflow of resources embodying economic benefits will result from the settlement of a present obligation and the amount at which the settlement will take place can be reliably measured.

c. Equity

- **Definition**: it is the residual interest in the asset of the entity after deducting all its liability.

d. Income

- **Definition:** Income is the increase in economic benefits during the accounting period in the form of inflows or enhancements of assets or decreases of liabilities those results in increase in equity, other than those relating to contribution from equity participants. It encompasses both revenue and gains.
- **Recognition:** When an increase in the future economic benefits related to an increase in an asset or decrease in a liability has arisen that can be reliably measured.

e. **Expenses**

- **Definition:** It is the decrease in economic benefits during the accounting period in the form of outflows or depletion of assets or incurrence of liabilities those results in decrease in equity, other than those relating to contribution to equity participants. It encompasses both losses and expenses that arise in the course of ordinary activity of the entity.

- **Recognition:** When an decrease in the future economic benefits related to an decrease in an asset or increase in a liability has arisen that can be reliably measured

The Principal Assumptions in Preparation of Financial Statements

- Going Concern
- Consistency
- Accruals
- Materiality
- Aggregation
- Offsetting

Classification of Accounting Standards for Study Purpose

These Accounting Standards are numbered according to their issuance. However, they may be classified for better understanding as follows:

A. Presentation & Disclosure Standards • Framework for the Preparation and Presentation of Financial Statements • AS 1 Disclosure of Accounting Policies • AS 3 Cash Flow Statements • AS 4 Contingencies and Events Occurring After the Balance Sheet Date • AS 5 Net Profit or Loss for the Period, Prior Period Items and Changes in Accounting Policies • AS 11 The Effects of Changes in Foreign Exchange Rates • AS 17 Segment Reporting • AS 18 Related Party Disclosures • AS 20 Earnings Per Share • AS 25 Interim Financial Reporting
B. Financial Reporting by Group Entities • AS 14 Accounting for Amalgamations • AS 21 Consolidated Financial Statements

• AS 23 Accounting for Investments in Associates in Consolidated Financial Statements • AS 27 Financial Reporting of Interests in Joint Ventures
C. Recognition, Measurement, Presentation & Disclosure of Assets • AS 2 Valuation of Inventories • AS 10 Property, Plant and Equipment • AS 12 Accounting for Government Grants • AS 13 Accounting for Investments • AS 16 Borrowing Costs • AS 19 Leases • AS 24 Discontinuing Operations • AS 26 Intangible Assets • AS 28 Impairment of Assets
D. Recognition, Measurement, Presentation & Disclosure of Revenue • AS 7 Construction Contracts • AS 9 Revenue Recognition
E. Recognition, Measurement, Presentation & Disclosure of Expenses & Liabilities • AS 15 Employee Benefits • AS 29 - Provisions, Contingent Liabilities and Contingent Assets • AS 22- Accounting for Taxes on Income

SUMMARY OF ACCOUNTING STANDARDS

A. Presentation & Disclosure Standards

A.1. AS 1: Disclosure of Accounting Policies

AS 1 deals with the disclosure of significant accounting policies which are followed in preparing and presenting financial statements. However, it should be noted that disclosure of accounting policies or of changes therein cannot remedy wrong or inappropriate treatment of the item in the books of accounts

Important Term

Accounting Policies: Accounting Policies refer to the specific accounting principles and methods of applying those principles adopted by the enterprise in the preparation and presentation of financial statements.

Consideration in Selection of Accounting Policies

There is no single list of accounting policies which are applicable to all circumstances. The choice of the appropriate accounting principles and the methods of applying those principles in the specific circumstances of each enterprise. Primary Consideration is that the financial statements should represent true and fair view. Prudence, Substance over form, Materiality are major determinants in achieving the primary consideration.

Fundamental Accounting Assumptions

There are three generally accepted as fundamental accounting assumptions: Going Concern, Consistency and Accrual.

Disclosure Requirements

- All significant accounting policies adopted in the preparation and presentation of financial statements should be disclosed.
- The disclosure of the significant accounting policies as such should form part of the financial statements and the significant accounting policies should normally be disclosed in one place.
- Any change in the accounting policies which has a material effect in the current period or which is reasonably expected to have a material effect in later periods should be disclosed. In the case of a change in accounting policies which has a material effect in the current period, the amount by which any item in the financial statements is affected by

such change should also be disclosed to the extent ascertainable. Where such amount is not ascertainable, wholly or in part, the fact should be indicated.

- If the fundamental accounting assumptions, viz. Going Concern, Consistency and Accrual are followed in financial statements, specific disclosure is not required. If a fundamental accounting assumption is not followed, the fact should be disclosed.

A.2. AS 3: Cash Flow Statements

AS 3 is not mandatory for Level II, III & IV enterprises. Large enterprises (Level-I) should prepare a cash flow statement and should present it for each period for which financial statements are presented. It is useful in providing users of financial statements with a basis to assess the ability of the enterprise to generate cash and cash equivalent and also timing of cash flows are important to make economic decisions. This statement deals with the inflow and outflow of cash and cash equivalent, where cash comprises of cash in hand and demand deposits with banks and cash equivalents are short term, highly liquid investments that are readily convertible into known amounts of cash and which are subject to an insignificant risk of changes in value.

For the purpose of the standard, cash flows are presented categorised as those derived from:

- *Operating activities* which are the principal revenue-producing activities of the enterprise and other activities that are not investing or financing activities;
- *Investing activities* which are the acquisition and disposal of long-term assets and other investments not included in cash equivalents; and
- *Financing activities* which are activities that result in changes in the size and composition of the owners' capital and borrowings of the enterprise.

Reporting of Cash Flows

An enterprise should report cash flows from **operating activities** using either:

(a) The ***direct method***, whereby major classes of gross cash receipts and gross cash payments are disclosed; or

(b) the ***indirect method***, whereby net profit or loss is adjusted for the effects of transactions of a non-cash nature, any deferrals or accruals of past or future operating cash receipts or payments, and items of income or expense associated with investing or financing cash flows.

An enterprise should report separately major classes of gross cash receipts and gross cash payments arising from investing and financing activities. However, the cash flows arising from the following operating, investing or financing activities may be reported on a net basis:

(a) cash receipts and payments on behalf of customers when the cash flows reflect the activities of the customer rather than those of the enterprise for instance the acceptance and repayment of demand deposits by a bank or rents collected on behalf of, and paid over to, the owners of properties.; and
(b) Cash receipts and payments for items in which the turnover is quick, the amounts are large, and the maturities are short for instance cash receipts and payments for the acceptance and repayment of deposits with a fixed maturity date or cash advances and loans made to customers and the repayment of those advances and loans.

The cash flows associated with extraordinary items should be classified as arising from operating, investing or financing activities as appropriate and separately disclosed.

Cash flows from interest and dividends received and paid and from taxes on income should each be disclosed separately.

Reporting of Foreign Currency Cash Flows

Cash flows arising from transactions in a foreign currency should be recorded in an enterprise's reporting currency by applying to the foreign currency amount the exchange rate between the reporting currency and the foreign currency at the date of the cash flow. A rate that approximates the actual rate may be used if the result is substantially the same as would arise if the rates at the dates of the cash flows were used. The effect of changes in exchange rates on cash and cash equivalents held in a foreign currency should be reported as a separate part of the reconciliation of the changes in cash and cash equivalents during the period.

Reporting for Investments in Subsidiaries, Associates and Joint Ventures

When accounting for an investment in an associate or a subsidiary or a joint venture, an investor restricts its reporting in the cash flow statement to the cash flows between itself and the investee/joint venture, for example, cash flows relating to dividends and advances.

The aggregate cash flows arising from acquisitions and from disposals of subsidiaries or other business units should be presented separately and classified as investing activities. An enterprise should disclose, in aggregate, in respect of both acquisition and disposal of subsidiaries or other business units during the period each of the following:

- the total purchase or disposal consideration; and
- The portion of the purchase or disposal consideration discharged by means of cash and cash equivalents.

Other Disclosures

- An enterprise should disclose the components of cash and cash equivalents and should present a reconciliation of the amounts in its cash flow statement with the equivalent items reported in the balance sheet
- An enterprise should disclose, together with a commentary by management, the amount of significant cash and cash equivalent balances held by the enterprise that are not available for use by it.

A.3. AS 4 Contingencies and Events Occurring after Balance Sheet Date

This standard deals with

- Contingencies which is a condition or situation, the ultimate outcome of which, gain or loss, will be known or determined only on the occurrence, or non-occurrence, of one or more uncertain future events, and
- Events occurring after the balance sheet date which are those significant events, both favourable and unfavourable, that occur between the balance sheet date and the date on which the financial statements are approved... Two types of events can be identified:
    - those which provide further evidence of conditions that existed at the balance sheet date; and

- Those which are indicative of conditions that arose subsequent to the balance sheet date...

Treatment of Contingencies and related Disclosure

The amount of a **contingent loss** should be provided for by a charge in the statement of profit and loss in following circumstances only:

A. if it is probable that future events will confirm that, after taking into account any related probable recovery, an asset has been impaired or a liability has been incurred as at the balance sheet date, and
B. A reasonable estimate of the amount of the resulting loss can be made.

The existence of a contingent loss should be disclosed in the financial statements if either of the conditions mentioned above is not met, unless the possibility of a loss is remote.

The **Contingent gains** ***should not*** be recognized in the financial statements.

The following the following information should be disclosed where the above conditions are met:

(a) the nature of the contingency;
(b) the uncertainties which may affect the future outcome;
(c) An estimate of the financial effect, or a statement that such an estimate cannot be made.

Treatment of Events Occurring after the Balance Sheet Date

Assets and liabilities should be adjusted for events occurring after the balance sheet date that provide additional evidence to assist the estimation of amounts relating to conditions existing at the balance sheet date or that indicate that the fundamental accounting assumption of going concern (i.e., the continuance of existence or substratum of the enterprise) is not appropriate.

Disclosure should be made in the report of the approving authority of those events occurring after the balance sheet date that represent material changes and commitments affecting the financial position of the enterprise. If disclosure of events occurring after the balance sheet date in the report of the approving authority, the following information should be provided:

(a) The nature of the event;

(b) An estimate of the financial effect, or a statement that such an estimate cannot be made.

A.4. AS 5: Net Profit or Loss for the Period, Prior Period Items and Changes in Accounting Policies

The objective of this Standard is to prescribe the classification and disclosure of certain items in the statement of profit and loss so that all enterprises prepare and present such a statement on a uniform basis. It is applied by an enterprise in presenting profit or loss from ordinary activities, extraordinary items and prior period items in the statement of profit and loss, in accounting for changes in accounting estimates, and in disclosure of changes in accounting policies.

Important Terms:

Ordinary activities are any activities which are undertaken by an enterprise as part of its business and such related activities in which the enterprise engages in furtherance of, incidental to, or arising from, these activities.

Extraordinary items are income or expenses that arise from events or transactions that are clearly distinct from the ordinary activities of the enterprise and, therefore, are not expected to recur frequently or regularly.

Prior period items are income or expenses which arise in the current period as a result of errors or omissions in the preparation of the financial statements of one or more prior periods.

Accounting policies are the specific accounting principles and the methods of applying those principles adopted by an enterprise in the preparation and presentation of financial statements.

Key Points

- The net profit or loss for the period comprises of profit or loss from ordinary activities and (extraordinary items that forms components, each of which should be disclosed on the face of the statement of profit and loss.
- Extraordinary items should be disclosed in the statement of profit and loss as a part of net profit or loss for the period. The nature and the amount of each extraordinary item should

be separately disclosed in the statement of profit and loss in a manner that its impact on current profit or loss can be perceived.

- When items of income and expense within profit or loss from ordinary activities are of such size, nature or incidence that their disclosure is relevant to explain the performance of the enterprise for the period, the nature and amount of such items should be disclosed separately.
- The nature and amount of prior period items should be separately disclosed in the statement of profit and loss in a manner that their impact on the current profit or loss can be perceived.
- The effect of a change in an accounting estimate should be included in the determination of net profit or loss in the period of the change, if the change affects the period only or the period of the change and future periods, if the change affects both.
- The effect of a change in an accounting estimate should be classified using the same classification in the statement of profit and loss as was used previously for the estimate.
- The nature and amount of a change in an accounting estimate which has a material effect in the current period, or which is expected to have a material effect in subsequent periods, should be disclosed. If it is impracticable to quantify the amount, this fact should be disclosed.
- A change in an accounting policy should be made only if the adoption of a different accounting policy is required by statute or for compliance with an accounting standard or if it is considered that the change would result in a more appropriate presentation of the financial statements of the enterprise.
- Any change in an accounting policy which has a material effect should be disclosed. The impact of, and the adjustments resulting from, such change, if material, should be shown in the financial statements of the period in which such change is made, to reflect the effect of such change. Where the effect of such change is not ascertainable, wholly or in part, the fact should be indicated.

A.5. AS 11: The Effects of Changes in Foreign Exchange Rates

This Standard should be applied in accounting for transactions in foreign currencies; and in translating the financial statements of foreign operations.

Key Definitions

Exchange difference is the difference resulting from reporting the same number of units of a foreign currency in the reporting currency at different exchange rates.

Foreign operation is a subsidiary, associate, joint venture or branch of the reporting enterprise, the activities of which are based or conducted in a country other than the country of the reporting enterprise.

Forward exchange contract means an agreement to exchange different currencies at a forward rate.

Integral foreign operation is a foreign operation, the activities of which are an integral part of those of the reporting enterprise.

Non-integral foreign operation is a foreign operation that is not an integral foreign operation.

Monetary items are money held and assets and liabilities to be received or paid in fixed or determinable amounts of money.

Non-monetary items are assets and liabilities other than monetary items

Net investment in a non-integral foreign operation is the reporting enterprise's share in the net assets of that operation.

Reporting currency is the currency used in presenting the financial statements.

Key Points

- A foreign currency transaction should be recorded, on initial recognition in the reporting currency, by applying to the foreign currency amount the exchange rate between the reporting currency and the foreign currency at the date of the transaction.
- On subsequent date:
  - foreign currency monetary items should be reported using the closing rate;
  - non-monetary items which are carried in terms of historical cost denominated in a foreign currency should be reported using the exchange rate at the date of the transaction; and

- Non-monetary items which are carried at fair value or other similar valuation denominated in a foreign currency should be reported using the exchange rates that existed when the values were determined.

- Exchange differences arising on the settlement of monetary items or on reporting an enterprise's monetary items at rates different from those at which they were initially recorded during the period, or reported in previous financial statements, should be recognized as income or as expenses in the period in which they arise.
- Exchange differences arising on a monetary item that, in substance, forms part of an enterprise's net investment in a non-integral foreign operation should be accumulated in a foreign currency translation reserve in the enterprise's financial statements until the disposal of the net investment, at which time they should be recognized as income or as expenses.
- The financial statements of an integral foreign operation should be translated using the principles and procedures as if the transactions of the foreign operation had been those of the reporting enterprise itself.
- In translating the financial statements of a non-integral foreign operation for incorporation in its financial statements, the reporting enterprise should use the following procedures:
  (a) the assets and liabilities, both monetary and non-monetary, of the non-integral foreign operation should be translated at the closing rate;
  (b) income and expense items of the non-integral foreign operation should be translated at exchange rates at the dates of the transactions; and
  (c) All resulting exchange differences should be accumulated in a foreign currency translation reserve until the disposal of the net investment.
- On the disposal of a non-integral foreign operation, the cumulative amount of the exchange differences which have been deferred and which relate to that operation should be recognized as income or as expenses
- When there is a change in the classification of a foreign operation, the translation procedures applicable to the revised classification should be applied from the date of the change in the classification.

- The premium or discount arising at the inception of a forward exchange contract should be amortized as expense or income over the life of the contract. Exchange differences on such a contract should be recognized in the statement of profit and loss in the reporting period in which the exchange rates change. Any profit or loss arising on cancellation or renewal of such a forward exchange contract should be recognized as income or as expense for the period.
- An enterprise should disclose the amount of exchange differences included in the net profit or loss for the period; and net exchange differences accumulated in foreign currency translation reserve as a separate component of shareholders' funds, and a reconciliation of the amount of such exchange differences at the beginning and end of the period.

A.6. AS 17 Segment Reporting

The objective of this Standard is to establish principles for reporting financial information, about the different types of products and services an enterprise produces and the different geographical areas in which it operates. This Standard should be applied in presenting general purpose financial statements. Though this Standard is not mandatory for Level II, III & IV entities, they are encouraged to follow it.

If a single financial report contains both consolidated financial statements and the separate financial statements of the parent, segment information need be presented only on the basis of the consolidated financial statements.

Important Terms

A ***business segment*** is a distinguishable component of an enterprise that is engaged in providing an individual product or service or a group of related products or services and that is subject to risks and returns that are different from those of other business segments. Factors that should be considered in determining whether products or services are related include:

(a) the nature of the products or services;
(b) the nature of the production processes;
(c) the type or class of customers for the products or services;

(d) the methods used to distribute the products or provide the services; and
(e) If applicable, the nature of the regulatory environment, for example, banking, insurance, or public utilities.

A ***geographical segment*** is a distinguishable component of an enterprise that is engaged in providing products or services within a particular economic environment and that is subject to risks and returns that are different from those of components operating in other economic environments. Factors that should be considered in identifying geographical segments include:

(a) similarity of economic and political conditions;
(b) relationships between operations in different geographical areas;
(c) proximity of operations;
(d) special risks associated with operations in a particular area;
(e) exchange control regulations; and
(f) The underlying currency risks.

A ***reportable segment*** is a business segment or a geographical segment identified on the basis of foregoing definitions for which segment information is required to be disclosed by this Standard.

Key Points

- The dominant source and nature of risks and returns of an enterprise should govern whether its primary segment reporting format will be business segments or geographical segments. If the risks and returns of an enterprise are affected predominantly by differences in the products and services it produces, its primary format for reporting segment information should be business segments, with secondary information reported geographically. Similarly, if the risks and returns of the enterprise are by the fact that it operates in different countries or other geographical areas, its primary format for reporting segment information should be geographical segments, with secondary information reported for groups of related products and services.
- Internal organization and management structure of an enterprise and its system of internal financial reporting to the board of directors and the chief executive officer should normally be the basis for identifying the predominant source and nature of risks and differing rates of return facing the enterprise.

- Business and geographical segments of an enterprise for external reporting purposes should be those organizational units for which information is reported to the board of directors and to the chief executive officer for the purpose of evaluating the unit's performance and for making decisions about future allocations of resources.
- A business segment or geographical segment should be identified as a reportable segment if:

(a) its revenue from sales to external customers and from transactions with other segments is 10 per cent or more of the total revenue, external and internal, of all segments; or

(b) its segment result, whether profit or loss, is 10 per cent or more of –

(i) the combined result of all segments in profit, or

(ii) the combined result of all segments in loss, whichever is greater in absolute amount; or

(c) Its segment assets are 10 per cent or more of the total assets of all segments.

- Other segments may also be reported separately if desired by the management.
- If total external revenue attributable to reportable segments constitutes less than 75 per cent of the total enterprise revenue, additional segments should be identified as reportable segments, even if they do not meet the 10 per cent thresholds in paragraph 27, until at least 75 per cent.
- Segment information should be prepared in conformity with the accounting policies adopted for preparing and presenting the financial statements of the enterprise as a whole.
- Assets and liabilities that relate jointly to two or more segments should be allocated to segments if, and only if, their related revenues and expenses also are allocated to those segments.
- An enterprise should disclose the following for each reportable segment:
- segment revenue, classified into segment revenue from sales to external customers and segment revenue from transactions with other segments;
- segment result;
- total carrying amount of segment assets;
- total amount of segment liabilities;

- total cost incurred during the period to acquire segment assets that are expected to be used during more than one period (tangible and intangible fixed assets);
- total amount of expense included in the segment result for depreciation and amortisation in respect of segment assets for the period; and
- Total amount of significant non-cash expenses, other than depreciation and amortisation in respect of segment assets that were included in segment expense and, therefore, deducted in measuring segment result.
- An enterprise should present a reconciliation between the information disclosed for reportable segments and the aggregated information in the enterprise financial statements. In presenting the reconciliation, segment revenue should be reconciled to enterprise revenue; segment result should be reconciled to enterprise net profit or loss; segment assets should be reconciled to enterprise assets; and segment liabilities should be reconciled to enterprise liabilities.
- Changes in accounting policies adopted for segment reporting that have a material effect on segment information should be disclosed. Such disclosure should include a description of the nature of the change, and the financial effect of the change if it is reasonably determinable.

A.7. AS 18 Related Party Disclosures

The objective of this Standard is to establish requirements for disclosure of related party relationships; and transactions between a reporting enterprise and its related parties. This Standard should be applied in reporting related party relationships and transactions between a reporting enterprise and its related parties. The requirements of this Standard apply to the financial statements of each reporting enterprise as also to consolidate financial statements presented by a holding entity.

Important terms

Related party - parties are considered to be related if at any time during the reporting period one party has the ability to control the other party or exercise significant influence over the other party in making financial and/or operating decisions.

Related party transaction - a transfer of resources or obligations between related parties, regardless of whether or not a price is charged.

Key management personnel - those persons who have the authority and responsibility for planning, directing and controlling the activities of the reporting enterprise.

Relative – in relation to an individual, means the spouse, son, daughter, brother, sister, father and mother who may be expected to influence, or be influenced by, that individual in his/her dealings with the reporting enterprise.

Fellow subsidiary - an entity is considered to be a fellow subsidiary of another entity if both are subsidiaries of the same holding entity.

State-controlled enterprise - an enterprise which is under the control of the Central Government and/or any State Government.

Key Points

- Name of the related party and nature of the related party relationship where control exists should be disclosed irrespective of whether or not there have been transactions between the related parties.
- If there have been transactions between related parties, during the existence of a related party relationship, the reporting enterprise should disclose the following:
  - (a) the name of the transacting related party;
  - (b) a description of the relationship between the parties;
  - (c) a description of the nature of transactions;
  - (d) volume of the transactions either as an amount or as an appropriate proportion;
  - (e) any other elements of the related party transactions necessary for an understanding of the financial statements;
  - (f) the amounts or appropriate proportions of outstanding items pertaining to related parties at the balance sheet date and provisions for doubtful debts due from such parties at that date; and
  - (g) amounts written off or written back in the period in respect of debts due from or to related parties

- Related party disclosure requirements as laid down in this Standard do not apply in circumstances where providing such disclosures would conflict with the reporting enterprise's duties of confidentiality as specifically required in terms of a statute or by any regulator or similar competent authority.
- No disclosure is required in consolidated financial statements in respect of intra-group transactions
- No disclosure is required in the financial statements of state-controlled enterprises as regards related party relationships with other state-controlled enterprises and transactions with such enterprises.
- Items of a similar nature may be disclosed in aggregate by type of related party except when separate disclosure is necessary for an understanding of the effects of related party transactions on the financial statements of the reporting enterprise.

A.8. AS 20 Earnings per Share

The objective of this Standard is to prescribe principles for the determination and presentation of earnings per share which will improve comparison of performance among different enterprises for the same period and among different accounting periods for the same enterprise. This Standard is not to be applied by level II, III & IV entities. Even in Level I entities, very few entities like co-operatives will have shares and hence would be required to apply this Standard.

An ***equity share*** is a share other than a preference share.

A ***preference share*** is a share carrying preferential rights to dividends and repayment of capital.

A ***potential equity share*** is a financial instrument or other contract that entitles, or may entitle, its holder to equity shares.

Share warrants or options are financial instruments that give the holder the right to acquire equity shares.

Key Points

- An enterprise should present basic and diluted earnings per share on the face of the statement of profit and loss for each class of equity shares that has a different right to

share in the net profit for the period. An enterprise should present basic and diluted earnings per share with equal prominence for all periods presented.

- Basic earnings per share should be calculated by dividing the net profit or loss for the period attributable to equity shareholders by the weighted average number of equity shares outstanding during the period
- For the purpose of calculating basic earnings per share, the net profit or loss for the period attributable to equity shareholders should be the net profit or loss for the period after deducting preference dividends and any attributable tax thereto for the period.
- For the purpose of calculating basic earnings per share, the number of equity shares should be the weighted average number of equity shares outstanding during the period.
- The weighted average number of equity shares outstanding during the period and for all periods presented should be adjusted for events, other than the conversion of potential equity shares that have changed the number of equity shares outstanding, without a corresponding change in resources.
- For the purpose of calculating diluted earnings per share, the net profit or loss for the period attributable to equity shareholders and the weighted average number of shares outstanding during the period should be adjusted for the effects of all dilutive potential equity shares.
- For the purpose of calculating diluted earnings per share, the amount of net profit or loss for the period attributable to equity shareholders, should be adjusted by the following, after taking into account any attributable change in tax expense for the period:
  (a) any dividends on dilutive potential equity shares which have been deducted in arriving at the net profit attributable to equity shareholders
  (b) interest recognised in the period for the dilutive potential equity shares; and
  (c) Any other changes in expenses or income that would result from the conversion of the dilutive potential equity shares.
- For the purpose of calculating diluted earnings per share, the number of equity shares should be the aggregate of the weighted average number of equity, and the weighted average number of equity shares which would be issued on the conversion of all the dilutive potential equity shares into equity shares. Dilutive potential equity shares should

be deemed to have been converted into equity shares at the beginning of the period or, if issued later, the date of the issue of the potential equity shares.

- For the purpose of calculating diluted earnings per share, an enterprise should assume the exercise of dilutive options and other dilutive potential equity shares of the enterprise. The assumed proceeds from these issues should be considered to have been received from the issue of shares at fair value. The difference between the number of shares issuable and the number of shares that would have been issued at fair value should be treated as an issue of equity shares for no consideration.
- Potential equity shares should be treated as dilutive when, and only when, their conversion to equity shares would decrease net profit per share from continuing ordinary operations.
- If the number of equity or potential equity shares outstanding increases as a result of a bonus issue or share split or decreases as a result of a reverse share split (consolidation of shares), the calculation of basic and diluted earnings per share should be adjusted for all the periods presented. If these changes occur after the balance sheet date but before the date on which the financial statements are approved by the board of directors, the per share calculations for those financial statements and any prior period financial statements presented should be based on the new number of shares. When per share calculations reflect such changes in the number of shares, that fact should be disclosed.

A.9. AS 25 Interim Financial Reporting

The objective of this Standard is to prescribe the minimum content of an interim financial report and to prescribe the principles for recognition and measurement in complete or condensed financial statements for an interim period. This Standard does not mandate which enterprises should be required to present interim financial reports, how frequently, or how soon after the end of an interim period. If an enterprise is required or elects to prepare and present an interim financial report, it should comply with this Standard.

Important Terms

Interim period is a financial reporting period shorter than a full financial year.

Interim financial report means a financial report containing either a complete set of financial statements or a set of condensed financial statements (as described in this Standard) for an interim period.

Important Points

- An interim financial report should include, at a minimum, the following components:
  - (a) condensed balance sheet;
  - (b) condensed statement of profit and loss;
  - (c) condensed cash flow statement; and
  - **(d)** Selected explanatory notes.
- If an enterprise prepares and presents a complete set of financial statements in its interim financial report, the form and content of those statements should conform to the requirements as applicable to annual complete set of financial statements.
- An enterprise should include the following information, as a minimum, in the notes to its interim financial statements, if material and if not disclosed elsewhere in the interim financial report:
  - (a) a statement that the same accounting policies are followed in the interim financial statements as those followed in the most recent annual financial statements or, if those policies have been changed, a description of the nature and effect of the change;
  - (b) explanatory comments about the seasonality of interim operations;
  - (c) the nature and amount of items affecting assets, liabilities, equity, net income, or cash flows that are unusual because of their nature, size, or incidence
  - (d) The nature and amount of changes in estimates of amounts reported in prior interim periods of the current financial year or changes in estimates of amounts reported in prior financial years, if those changes have a material effect in the current interim period;
  - (e) issuances, buy-backs, repayments and restructuring of debt, equity and potential equity shares;
  - (f) dividends, aggregate or per share (in absolute or percentage terms), separately for equity shares and other shares;

(g) segment revenue, segment capital employed (segment assets minus segment liabilities) and segment result

(h) material events subsequent to the end of the interim period that have not been reflected in the financial statements for the interim period;

(i) the effect of changes in the composition of the enterprise during the interim period, such as amalgamations, acquisition or disposal of subsidiaries and long-term investments, restructurings, and discontinuing operations; and

(j) Material changes in contingent liabilities since the last annual balance sheet date.

- Interim reports should include interim financial statements (condensed or complete) for periods as follows:
  (a) balance sheet as of the end of the current interim period and a comparative balance sheet as of the end of the immediately preceding financial year;
  (b) statements of profit and loss for the current interim period and cumulatively for the current financial year to date, with comparative statements of profit and loss for the comparable interim periods (current and year-to-date) of the immediately preceding financial year;
  (c) Cash flow statement cumulatively for the current financial year to date, with a comparative statement for the comparable year to-date period of the immediately preceding financial year.
- In deciding how to recognise, measure, classify, or disclose an item for interim financial reporting purposes, materiality should be assessed in relation to the interim period financial data.
- If an estimate of an amount reported in an interim period is changed significantly during the final interim period of the financial year but a separate financial report is not prepared and presented for that final interim period, the nature and amount of that change in estimate should be disclosed in a note to the annual financial statements for that financial year.
- Revenues that are received seasonally or occasionally within a financial year should not be anticipated or deferred as of an interim date if anticipation or deferral would not be appropriate at the end of the enterprise's financial year.

- Costs that are incurred unevenly during an enterprise's financial year should be anticipated or deferred for interim reporting purposes if, and only if, it is also appropriate to anticipate or defer that type of cost at the end of the financial year.

B. Standards dealing with Financial Reporting by Group Entities

Standards in this category are:

AS 14 Accounting for Amalgamation

AS 21 Consolidated Financial Statements

AS 23 Accounting for Investments in Associates in Consolidated Financial Statements

AS 27 Financial Reporting in Interests in Joint Ventures

B.1. AS 14 Accounting for Amalgamation

This standard deals with accounting for amalgamations and the treatment of any resultant goodwill or reserves.

Important Terms

Amalgamation means an amalgamation pursuant to the provisions of the Companies Act, 2013 or any other statute which may be applicable to companies.

Pooling of interests is a method of accounting for amalgamations the object of which is to account for the amalgamation as if the separate businesses of the amalgamating companies were intended to be continued by the transferee entity. Accordingly, only minimal changes are made in aggregating the individual financial statements of the amalgamating companies.

Amalgamation in the nature of merger is an amalgamation which satisfies all the following conditions.

(i) All the assets and liabilities of the transferor entity become, after amalgamation, the assets and liabilities of the transferee entity.

(ii) Shareholders holding not less than 90% of the face value of the shares of the transferor entity (other than the equity shares already held therein, immediately before the amalgamation, by the transferee entity or its subsidiaries or their nominees) become equity shareholders of the transferee entity by virtue of the amalgamation.

(iii) The consideration for the amalgamation receivable by those equity shareholders of the transferor entity who agree to become equity shareholders of the transferee entity is discharged by the transferee entity wholly by the issue of equity shares in the transferee entity, except that cash may be paid in respect of any fractional shares.

(iv) The business of the transferor entity is intended to be carried on, after the amalgamation, by the transferee entity.

(v) No adjustment is intended to be made to the book values of the assets and liabilities of the transferor entity when they are incorporated in the financial statements of the transferee entity except to ensure uniformity of accounting policies.

Amalgamation in the nature of purchase is an amalgamation which does not satisfy any one or more of the conditions of amalgamation in nature of merger.

Consideration for the amalgamation means the aggregate of the shares and other securities issued and the payment made in the form of cash or other assets by the transferee entity to the shareholders of the transferor entity.

Key points

- An amalgamation may be either an amalgamation in the nature of merger, or an amalgamation in the nature of purchase
- When an amalgamation is considered to be an amalgamation in the nature of merger, it should be accounted for under the pooling of interests method.
- In pooling of interest method:
    - The assets, liabilities and reserves (whether capital or revenue or arising on revaluation) of the transferor entity should be recorded at their existing carrying amounts and in the same form as at the date of the amalgamation. The balance of the Profit and Loss Account of the transferor entity should be aggregated with the corresponding balance of the transferee entity or transferred to the General Reserve, if any
    - A uniform set of accounting policies should be adopted following the amalgamation. The effects on the financial statements of any changes in accounting policies should be reported in accordance with AS 5

- The difference between the amount recorded as share capital issued (plus any additional consideration in the form of cash or other assets) and the amount of share capital of the transferor entity should be adjusted in reserves.

- When an amalgamation is considered to be an amalgamation in the nature of purchase, it should be accounted for under the purchase method.
- In purchase method:
    - The assets and liabilities of the transferor entity should be incorporated at their existing carrying amounts or, alternatively, the consideration should be allocated to individual identifiable assets and liabilities on the basis of their fair values at the date of amalgamation. The reserves (whether capital or revenue or arising on revaluation) of the transferor entity, other than the statutory reserves, should not be included.
    - Any excess of the amount of the consideration over the value of the net assets of the transferor entity acquired by the transferee entity should be recognized in the transferee entity's financial statements as goodwill arising on amalgamation. If the amount of the consideration is lower than the value of the net assets acquired, the difference should be treated as Capital Reserve.
- The consideration for the amalgamation should include any noncash element at fair value. In case of issue of securities, the value fixed by the statutory authorities may be taken to be the fair value. In case of other assets, the fair value may be determined by reference to the market value of the assets given up. Where the market value of the assets given up cannot be reliably assessed, such assets may be valued at their respective net book values.
- Where the scheme of amalgamation provides for an adjustment to the consideration contingent on one or more future events, the amount of the additional payment should be included in the consideration if payment is probable and a reasonable estimate of the amount can be made. In all other cases, the adjustment should be recognised as soon as the amount is determinable.
- For all amalgamations, the following disclosures should be made in the first financial statements following the amalgamation:

    (a) names and general nature of business of the amalgamating companies;

(b) effective date of amalgamation for accounting purposes;

(c) the method of accounting used to reflect the amalgamation; and

(d) Particulars of the scheme sanctioned under a statute.

B.2. AS 21 Consolidated Financial Statements

This Standard should be applied in the preparation and presentation of consolidated financial statements for a group of enterprises under the control of a parent. This Standard should also be applied in accounting for investments in subsidiaries in the separate financial statements of a parent.

Important Terms

Control is:

(a) the ownership, directly or indirectly through subsidiary (ies), of more than one-half of the voting power of an enterprise; or

(b) Control of the composition of the board of directors in the case of a company or of the composition of the corresponding governing body in case of any other enterprise so as to obtain economic benefits from its activities.

A ***subsidiary*** is an enterprise that is controlled by another enterprise (known as the parent).

A ***parent*** is an enterprise that has one or more subsidiaries.

A ***group*** is a parent and all its subsidiaries.

Consolidated financial statements are the financial statements of a group presented as those of a single enterprise.

Equity is the residual interest in the assets of an enterprise after deducting all its liabilities.

Minority interest is that part of the net results of operations and of the net assets of a subsidiary attributable to interests which are not owned, directly or indirectly through subsidiary (ies), by the parent.

Key Points

- A parent which presents consolidated financial statements should present these statements in addition to its separate financial statements.
- A parent which presents consolidated financial statements should consolidate all subsidiaries, domestic as well as foreign, except when
    - control is intended to be temporary because the subsidiary is acquired and held exclusively with a view to its subsequent disposal in the near future; or
    - It operates under severe long-term restrictions which significantly impair its ability to transfer funds to the parent.
- In preparing consolidated financial statements, the financial statements of the parent and its subsidiaries should be combined on a line by line basis by adding together like items of assets, liabilities, income and expenses. In order that the consolidated financial statements present financial information about the group as that of a single enterprise.
- Where the carrying amount of the investment in the subsidiary is different from its cost, the carrying amount is considered for the purpose of above computations.
- Intragroup balances and intragroup transactions and resulting unrealised profits should be eliminated in full. Unrealised losses resulting from intragroup transactions should also be eliminated unless cost cannot be recovered.
- Minority interests should be presented in the consolidated balance sheet separately from liabilities and the equity of the parent's shareholders. Minority interests in the income of the group should also be separately presented.
- In a parent's separate financial statements, investments in subsidiaries should be accounted for in accordance with Accounting Standard (AS) 13, Accounting for Investments.

B.3. AS 23 Accounting for Investments in Associates in Consolidated Financial Statements

The objective of this Standard is to set out principles and procedures for recognising, in the consolidated financial statements, the effects of the investments in associates on the financial position and operating results of a group. It should be applied in accounting for investments in associates in the preparation and presentation of consolidated financial statements by an investor.

Important terms

An ***associate*** is an enterprise in which the investor has significant influence and which is neither a subsidiary nor a joint venture of the investor.

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

A ***subsidiary*** is an enterprise that is controlled by another enterprise (known as the parent).

A ***parent*** is an enterprise that has one or more subsidiaries. 3.6 A group is a parent and all its subsidiaries.

Consolidated financial statements are the financial statements of a group presented as those of a single enterprise.

The ***equity method*** is a method of accounting whereby the investment is initially recorded at cost, identifying any goodwill/capital reserve arising at the time of acquisition. The carrying amount of the investment is adjusted thereafter for the post acquisition change in the investor's share of net assets of the investee. The consolidated statement of profit and loss reflects the investor's share of the results of operations of the investee.

Key Points

- An investment in an associate should be accounted for in consolidated financial statements under the equity method except when the investment is acquired and held exclusively with a view to its subsequent disposal in the near future or the associate operates under severe long-term restrictions that significantly impair its ability to transfer funds to the investor.
- An investor should discontinue the use of the equity method from the date that it ceases to have significant influence in an associate but retains, either in whole or in part, its investment; or if the associate operates under severe long-term restrictions that significantly impair its ability to transfer funds to the investor.

- Goodwill/capital reserve arising on the acquisition of an associate by an investor should be included in the carrying amount of investment in the associate but should be disclosed separately.
- In using equity method, unrealised profits and losses resulting from transactions between the investor and the associate should be eliminated to the extent of the investor's interest in the associate. Unrealised losses should not be eliminated if and to the extent the cost of the transferred asset cannot be recovered.
- The carrying amount of investment in an associate should be reduced to recognise a decline, other than temporary, in the value of the investment, such reduction being determined and made for each investment individually.
- An appropriate listing and description of associates including the proportion of ownership interest and, if different, the proportion of voting power held should be disclosed in the consolidated financial statements.
- Investments in associates accounted for using the equity method should be classified as long-term investments and disclosed separately in the consolidated balance sheet. The investor's share of the profits or losses of such investments should be disclosed separately in the consolidated statement of profit and loss. The investor's share of any extraordinary or prior period items should also be separately disclosed.

B.4. AS 27 Financial Reporting of Interests in Joint Ventures

The objective of this Standard is to set out principles and procedures for accounting for interests in joint ventures and reporting of joint venture assets, liabilities, income and expenses in the financial statements of venturers and investors. It is to be applied in accounting for interests in joint ventures and the reporting of joint venture assets, liabilities, income and expenses in the financial statements of venturers and investors.

Important Terms

A ***joint venture*** is a contractual arrangement whereby two or more parties undertake an economic activity, which is subject to joint control.

Joint control is the contractually agreed sharing of control over an economic activity.

Control is the power to govern the financial and operating policies of an economic activity so as to obtain benefits from it.

A ***venturer*** is a party to a joint venture and has joint control over that joint venture.

An ***investor*** in a joint venture is a party to a joint venture and does not have joint control over that joint venture.

Proportionate consolidation is a method of accounting and reporting whereby a venturer's share of each of the assets, liabilities, income and expenses of a jointly controlled entity is reported as separate line items in the venturer's financial statements.

Key Points

- Joint ventures take many different forms and structures. The AS 27 applies to three broad types - jointly controlled operations, jointly controlled assets and jointly controlled entities.
- In jointly controlled operations, a venturer should recognise in its separate financial statements and consequently in its consolidated financial statements the assets controlled, income earned and the liabilities and expenses incurred by it in joint venture.
- In respect of its interest in jointly controlled assets, a venturer should recognise, in its separate financial statements, and consequently in its consolidated financial statements:
  (a) its share of the jointly controlled assets, classified according to the nature of the assets;
  (b) any liabilities which it has incurred;
  (c) its share of any liabilities incurred jointly with the other venturers in relation to the joint venture; (d) any income from the sale or use of its share of the output of the joint venture, together with its share of any expenses incurred by the joint venture; and
  (d) Any expenses which it has incurred in respect of its interest in the joint venture.
- In a venturer's separate financial statements, interest in a jointly controlled entity should be accounted for as an investment.
- In its consolidated financial statements, a venturer should report its interest in a jointly controlled entity using proportionate consolidation.

- In SFS as well as CFS, a venturer should disclose the aggregate amount of the following contingent liabilities, unless the probability of loss is remote, separately from the amount of other contingent liabilities:
  (a) any contingent liabilities that the venturer has incurred in relation to its interests in joint ventures and its share in each of the contingent liabilities which have been incurred jointly with other venturers;
  (b) its share of the contingent liabilities of the joint ventures themselves for which it is contingently liable; and
  (c) Those contingent liabilities that arise because the venturer is contingently liable for the liabilities of the other venturers of a joint venture.
- In SFC as well as CFS, a venturer should disclose the aggregate amount of the following commitments in respect of its interests in joint ventures separately from other commitments:
  (a) any capital commitments of the venturer in relation to its interests in joint ventures and its share in the capital commitments that have been incurred jointly with other venturers; and
  (b) Its share of the capital commitments of the joint ventures themselves.
- A venturer should disclose a list of all joint ventures and description of interests in significant joint ventures. In respect of jointly controlled entities, the venturer should also disclose the proportion of ownership interest, name and country of incorporation or residence.
- A venturer should disclose, in its separate financial statements, the aggregate amounts of each of the assets, liabilities, income and expenses related to its interests in the jointly controlled entities.

C. Standards pertaining to Recognition, Measurement, Presentation & Disclosure of Assets

The standards dealing mainly with the assets are as follows:

- AS 2 Valuation of Inventories
- AS 10 Property, Plant and Equipment
- AS 13 Accounting for Investments
- AS 16 Borrowing Costs
- AS 19 Leases
- AS 24 Discontinued Operations
- AS 26 Intangible Assets
- AS 28 Impairment of Assets

C.1. AS 2 Valuation of Inventories

This Standard should be applied in accounting for inventories other than:

a. work in progress arising under construction contracts, including directly related service contracts (see Accounting Standard (AS) 7, Construction Contracts);
b. work in progress arising in the ordinary course of business of service providers;
c. shares, debentures and other financial instruments held as stock-in-trade; and
d. producers' inventories of livestock, agricultural and forest products, and mineral oils, ores and gases to the extent that they are measured at net realisable value in accordance with well-established practices in those industries.

Important Terms

Inventories are assets:

(A) Held for sale in the ordinary course of business;

(b) In the process of production for such sale; or

(c) In the form of materials or supplies to be consumed in the production process or in the rendering of services.

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.

Key Points

- Inventories should be valued at the lower of cost and net realisable value.
- The cost of inventories should comprise all costs of purchase, costs of conversion and other costs incurred in bringing the inventories to their present location and condition.
- The cost of inventories of items that are not ordinarily interchangeable and goods or services produced and segregated for specific projects should be assigned by specific identification of their individual costs.
- The cost of inventories, in other cases, should be assigned by using the first-in, first-out (FIFO), or weighted average cost formula. The formula used should reflect the fairest possible approximation to the cost incurred in bringing the items of inventory to their present location and condition.
- The financial statements should disclose the accounting policies adopted in measuring inventories, including the cost formula used; and the total carrying amount of inventories and its classification appropriate to the enterprise.

C.2. AS 10 Property, Plant and Equipment

This Standard should be applied in accounting for property, plant and equipment except when another Accounting Standard requires or permits a different accounting treatment. However, this Standard does not apply to:

(a) Biological assets related to agricultural activity other than bearer plants. This Standard applies to bearer plants but it does not apply to the produce on bearer plants; and

(b) Wasting assets including mineral rights, expenditure on the exploration for and extraction of minerals, oil, natural gas and similar non-regenerative resources.

Key Terms

Property, plant and equipment are tangible items that:

- are held for use in the production or supply of goods or services, for rental to others, or for administrative purposes; and
- Are expected to be used during more than a period of twelve months.

Carrying amount is the amount at which an asset is recognised after deducting any accumulated depreciation and accumulated impairment losses.

Cost is the amount of cash or cash equivalents paid or the fair value of the other consideration given to acquire an asset at the time of its acquisition or construction or, where applicable, the amount attributed to that asset when initially recognised in accordance with the specific requirements of other Accounting Standards.

Depreciable amount is the cost of an asset, or other amount substituted for cost, less its residual value.

Depreciation is the systematic allocation of the depreciable amount of an asset over its useful life.

Useful life is:

- the period over which an asset is expected to be available for use by an enterprise; or
- The number of production or similar units expected to be obtained from the asset by an enterprise.

Key Points

- The cost of an item of property, plant and equipment should be recognised as an asset if, and only if:
  - (a) it is probable that future economic benefits associated with the item will flow to the enterprise; and
  - **(b)** The cost of the item can be measured reliably.
- An item of property, plant and equipment that qualifies for recognition as an asset should be measured at its cost.

- An enterprise should choose either the cost model or the revaluation model as its accounting policy and should apply that policy to an entire class of property, plant and equipment.
- Under cost model, after recognition as an asset, an item of property, plant and equipment should be carried at its cost less any accumulated depreciation and any accumulated impairment losses.
- Under revaluation model, after recognition as an asset, an item of property, plant and equipment whose fair value can be measured reliably should be carried at a revalued amount, being its fair value at the date of the revaluation less any subsequent accumulated depreciation and subsequent accumulated impairment losses. Revaluations should be made with sufficient regularity to ensure that the carrying amount does not differ materially from that which would be determined using fair value at the balance sheet date.
- If an item of property, plant and equipment is revalued, the entire class of property, plant and equipment to which that asset belongs should be revalued.
- An increase in the carrying amount of an asset arising on revaluation should be credited directly to owners' interests under the heading of revaluation surplus. However, the increase should be recognised in the statement of profit and loss to the extent that it reverses a revaluation decrease of the same asset previously recognised in the statement of profit and loss.
- A decrease in the carrying amount of an asset arising on revaluation should be charged to the statement of profit and loss. However, the decrease should be debited directly to owners' interests under the heading of revaluation surplus to the extent of any credit balance existing in the revaluation surplus in respect of that asset.
- Each part of an item of property, plant and equipment with a cost that is significant in relation to the total cost of the item should be depreciated separately.
- The depreciation charge for each period should be recognized in the statement of profit and loss unless it is included in the carrying amount of another asset.
- The depreciable amount of an asset should be allocated on a systematic basis over its useful life.

- The residual value and the useful life of an asset should be reviewed at least at each financial year-end and, if expectations differ from previous estimates, the change(s) should be accounted for as a change in an accounting estimate.
- The depreciation method used should reflect the pattern in which the future economic benefits of the asset are expected to be consumed by the enterprise.
- The depreciation method applied to an asset should be reviewed at least at each financial year-end and, if there has been a significant change in the expected pattern of consumption of the future economic benefits embodied in the asset, the method should be changed to reflect the changed pattern. Such a change should be accounted for as a change in an accounting estimate.
- The cost of property, plant and equipment may undergo changes subsequent to its acquisition or construction on account of changes in liabilities, price adjustments, changes in duties, changes in initial estimates of amounts provided for dismantling, removing, restoration and similar factors and included in the cost of the asset.
- Compensation from third parties for items of property, plant and equipment that were impaired, lost or given up should be included in the statement of profit and loss when the compensation becomes receivable.
- Items of property, plant and equipment retired from active use and held for disposal should be stated at the lower of their carrying amount and net realizable value. Any write-down in this regard should be recognized immediately in the statement of profit and loss.
- The carrying amount of an item of property, plant and equipment should be derecognized on disposal; or when no future economic benefits are expected from its use or disposal.
- The gain or loss arising from the de-recognition of an item of property, plant and equipment should be determined as the difference between the net disposal proceeds, if any, and the carrying amount of the item.
- The gain or loss arising from the de-recognition of an item of property, plant and equipment should be included in the statement of profit and loss when the item is derecognized. Gains should not be classified as revenue.

C.3. AS 12 Accounting for Government Grants

This Standard deals with accounting for government grants which are sometimes called by other names such as subsidies, cash incentives, duty drawbacks, etc. However, it does not deal with

- the special problems arising in accounting for government grants in financial statements reflecting the effects of changing prices or in supplementary information of a similar nature;
- government assistance other than in the form of government grants; or
- Government participation in the ownership of the enterprise.

Important Terms

Government refers to government, government agencies and similar bodies whether local, national or international.

Government grants are assistance by government in cash or kind to an enterprise for past or future compliance with certain conditions. They exclude those forms of government assistance which cannot reasonably have a value placed upon them and transactions with government which cannot be distinguished from the normal trading transactions of the enterprise.

Key Points

Government grants should not be recognized until there is reasonable assurance that the enterprise will comply with the conditions attached to them, and the grants will be received.

Government grants related to specific fixed assets should be presented in the balance sheet by showing the grant as a deduction from the gross value of the assets concerned in arriving at their book value. Where the grant related to a specific fixed asset equals the whole, or virtually the whole, of the cost of the asset, the asset should be shown in the balance sheet at a nominal value. Alternatively, government grants related to depreciable fixed assets may be treated as deferred income which should be recognized in the profit and loss statement on a systematic and rational basis over the useful life of the asset, i.e., such grants should be allocated to income over the periods and in the proportions in which depreciation on those assets is charged. Grants related to non-depreciable assets should be credited to capital reserve under this method. However, if a grant related to a non-depreciable asset requires the fulfilment of certain obligations, the grant

should be credited to income over the same period over which the cost of meeting such obligations is charged to income. The deferred income balance should be separately disclosed in the financial statements.

Government grants related to revenue should be recognised on a systematic basis in the profit and loss statement over the periods necessary to match them with the related costs which they are intended to compensate. Such grants should either be shown separately under 'other income' or deducted in reporting the related expense.

Government grants in the form of non-monetary assets, given at a concessional rate, should be accounted for on the basis of their acquisition cost. In case a non-monetary asset is given free of cost, it should be recorded at a nominal value.

Government grants that are receivable as compensation for expenses or losses incurred in a previous accounting period or for the purpose of giving immediate financial support to the enterprise with no further related costs, should be recognized and disclosed in the profit and loss statement of the period in which they are receivable, as an extraordinary item if appropriate.

Government grants that become refundable should be accounted for as an extraordinary item.

The amount refundable in respect of a grant related to revenue should be applied first against any unamortized deferred credit remaining in respect of the grant and excess should be charged to profit and loss statement. The amount refundable in respect of a grant related to a specific fixed asset should be recorded by increasing the book value of the asset or by reducing the capital reserve or the deferred income balance, as appropriate, by the amount refundable. In the first alternative, i.e., where the book value of the asset is increased, depreciation on the revised book value should be provided prospectively over the residual useful life of the asset.

The following should be disclosed:

- the accounting policy adopted for government grants, including the methods of presentation in the financial statements;
- The nature and extent of government grants recognized in the financial statements, including grants of non-monetary assets given at a concessional rate or free of cost.

C.4. AS 13 Accounting for Investments

This Standard deals with accounting for investments in the financial statements of enterprises and related disclosure requirements. However, this does not deal with:

- the bases for recognition of interest, dividends and rentals earned on investments which are covered by Accounting Standard 9 on Revenue Recognition;
- operating or finance leases;
- investments of retirement benefit plans and life insurance enterprises; and
- Mutual funds and venture capital funds and/or the related asset management companies, banks and public financial institutions formed under a Central or State Government Act or so declared under the Companies Act, 2013.

Important Terms

Investments are assets held by an enterprise for earning income by way of dividends, interest, and rentals, for capital appreciation, or for other benefits to the investing enterprise. Assets held as stock-in-trade are not 'investments'.

A ***current investment*** is an investment that is by its nature readily realisable and is intended to be held for not more than one year from the date on which such investment is made.

A ***long term investment*** is an investment other than a current investment.

An ***investment property*** is an investment in land or buildings that are not intended to be occupied substantially for use by, or in the operations of, the investing enterprise.

Market value is the amount obtainable from the sale of an investment in an open market, net of expenses necessarily to be incurred on or before disposal.

Key Points

Investments are classified as long term investments and current investments. Current investments are in the nature of current assets, although the common practice may be to include them in investments.

Further classification of current and long-term investments should be as specified in the statute governing the enterprise. In the absence of a statutory requirement, such further classification should disclose, where applicable, investments in:

(a) Government or Trust securities

(b) Shares, debentures or bonds

(c) Investment properties

(d) Others—specifying nature

- The cost of an investment should include acquisition charges such as brokerage, fees and duties.
- If an investment is acquired, or partly acquired, by the issue of shares or other securities, the acquisition cost should be the fair value of the securities issued (which in appropriate cases may be indicated by the issue price as determined by statutory authorities). The fair value may not necessarily be equal to the nominal or par value of the securities issued. If an investment is acquired in exchange for another asset, the acquisition cost of the investment should be determined by reference to the fair value of the asset given up. Alternatively, the acquisition cost of the investment may be determined with reference to the fair value of the investment acquired if it is more clearly evident.
- .An enterprise holding investment properties should account for them in accordance with cost model used in AS 10 *Property, Plant and Equipment.*
- Investments classified as current investments should be carried in the financial statements at the lower of cost and fair value determined either on an individual investment basis or by category of investment, but not on an overall (or global) basis.
- Investments classified as long term investments should be carried in the financial statements at cost. However, provision for diminution shall be made to recognise a decline, other than temporary, in the value of the investments, such reduction being determined and made for each investment individually.
- Any reduction in the carrying amount and any reversals of such reductions should be charged or credited to the profit and loss statement.
- On disposal of an investment, the difference between the carrying amount and net disposal proceeds should be charged or credited to the profit and loss statement.

C.5. AS 16 Borrowing Costs

The objective of this Standard is to prescribe the accounting treatment for borrowing costs.

Important Terms

Borrowing costs are interest and other costs incurred by an enterprise in connection with the borrowing of funds.

A ***qualifying asset*** is an asset that necessarily takes a substantial period of time to get ready for its intended use or sale.

Key Points

- Ordinarily, a period of twelve months is considered as substantial period of time unless a shorter or longer period can be justified on the basis of facts and circumstances of the case.
- Borrowing costs that are directly attributable to the acquisition, construction or production of a qualifying asset should be capitalized as part of the cost of that asset. The amount of borrowing costs eligible for capitalization should be determined in accordance with this Standard. Other borrowing costs should be recognized as an expense in the period in which they are incurred.
- To the extent that funds are borrowed specifically for the purpose of obtaining a qualifying asset, the amount of borrowing costs eligible for capitalization on that asset should be determined as the actual borrowing costs incurred on that borrowing during the period less any income on the temporary investment of those borrowings.
- To the extent that funds are borrowed generally and used for the purpose of obtaining a qualifying asset, the amount of borrowing costs eligible for capitalization should be determined by applying a capitalization rate to the expenditure on that asset. The capitalization rate should be the weighted average of the borrowing costs applicable to the borrowings of the enterprise that are outstanding during the period, other than borrowings made specifically for the purpose of obtaining a qualifying asset. The amount of borrowing

costs capitalized during a period should not exceed the amount of borrowing costs incurred during that period.

- The capitalization of borrowing costs as part of the cost of a qualifying asset should commence when all the following conditions are satisfied:
  - **(a)** expenditure for the acquisition, construction or production of a qualifying asset is being incurred;
  - **(b)** borrowing costs are being incurred; and
  - **(c)** Activities that are necessary to prepare the asset for its intended use or sale are in progress.
- Capitalization of borrowing costs should be suspended during extended periods in which active development is interrupted.
- Capitalization of borrowing costs should cease when substantially all the activities necessary to prepare the qualifying asset for its intended use or sale are complete.
- When the construction of a qualifying asset is completed in parts and a completed part is capable of being used while construction continues for the other parts, capitalization of borrowing costs in relation to a part should cease when substantially all the activities necessary to prepare that part for its intended use or sale are complete.
- The financial statements should disclose:
  - (a) the accounting policy adopted for borrowing costs; and
  - (b) The amount of borrowing costs capitalized during the period.

C.6. AS 19 Leases

The objective of this Standard is to prescribe, for lessees and lessors, the appropriate accounting policies and disclosures in relation to finance leases and operating leases. However, it should not be applied in accounting for all leases other than:

- lease agreements to explore for or use natural resources, such as oil, gas, timber, metals and other mineral rights; and
- licensing agreements for items such as motion picture films, video recordings, plays, manuscripts, patents and copyrights; and
- Lease agreements to use lands.

Important Terms

A ***lease*** is an agreement whereby the lessor conveys to the lessee in return for a payment or series of payments the right to use an asset for an agreed period of time.

A ***finance lease*** is a lease that transfers substantially all the risks and rewards incident to ownership of an asset.

An ***operating lease*** is a lease other than a finance lease.

A ***non-cancellable lease*** is a lease that is cancellable only:

(a) upon the occurrence of some remote contingency; or
(b) with the permission of the lessor; or
(c) if the lessee enters into a new lease for the same or an equivalent asset with the same lessor; or
(d) Upon payment by the lessee of an additional amount such that, at inception, continuation of the lease is reasonably certain.

The ***inception of the lease*** is the earlier of the date of the lease agreement and the date of a commitment by the parties to the principal provisions of the lease.

The ***lease term*** is the non-cancellable period for which the lessee has agreed to take on lease the asset together with any further periods for which the lessee has the option to continue the lease of the asset, with or without further payment, which option at the inception of the lease it is reasonably certain that the lessee will exercise.

Minimum lease payments are the payments over the lease term that the lessee is, or can be required, to make excluding contingent rent, costs for services and taxes to be paid by and reimbursed to the lessor, together with:

(a) in the case of the lessee, any residual value guaranteed by or on behalf of the lessee; or
(b) in the case of the lessor, any residual value guaranteed to the lessor:
    - by or on behalf of the lessee; or
    - By an independent third party financially capable of meeting this guarantee.

Guaranteed residual value is:

(a) in the case of the lessee, that part of the residual value which is guaranteed by the lessee or by a party on behalf of the lessee (the amount of the guarantee being the maximum amount that could, in any event, become payable); and

(b) In the case of the lessor, that part of the residual value which is guaranteed by or on behalf of the lessee, or by an independent third party who is financially capable of discharging the obligations under the guarantee

Net investment in the lease is the gross investment in the lease less unearned finance income.

The ***interest rate implicit in the lease*** is the discount rate that, at the inception of the lease, causes the aggregate present value of

(a) the minimum lease payments under a finance lease from the standpoint of the lessor; and
(b) Any unguaranteed residual value accruing to the lessor, to be equal to the fair value of the leased asset.

The ***lessee's incremental borrowing rate of interest*** is the rate of interest the lessee would have to pay on a similar lease or, if that is not determinable, the rate that, at the inception of the lease, the lessee would incur to borrow over a similar term, and with a similar security, the funds necessary to purchase the asset.

Contingent rent is that portion of the lease payments that is not fixed in amount but is based on a factor other than just the passage of time (e.g., percentage of sales, amount of usage, price indices, and market rates of interest).

Key Points

Finance Lease

- At the inception of a finance lease, the lessee should recognise the lease as an asset and a liability. Such recognition should be at an amount equal to the fair value of the leased asset at the inception of the lease. However, if the fair value of the leased asset exceeds the present value of the minimum lease payments from the standpoint of the lessee, the

amount recorded as an asset and a liability should be the present value of the minimum lease payments from the standpoint of the lessee. In calculating the present value of the minimum lease payments the discount rate is the interest rate implicit in the lease, if this is practicable to determine; if not, the lessee's incremental borrowing rate should be used.

- Lease payments should be apportioned between the finance charge and the reduction of the outstanding liability. The finance charge should be allocated to periods during the lease term so as to produce a constant periodic rate of interest on the remaining balance of the liability for each period.
- A finance lease gives rise to a depreciation expense for the asset as well as a finance expense for each accounting period. The depreciation policy for a leased asset should be consistent with that for depreciable assets which are owned. If there is no reasonable certainty that the lessee will obtain ownership by the end of the lease term, the asset should be fully depreciated over the lease term or its useful life, whichever is shorter.
- The lessor should recognise assets given under a finance lease in its balance sheet as a receivable at an amount equal to the net investment in the lease.
- The recognition of finance income should be based on a pattern reflecting a constant periodic rate of return on the net investment of the lessor outstanding in respect of the finance lease.
- The manufacturer or dealer lessor should recognise the transaction of sale in the statement of profit and loss for the period, in accordance with the policy followed by the enterprise for outright sales. If artificially low rates of interest are quoted, profit on sale should be restricted to that which would apply if a commercial rate of interest were charged. Initial direct costs should be recognised as an expense in the statement of profit and loss at the inception of the lease.
- The lessee and lessor should make appropriate disclosures for finance leases as prescribed in standards. Note certain exemption have been prescribed for smaller enterprises.

Operating Leases

- Lease payments under an operating lease should be recognised as an expense in the statement of profit and loss on a straight line basis over the lease term unless another systematic basis is more representative of the time pattern of the user's benefit.
- The lessor should present an asset given under operating lease in its balance sheet under fixed assets.
- Lease income from operating leases should be recognized in the statement of profit and loss on a straight line basis over the lease term, unless another systematic basis is more representative of the time pattern in which benefit derived from the use of the leased asset is diminished.
- The depreciation of leased assets should be on a basis consistent with the normal depreciation policy of the lessor for similar assets.
- The lessee and the leasor should make appropriate disclosures as prescribed for operating leases after giving due consideration for exemptions provided to smaller entities.
- If a sale and leaseback transaction results in a finance lease, any excess or deficiency of sales proceeds over the carrying amount should not be immediately recognized as income or loss in the financial statements of a seller-lessee. Instead, it should be deferred and amortized over the lease term in proportion to the depreciation of the leased asset.
- If a sale and leaseback transaction results in an operating lease, and it is clear that the transaction is established at fair value, any profit or loss should be recognized immediately. If the sale price is below fair value, any profit or loss should be recognized immediately except that, if the loss is compensated by future lease payments at below market price, it should be deferred and amortized in proportion to the lease payments over the period for which the asset is expected to be used. If the sale price is above fair value, the excess over fair value should be deferred and amortized over the period for which the asset is expected to be used.
- For operating leases, if the fair value at the time of a sale and leaseback transaction is less than the carrying amount of the asset, a loss equal to the amount of the difference between the carrying amount and fair value should be recognized immediately.

C.7. AS 24 Discontinued Operations

This Standard applies to all discontinuing operations of an enterprise.

Important Terms

A ***discontinuing operation*** is a component of an enterprise:

(a) that the enterprise, pursuant to a single plan, is:
   i. disposing of substantially in its entirety, such as by selling the component in a single transaction or by demerger or spin-off of ownership of the component to the enterprise's shareholders; or
   ii. disposing of piecemeal, such as by selling off the component's assets and settling its liabilities individually; or
   iii. terminating through abandonment; and

(b) that represents a separate major line of business or geographical area of operations; and

(c) That can be distinguished operationally and for financial reporting purposes.

Key Points

- With respect to a discontinuing operation, the initial disclosure event is the occurrence of one of the following, whichever occurs earlier:
    (a) the enterprise has entered into a binding sale agreement for substantially all of the assets attributable to the discontinuing operation; or
    (b) the enterprise's board of directors or similar governing body has both approved a detailed, formal plan for the discontinuance and made an announcement of the plan
- An enterprise should apply the principles of recognition and measurement that are set out in other Accounting Standards for the purpose of deciding as to when and how to recognize and measure the changes in assets and liabilities and the revenue, expenses, gains, losses and cash flows relating to a discontinuing operation.
- An enterprise should include the following information relating to a discontinuing operation in its financial statements beginning with the financial statements for the period in which the initial disclosure event occurs:
    (a) a description of the discontinuing operation(s);
    (b) the business or geographical segment(s) in which it is reported

(c) the date and nature of the initial disclosure event;

(d) the date or period in which the discontinuance is expected to be completed if known or determinable;

(e) the carrying amounts, as of the balance sheet date, of the total assets to be disposed of and the total liabilities to be settled;

(f) the amounts of revenue and expenses in respect of the ordinary activities attributable to the discontinuing operation during the current financial reporting period;

(g) the amount of pre-tax profit or loss from ordinary activities attributable to the discontinuing operation during the current financial reporting period, and the income tax expense4 related thereto; and

(h) The amounts of net cash flows attributable to the operating, investing, and financing activities of the discontinuing operation during the current financial reporting period.

- When an enterprise disposes of assets or settles liabilities attributable to a discontinuing operation or enters into binding agreements for the sale of such assets or the settlement of such liabilities, it should include, in its financial statements, the following information when the events occur:

  (a) for any gain or loss that is recognised on the disposal of assets or settlement of liabilities attributable to the discontinuing operation,

    - the amount of the pre-tax gain or loss and
    - income tax expense relating to the gain or loss; and

  (b) the net selling price or range of prices (which is after deducting expected disposal costs) of those net assets for which the enterprise has entered into one or more binding sale agreements, the expected timing of receipt of those cash flows and the carrying amount of those net assets on the balance sheet date.

- An enterprise should also include, in its financial statements, for periods subsequent to the one in which the initial disclosure event occurs, a description of any significant changes in the amount or timing of cash flows relating to the assets to be disposed or liabilities to be settled and the events causing those changes.

- Discontinuance is completed when the plan is substantially completed or abandoned, though full payments from the buyer(s) may not yet have been received. Till then all disclosures should continue.
- If an enterprise abandons or withdraws from a plan that was previously reported as a discontinuing operation, that fact, reasons therefore and its effect should be disclosed.
- All disclosures required by this Standard should be presented separately for each discontinuing operation.

C.8. AS 26 Intangible Assets

The objective of this Standard is to prescribe the accounting treatment for intangible assets that are not dealt with specifically in another Accounting Standard. This Standard is not to be applied in following cases:

- financial assets,
- mineral rights and expenditure on the exploration for, or development and extraction of, minerals, oil, natural gas and similar non-regenerative resources;
- intangible assets arising in insurance enterprises from contracts with policyholders,
- termination benefits, and
- where such termination have dealt in other standards

Important Terms

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.

Research is original and planned investigation undertaken with the prospect of gaining new scientific or technical knowledge and understanding.

Development is the application of research findings or other knowledge to a plan or design for the production of new or substantially improved materials, devices, products, processes, systems or services prior to the commencement of commercial production or use.

Amortization is the systematic allocation of the depreciable amount of an intangible asset over its useful life.

An ***impairment loss*** is the amount by which the carrying amount of an asset exceeds its recoverable amount.

Key Points

- An intangible asset should be recognized if, and only if:
  - (a) it is probable that the future economic benefits that are attributable to the asset will flow to the enterprise; and
  - (b) The cost of the asset can be measured reliably.
- An enterprise should assess the probability of future economic benefits using reasonable and supportable assumptions that represent best estimate of the set of economic conditions that will exist over the useful life of the asset.
- An intangible asset should be measured initially at cost.
- Internally generated goodwill should not be recognized as an asset
- No intangible asset arising from research (or from the research phase of an internal project) should be recognized. Expenditure on research (or on the research phase of an internal project) should be recognized as an expense when it is incurred.
- An intangible asset arising from development (or from the development phase of an internal project) should be recognized if, and only if, an enterprise can demonstrate all of the following:
  - (a) the technical feasibility of completing the intangible asset so that it will be available for use or sale;
  - (b) its intention to complete the intangible asset and use or sell it;
  - (c) its ability to use or sell the intangible asset;
  - (d) How the intangible asset will generate probable future economic benefits. Among other things, the enterprise should demonstrate the existence of a market for the output of the intangible asset or the intangible asset itself or, if it is to be used internally, the usefulness of the intangible asset;
  - (e) the availability of adequate technical, financial and other resources to complete the development and to use or sell the intangible asset; and

(f) Its ability to measure the expenditure attributable to the intangible asset during its development reliably.

- Internally generated brands, mastheads, publishing titles, customer lists and items similar in substance should not be recognized as intangible assets.
- Expenditure on an intangible item should be recognized as an expense when it is incurred unless:
  - **(a)** it forms part of the cost of an intangible asset that meets the recognition criteria or
  - **(b)** The item is acquired in an amalgamation in the nature of purchase and cannot be recognized as an intangible asset. If this is the case, this expenditure (included in the cost of acquisition) should form part of the amount attributed to goodwill (capital reserve) at the date of acquisition.
- Expenditure on an intangible item that was initially recognized as an expense by a reporting enterprise in previous annual financial statements or interim financial reports should not be recognized as part of the cost of an intangible asset at a later date.
- Subsequent expenditure on an intangible asset after its purchase or its completion should be recognized as an expense when it is incurred unless:
  - **(a)** it is probable that the expenditure will enable the asset to generate future economic benefits in excess of its originally assessed standard of performance; and
  - **(b)** The expenditure can be measured and attributed to the asset reliably. If these conditions are met, the subsequent expenditure should be added to the cost of the intangible asset.
- After initial recognition, an intangible asset should be carried at its cost less any accumulated amortization and any accumulated impairment losses.
- The depreciable amount of an intangible asset should be allocated on a systematic basis over the best estimate of its useful life. There is a rebuttable presumption that the useful life of an intangible asset will not exceed ten years from the date when the asset is available for use. Amortization should commence when the asset is available for use.
- If control over the future economic benefits from an intangible asset is achieved through legal rights that have been granted for a finite period, the useful life of the intangible asset should not exceed the period of the legal rights unless:
  - **(a)** the legal rights are renewable; and

(b) Renewal is virtually certain.

- The amortization method used should reflect the pattern in which the asset's economic benefits are consumed by the enterprise. If that pattern cannot be determined reliably, the straight-line method should be used. The amortization charge for each period should be recognized as an expense unless another Accounting Standard permits or requires it to be included in the carrying amount of another asset.
- The residual value of an intangible asset should be assumed to be zero unless:
  - **(a)** there is a commitment by a third party to purchase the asset at the end of its useful life; or
  - **(b)** there is an active market for the asset and:
    - (i) residual value can be determined by reference to that market; and
    - (ii) It is probable that such a market will exist at the end of the asset's useful life.
- The amortization period and the amortization method should be reviewed at least at each financial year end. If the expected useful life of the asset is significantly different from previous estimates, the amortization period should be changed accordingly. If there has been a significant change in the expected pattern of economic benefits from the asset, the amortization method should be changed to reflect the changed pattern. Such changes should be accounted for in accordance with AS 5*, Net Profit or Loss for the Period, Prior Period Items and Changes in Accounting Policies*.
- In addition to the requirements of Accounting Standard on Impairment of Assets, an enterprise should estimate the recoverable amount of the following intangible assets at least at each financial year end even if there is no indication that the asset is impaired:
  - **(a)** an intangible asset that is not yet available for use; and
  - **(b)** An intangible asset that is amortized over a period exceeding ten years from the date when the asset is available for use. The recoverable amount should be determined under Accounting Standard on Impairment of Assets and impairment losses recognized accordingly.
- An intangible asset should be derecognized (eliminated from the balance sheet) on disposal or when no future economic benefits are expected from its use and subsequent disposal.

- Gains or losses arising from the retirement or disposal of an intangible asset should be determined as the difference between the net disposal proceeds and the carrying amount of the asset and should be recognized as income or expense in the statement of profit and loss.
- Adequate disclosures as prescribed in the standards should be made.

C.9. AS 28 Impairment of Assets

This Standard should be applied in accounting for the impairment of all assets, other than inventories, assets arising from construction contracts, financial assets, and deferred tax assets.

Important Terms

Recoverable amount is the higher of an asset's net selling price and its value in use.

Value in use is the present value of estimated future cash flows expected to arise from the continuing use of an asset and from its disposal at the end of its useful life.

Net selling price is the amount obtainable from the sale of an asset in an arm's length transaction between knowledgeable, willing parties, less the costs of disposal.

Costs of disposal are incremental costs directly attributable to the disposal of an asset, excluding finance costs and income tax expense.

An ***impairment loss*** is the amount by which the carrying amount of an asset exceeds its recoverable amount.

A ***cash generating unit*** is the smallest identifiable group of assets that generates cash inflows from continuing use that are largely independent of the cash inflows from other assets or groups of assets.

Corporate assets are assets other than goodwill that contribute to the future cash flows of both the cash generating unit under review and other cash generating units.

Key Points

- An enterprise should assess at each balance sheet date whether there is any indication that an asset may be impaired. If any such indication exists, the enterprise should estimate the recoverable amount of the asset.
- In assessing whether there is any indication that an asset may be impaired, an enterprise should consider, as a minimum, the following indications:

External sources of information

(a) during the period, an asset's market value has declined significantly more than would be expected as a result of the passage of time or normal use;

(b) significant changes with an adverse effect on the enterprise have taken place during the period, or will take place in the near future, in the technological, market, economic or legal environment in which the enterprise operates or in the market to which an asset is dedicated;

(c) market interest rates or other market rates of return on investments have increased during the period, and those increases are likely to affect the discount rate used in calculating an asset's value in use and decrease the asset's recoverable amount materially;

(d) The carrying amount of the net assets of the reporting enterprise is more than its market capitalization.

Internal sources of information

(e) evidence is available of obsolescence or physical damage of an asset;

- significant changes with an adverse effect on the enterprise have taken place during the period, or are expected to take place in the near future, in the extent to which, or manner in which, an asset is used or is expected to be used. These changes include plans to discontinue or restructure the operation to which an asset belongs or to dispose of an asset before the previously expected date; and

(f) Evidence is available from internal reporting that indicates that the economic performance of an asset is, or will be, worse than expected.

- If the recoverable amount of an asset is less than its carrying amount, the carrying amount of the asset should be reduced to its recoverable amount. That reduction is an impairment loss.
- An impairment loss should be recognized as an expense in the statement of profit and loss immediately, unless the asset is carried at revalued amount in accordance with another Accounting Standard, in which case any impairment loss of a revalued asset should be treated as a revaluation decrease under that Accounting Standard.
- When the amount estimated for an impairment loss is greater than the carrying amount of the asset to which it relates, an enterprise should recognize a liability if, and only if, that is required by another Accounting Standard.
- After the recognition of an impairment loss, the depreciation (amortization) charge for the asset should be adjusted in future periods to allocate the asset's revised carrying amount, less its residual value (if any), on a systematic basis over its remaining useful life.
- If there is any indication that an asset may be impaired, the recoverable amount should be estimated for the individual asset. If it is not possible to estimate the recoverable amount of the individual asset, an enterprise should determine the recoverable amount of the cash-generating unit to which the asset belongs (the asset's cash-generating unit).
- If an active market exists for the output produced by an asset or a group of assets, this asset or group of assets should be identified as a separate cash-generating unit, even if some or all of the output is used internally. If this is the case, management's best estimate of future market prices for the output should be used:
  (a) in determining the value in use of this cash-generating unit, when estimating the future cash inflows that relate to the internal use of the output; and
  (b) In determining the value in use of other cash-generating units of the reporting enterprise, when estimating the future cash outflows that relate to the internal use of the output.
- Cash-generating units should be identified consistently from period to period for the same asset or types of assets, unless a change is justified.
- The carrying amount of a cash-generating unit should be determined consistently with the way the recoverable amount of the cash-generating unit is determined.
- In testing a cash-generating unit for impairment, an enterprise should identify whether goodwill that relates to this cash-generating unit is recognized in the financial statements.

- In testing a cash-generating unit for impairment, an enterprise should identify all the corporate assets that relate to the cash-generating unit under review.
- An impairment loss should be recognized for a cash-generating unit if, and only if, its recoverable amount is less than its carrying amount. The impairment loss should be allocated to reduce the carrying amount of the assets of the unit in the following order:
  (a) first, to goodwill allocated to the cash-generating unit (if any); and
  (b) Then, to the other assets of the unit on a pro-rata basis based on the carrying amount of each asset in the unit.

  These reductions in carrying amounts should be treated as impairment losses on individual assets.

- In allocating an impairment loss, the carrying amount of an asset should not be reduced below the highest of:
  (a) its net selling price (if determinable);
  (b) its value in use (if determinable); and
  (c) Zero.

The amount of the impairment loss that would otherwise have been allocated to the asset should be allocated to the other assets of the unit on a pro-rata basis.

- A liability should be recognized for any remaining amount of an impairment loss for a cash-generating unit if that is required by another Accounting Standard.
- An enterprise should assess at each balance sheet date whether there is any indication that an impairment loss recognized for an asset in prior accounting periods may no longer exist or may have decreased. If any such indication exists, the enterprise should estimate the recoverable amount of that asset.
- In assessing whether there is any indication that an impairment loss recognized for an asset in prior accounting periods may no longer exist or may have decreased, an enterprise should consider, as a minimum, the following indications:
- An impairment loss recognized for an asset in prior accounting periods should be reversed if there has been a change in the estimates of cash inflows, cash outflows or discount rates used to determine the asset's recoverable amount since the last impairment loss was recognized. If

this is the case, the carrying amount of the asset should be increased to its recoverable amount. That increase is a reversal of an impairment loss.

- The increased carrying amount of an asset due to a reversal of an impairment loss should not exceed the carrying amount that would have been determined (net of amortization or depreciation) had no impairment loss been recognized for the asset in prior accounting periods.
- A reversal of an impairment loss for an asset should be recognized as income immediately in the statement of profit and loss, unless the asset is carried at revalued amount in accordance with another Accounting Standard in which case any reversal of an impairment loss on a revalued asset should be treated as a revaluation increase under that Accounting Standard.
- After a reversal of an impairment loss is recognized, the depreciation (amortization) charge for the asset should be adjusted in future periods to allocate the asset's revised carrying amount, less its residual value (if any), on a systematic basis over its remaining useful life.
- Appropriate disclosures as prescribed should be made.

D. Standards dealing with Reorganization, Measurement, Presentation and Disclosure of Revenue

The following standards deal with Revenue:

AS 7 Construction Contracts

AS 9 Revenue Recognition

These standards are discussed hereafter.

D.1. AS 7 Construction Contracts

The objective of this Standard is to prescribe the accounting treatment of revenue and costs associated with construction contracts.

Important Terms

A ***construction contract*** is a contract specifically negotiated for the construction of an asset or a combination of assets that are closely interrelated or interdependent in terms of their design, technology and function or their ultimate purpose or use.

A ***fixed price contract*** is a construction contract in which the contractor agrees to a fixed contract price, or a fixed rate per unit of output, which in some cases is subject to cost escalation clauses.

A ***cost plus contract*** is a construction contract in which the contractor is reimbursed for allowable or otherwise defined costs, plus percentage of these costs or a fixed fee.

Key Points

- Contract revenue should comprise:
  (a) the initial amount of revenue agreed in the contract; and
  (b) variations in contract work, claims and incentive payments:

    (i) To the extent that it is probable that they will result in revenue; and

    (ii) They are capable of being reliably measured.

- Contract costs should comprise:
  - costs that relate directly to the specific contract;
  - costs that are attributable to contract activity in general and can be allocated to the contract; and
  - Such other costs as are specifically chargeable to the customer under the terms of the contract.
- When the outcome of a construction contract can be estimated reliably, contract revenue and contract costs associated with the construction contract should be recognised as revenue and expenses respectively by reference to the stage of completion of the contract activity at the reporting date. An expected loss on the construction contract should be recognised as an expense immediately.
- In the case of a fixed price contract, the outcome of a construction contract can be estimated reliably when all the following conditions are satisfied:
  (a) total contract revenue can be measured reliably;
  (b) it is probable that the economic benefits associated with the contract will flow to the enterprise;
  (c) both the contract costs to complete the contract and the stage of contract completion at the reporting date can be measured reliably; and
  (d) The contract costs attributable to the contract can be clearly identified and measured reliably so that actual contract costs incurred can be compared with prior estimates.

- In the case of a cost plus contract, the outcome of a construction contract can be estimated reliably when all the following conditions are satisfied:
  (a) it is probable that the economic benefits associated with the contract will flow to the enterprise; and
  (b) The contract costs attributable to the contract, whether or not specifically reimbursable, can be clearly identified and measured reliably.
- When the outcome of a construction contract cannot be estimated reliably revenue should be recognised only to the extent of contract costs incurred of which recovery is probable; and contract costs should be recognised as an expense in the period in which they are incurred.

- When the uncertainties that prevented the outcome of the contract being estimated reliably no longer exist, revenue and expenses associated with the construction contract should be recognised.
- When it is probable that total contract costs will exceed total contract revenue, the expected loss should be recognised as an expense immediately.
- An enterprise should disclose:
  - (a) the amount of contract revenue recognised as revenue in the period;
  - (b) the methods used to determine the contract revenue recognised in the period; and
  - (c) The methods used to determine the stage of completion of contracts in progress.
- An enterprise should disclose the following for contracts in progress at the reporting date:
  - (a) the aggregate amount of costs incurred and recognised profits (less recognised losses) upto the reporting date;
  - (b) the amount of advances received; and
  - (c) The amount of retentions.
- An enterprise should present:

  (a) The gross amount due from customers for contract work as an asset; and

  (b) The gross amount due to customers for contract work as a liability.

D.2. AS 9 Revenue Recognition

This Standard deals with the bases for recognition of revenue in the statement of profit and loss of an enterprise. The Standard is concerned with the recognition of revenue arising in the course of the ordinary activities of the enterprise from

- **(a)** the sale of goods,
- **(b)** the rendering of services, and
- **(c)** The use by others of enterprise resources yielding interest, royalties and dividends.

Important Terms

Revenue is the gross inflow of cash, receivables or other consideration arising in the course of the ordinary activities of an enterprise4 from the sale of goods, from the rendering of services,

and from the use by others of enterprise resources yielding interest, royalties and dividends. Revenue is measured by the charges made to customers or clients for goods supplied and services rendered to them and by the charges and rewards arising from the use of resources by them. In an agency relationship, the revenue is the amount of commission and not the gross inflow of cash, receivables or other consideration.

Completed service contract method is a method of accounting which recognises revenue in the statement of profit and loss only when the rendering of services under a contract is completed or substantially completed.

Proportionate completion method is a method of accounting which recognises revenue in the statement of profit and loss proportionately with the degree of completion of services under a contract.

Key Points

- Revenue from sales or service transactions should be recognised when the requirements as to performance set out in paragraphs 11 and 12 are satisfied, provided that at the time of performance it is not unreasonable to expect ultimate collection. If at the time of raising of any claim it is unreasonable to expect ultimate collection, revenue recognition should be postponed.
- In a transaction involving the sale of goods, performance should be regarded as being achieved when the following conditions have been fulfilled:
  - **(a)** the seller of goods has transferred to the buyer the property in the goods for a price or all significant risks and rewards of ownership have been transferred to the buyer and the seller retains no effective control of the goods transferred to a degree usually associated with ownership; and
  - **(b)** No significant uncertainty exists regarding the amount of the consideration that will be derived from the sale of the goods.
- In a transaction involving the rendering of services, performance should be measured either under the completed service contract method or under the proportionate completion method, whichever relates the revenue to the work accomplished. Such performance should be

regarded as being achieved when no significant uncertainty exists regarding the amount of the consideration that will be derived from rendering the service.

- Revenue arising from the use by others of enterprise resources yielding interest, royalties and dividends should only be recognised when no significant uncertainty as to measurability or collectability exists.
- Interest should be recognised on a time proportion basis taking into account the amount outstanding and the rate applicable.
- Royalties should be recognised: on an accrual basis in accordance with the terms of the relevant agreement.
- Dividends from shares should be recognised when the owner's right to receive payment investments in is established.
- An enterprise should also disclose the circumstances in which revenue recognition has been postponed pending the resolution of significant uncertainties.

E. Standards dealing with Recognition, Measurement, Presentation & Disclosure of Expenses & Liabilities

The accounting standards falling in this category are:

AS 15 Employee Benefits

AS 29 Provisions, Contingent Liabilities and Contingent Assets.

AS 22- Accounting for Taxes on Income

E.1. AS 15 Employee Benefits

The objective of this Standard is to prescribe the accounting and disclosure for employee benefits. This Standard should be applied by an employer in accounting for all employee benefits, except employee share-based payments.

Important Terms

Employee benefits are all forms of consideration given by an enterprise in exchange for service rendered by employees.

Short-term employee benefits are employee benefits (other than termination benefits) which fall due wholly within twelve months after the end of the period in which the employees render the related service.

Post-employment benefits are employee benefits (other than termination benefits) which are payable after the completion of employment.

Post-employment benefit plans are formal or informal arrangements under which an enterprise provides post-employment benefits for one or more employees.

Defined contribution plans are post-employment benefit plans under which an enterprise pays fixed contributions into a separate entity (a fund) and will have no obligation to pay further

contributions if the fund does not hold sufficient assets to pay all employee benefits relating to employee service in the current and prior periods.

Defined benefit plans are post-employment benefit plans other than defined contribution plans.

Multi-employer plans are defined contribution plans (other than state plans) or defined benefit plans (other than state plans) that:

- pool the assets contributed by various enterprises that are not under common control; and
- Use those assets to provide benefits to employees of more than one enterprise, on the basis that contribution and benefit levels are determined without regard to the identity of the enterprise that employs the employees concerned.

Other long-term employee benefits are employee benefits (other than post-employment benefits and termination benefits) which do not fall due wholly within twelve months after the end of the period in which the employees render the related service.

Termination benefits are employee benefits payable as a result of either:

- an enterprise's decision to terminate an employee's employment before the normal retirement date; or
- An employee's decision to accept voluntary redundancy in exchange for those benefits (voluntary retirement).

Vested employee benefits are employee benefits that are not conditional on future employment.

The ***present value of a defined benefit obligation*** is the present value, without deducting any plan assets, of expected future payments required to settle the obligation resulting from employee service in the current and prior periods.

Current service cost is the increase in the present value of the defined benefit obligation resulting from employee service in the current period.

Interest cost is the increase during a period in the present value of a defined benefit obligation which arises because the benefits are one period closer to settlement.

Plan assets comprise assets held by a long-term employee benefit fund; and qualifying insurance policies.

Assets held by a long-term employee benefit fund are assets (other than non-transferable financial instruments issued by the reporting enterprise) that:

- are held by an entity (a fund) that is legally separate from the reporting enterprise and exists solely to pay or fund employee benefits; and
- are available to be used only to pay or fund employee benefits, are not available to the reporting enterprise's own creditors (even in bankruptcy), and cannot be returned to the reporting enterprise, unless either:
  (a) the remaining assets of the fund are sufficient to meet all the related employee benefit obligations of the plan or the reporting enterprise; or
  (b) The assets are returned to the reporting enterprise to reimburse it for employee benefits already paid.

The ***return on plan assets*** is interest, dividends and other revenue derived from the plan assets, together with realised and unrealised gains or losses on the plan assets, less any costs of administering the plan and less any tax payable by the plan itself.

Actuarial gains and losses comprise: (a) experience adjustments (the effects of differences between the previous actuarial assumptions and what has actually occurred); and (b) the effects of changes in actuarial assumptions.

Past service cost is the change in the present value of the defined benefit obligation for employee service in prior periods, resulting in the current period from the introduction of, or changes to, post-employment benefits or other long-term employee benefits. Past service cost may be either positive (where benefits are introduced or improved) or negative (where existing benefits are reduced).

Key Points

- When an employee has rendered service to an enterprise during an accounting period, the enterprise should recognise the undiscounted amount of short-term employee benefits expected to be paid in exchange for that service:

(a) As a liability (accrued expense), after deducting any amount already paid. If the amount already paid exceeds the undiscounted amount of the benefits, an enterprise should recognise that excess as an asset (prepaid expense) to the extent that the prepayment will lead to, for example, a reduction in future payments or a cash refund; and

(b) As an expense, unless another Accounting Standard requires or permits the inclusion of the benefits in the cost of an asset.

- An enterprise should recognise the expected cost of short-term employee benefits in the form of compensated absences as follows:

  (a) in the case of accumulating compensated absences, when the employees render service that increases their entitlement to future compensated absences; and

  (b) In the case of non-accumulating compensated absences, when the absences occur.

- An enterprise should measure the expected cost of accumulating compensated absences as the additional amount that the enterprise expects to pay as a result of the unused entitlement that has accumulated at the balance sheet date.
- An enterprise should recognise the expected cost of profit-sharing and bonus payments only when:

  (a) the enterprise has a present obligation to make such payments as a result of past events; and

  (b) A reliable estimate of the obligation can be made.

- A present obligation exists when, and only when, the enterprise has no realistic alternative but to make the payments.
- Post-employment benefit plans are classified as either defined contribution plans or defined benefit plans, depending on the economic substance of the plan as derived from its principal terms and conditions.
- An enterprise should classify a multi-employer plan as a defined contribution plan or a defined benefit plan under the terms of the plan (including any obligation that goes beyond the formal terms). Where a multi-employer plan is a defined benefit plan, an enterprise should account for its proportionate share of the defined benefit obligation, plan assets and cost associated with the plan in the same way as for any other defined benefit plan; and make appropriate disclosure.

- An enterprise should account for a state plan in the same way as for a multi-employer plan.
- An enterprise may pay insurance premiums to fund a postemployment benefit plan. The enterprise should treat such a plan as a defined contribution plan unless the enterprise will have (either directly, or indirectly through the plan) an obligation to either:
  (a) pay the employee benefits directly when they fall due; or
  (b) Pay further amounts if the insurer does not pay all future employee benefits relating to employee service in the current and prior periods. If the enterprise retains such an obligation, the enterprise should treat the plan as a defined benefit plan.
- When an employee has rendered service to an enterprise during a period, the enterprise should recognise the contribution payable to a defined contribution plan in exchange for that service:
  (a) As a liability (accrued expense), after deducting any contribution already paid. If the contribution already paid exceeds the contribution due for service before the balance sheet date, an enterprise should recognise that excess as an asset (prepaid expense) to the extent that the prepayment will lead to, for example, a reduction in future payments or a cash refund; and
  (b) as an expense, unless another Accounting Standard requires or permits the inclusion of the contribution in the cost of an asset
- Where contributions to a defined contribution plan do not fall due wholly within twelve months after the end of the period in which the employees render the related service, they should be discounted using the discount rate determined by reference to market yields at the balance sheet date on government bonds.
- An enterprise should disclose the amount recognised as an expense for defined contribution plans.
- An enterprise should account not only for its legal obligation under the formal terms of a defined benefit plan, but also for any other obligation that arises from the enterprise's informal practices. Informal practices give rise to an obligation where the enterprise has no realistic alternative but to pay employee benefits. An example of such an obligation is where a change in the enterprise's informal practices would cause unacceptable damage to its relationship with employees.

- The amount recognised as a defined benefit liability should be the net total of the following amounts:
  (a) the present value of the defined benefit obligation at the balance sheet date
  (b) minus any past service cost not yet recognised
  (c) Minus the fair value at the balance sheet date of plan assets (if any) out of which the obligations are to be settled directly.
- An enterprise should determine the present value of defined benefit obligations and the fair value of any plan assets with sufficient regularity that the amounts recognised in the financial statements do not differ materially from the amounts that would be determined at the balance sheet date.
- The amount of defined benefit liability may be negative (an asset). An enterprise should measure the resulting asset at the lower of:
  (a) the amount determined and
  (b) The present value of any economic benefits available in the form of refunds from the plan or reductions in future contributions to the plan. The present value of these economic benefits should be determined using the discount rate determined by reference to market yields at the balance sheet date on government bonds.
- An enterprise should recognise the net total of the following amounts in the statement of profit and loss, except to the extent that another Accounting Standard requires or permits their inclusion in the cost of an asset:
  (a) current service cost
  (b) interest cost
  (c) the expected return on any plan assets and on any reimbursement rights
  (d) actuarial gains and losses
  (e) past service cost
  (f) the effect of any curtailments or settlements and
  (g) The effect of the limit, i.e., the extent to which defined benefit liability exceeds the the present value of any economic benefits available in the form of refunds from the plan or reductions in future contributions to the plan.

- An enterprise should use the Projected Unit Credit Method to determine the present value of its defined benefit obligations and the related current service cost and, where applicable, past service cost.
- In determining the present value of its defined benefit obligations and the related current service cost and, where applicable, past service cost, an enterprise should attribute benefit to periods of service under the plan's benefit formula. However, if an employee's service in later years will lead to a materially higher level of benefit than in earlier years, an enterprise should attribute benefit on a straight-line basis from:
  (a) the date when service by the employee first leads to benefits under the plan (whether or not the benefits are conditional on further service); until
  (b) The date when further service by the employee will lead to no material amount of further benefits under the plan, other than from further salary increases.
- Actuarial assumptions comprising demographic assumptions and financial assumptions should be unbiased and mutually compatible. Financial assumptions should be based on market expectations, at the balance sheet date, for the period over which the obligations are to be settled.
- Post-employment benefit obligations should be measured on a basis that reflects:
  (a) estimated future salary increases;
  (b) the benefits set out in the terms of the plan (or resulting from any obligation that goes beyond those terms) at the balance sheet date; and
  (c) estimated future changes in the level of any state benefits that affect the benefits payable under a defined benefit plan, if, and only if, either:

  (i) Those changes were enacted before the balance sheet date; or

  (ii) Past history, or other reliable evidence, indicates that those state benefits will change in some predictable manner, for example, in line with future changes in general price levels or general salary levels.

- Assumptions about medical costs should take account of estimated future changes in the cost of medical services, resulting from both inflation and specific changes in medical costs.
- Actuarial gains and losses should be recognised immediately in the statement of profit and loss as income or expense

- In measuring its defined benefit liability under paragraph 55, an enterprise should recognise past service cost as an expense on a straight-line basis over the average period until the benefits become vested. To the extent that the benefits are already vested immediately following the introduction of, or changes to, a defined benefit plan, an enterprise should recognise past service cost immediately.
- When, and only when, it is virtually certain that another party will reimburse some or all of the expenditure required to settle a defined benefit obligation, an enterprise should recognise its right to reimbursement as a separate asset. The enterprise should measure the asset at fair value. In all other respects, an enterprise should treat that asset in the same way as plan assets. In the statement of profit and loss, the expense relating to a defined benefit plan may be presented net of the amount recognised for a reimbursement.
- The expected return on plan assets is a component of the expense recognised in the statement of profit and loss. The difference between the expected return on plan assets and the actual return on plan assets is an actuarial gain or loss.
- An enterprise should recognise gains or losses on the curtailment or settlement of a defined benefit plan when the curtailment or settlement occurs. The gain or loss on a curtailment or settlement should comprise:
  (a) any resulting change in the present value of the defined benefit obligation;
  (b) any resulting change in the fair value of the plan assets;
  (c) Any related past service cost that had not previously been recognised.
- Before determining the effect of a curtailment or settlement, an enterprise should remeasure the obligation (and the related plan assets, if any) using current actuarial assumptions (including current market interest rates and other current market prices).
- An enterprise should disclose information that enables users of financial statements to evaluate the nature of its defined benefit plans and the financial effects of changes in those plans during the period.

E.2. AS 29 Provisions, Contingent Liabilities and Contingent Assets

The objective of this Standard is to ensure that appropriate recognition criteria and measurement bases are applied to provisions and contingent liabilities and that sufficient information is disclosed in the notes to the financial statements to enable users to understand their nature,

timing and amount. This Standard should be applied in accounting for provisions and contingent liabilities and in dealing with contingent assets, except:

(a) those resulting from financial instruments that are carried at fair value;
(b) those resulting from executory contracts, except where the contract is onerous;
(c) those arising in insurance enterprises from contracts with policy-holders; and
(d) Those covered by another Accounting Standard.

Important Terms

A ***provision*** is a liability which can be measured only by using a substantial degree of estimation.

A ***liability*** is a present obligation of the enterprise arising from past events, the settlement of which is expected to result in an outflow from the enterprise of resources embodying economic benefits.

An ***obligating event*** is an event that creates an obligation that results in an enterprise having no realistic alternative to settling that obligation.

A ***contingent liability*** is:

(a) a possible obligation that arises from past events and the existence of which will be confirmed only by the occurrence or non-occurrence of one or more uncertain future events not wholly within the control of the enterprise; or
(b) a present obligation that arises from past events but is not recognized because:
    - it is not probable that an outflow of resources embodying economic benefits will be required to settle the obligation; or
    - A reliable estimate of the amount of the obligation cannot be made.

A ***contingent asset*** is a possible asset that arises from past events the existence of which will be confirmed only by the occurrence or non-occurrence of one or more uncertain future events not wholly within the control of the enterprise.

Present obligation - an obligation is a present obligation if, based on the evidence available, its existence at the balance sheet date is considered probable, i.e., more likely than not.

Possible obligation - an obligation is a possible obligation if, based on the evidence available, its existence at the balance sheet date is considered not probable.

A ***restructuring*** is a programme that is planned and controlled by management, and materially changes either:

- the scope of a business undertaken by an enterprise; or
- The manner in which that business is conducted.

Key Points

- A provision should be recognized when:
  - an enterprise has a present obligation as a result of a past event;
  - it is probable that an outflow of resources embodying economic benefits will be required to settle the obligation; and
  - A reliable estimate can be made of the amount of the obligation.

If these conditions are not met, no provision should be recognised.

- The amount recognised as a provision should be the best estimate of the expenditure required to settle the present obligation at the balance sheet date. The amount of a provision should not be discounted to its present value.
- The risks and uncertainties that inevitably surround many events and circumstances should be taken into account in reaching the best estimate of a provision.
- Future events that may affect the amount required to settle an obligation should be reflected in the amount of a provision where there is sufficient objective evidence that they will occur.
- Gains from the expected disposal of assets should not be taken into account in measuring a provision.
- Where some or all of the expenditure required to settle a provision is expected to be reimbursed by another party, the reimbursement should be recognized when, and only when, it is virtually certain that reimbursement will be received if the enterprise settles the obligation. The reimbursement should be treated as a separate asset. The amount recognized for the reimbursement should not exceed the amount of the provision.
- In the statement of profit and loss, the expense relating to a provision may be presented net of

the amount recognized for a reimbursement.

- Provisions should be reviewed at each balance sheet date and adjusted to reflect the current best estimate. If it is no longer probable that an outflow of resources embodying economic benefits will be required to settle the obligation, the provision should be reversed.
- A provision should be used only for expenditures for which the provision was originally recognized.
- Provisions should not be recognized for future operating losses.
- No obligation arises for the sale of an operation until the enterprise is committed to the sale, i.e., there is a binding sale agreement
- A restructuring provision should include only the direct expenditures arising from the restructuring which are those that are both:

  (a) Necessarily entailed by the restructuring; and

  (b) Not associated with the ongoing activities of the enterprise

- An enterprise should not recognize a contingent liability.
- Unless the possibility of any outflow in settlement is remote, an enterprise should disclose for each class of contingent liability at the balance sheet date a brief description of the nature of the contingent liability and, where practicable:

  (a) An estimate of its financial effect

  (b) An indication of the uncertainties relating to any outflow; and

  (c) The possibility of any reimbursement.

- An enterprise should not recognize a contingent asset.

E.3. AS 22- Accounting for Taxes on Income

The objective of this Standard is to prescribe accounting treatment for taxes on income. In accordance with the matching concept, taxes on income are accrued in the same period as the revenue and expenses to which they relate. Matching of such taxes against revenue for a period

poses special problems arising from the fact that in a number of cases, taxable income may be significantly different from the accounting income.

Important Terms

Accounting income (loss) is the net profit or loss for a period, as reported in the statement of profit and loss, before deducting income tax expense or adding income tax saving.

Taxable income (tax loss) is the amount of the income (loss) for a period, determined in accordance with the tax laws, based upon which income tax payable (recoverable) is determined.

Tax expense (tax saving) is the aggregate of current tax and deferred tax charged or credited to the statement of profit and loss for the period.

Current tax is the amount of income tax determined to be payable (recoverable) in respect of the taxable income (tax loss) for a period.

Deferred tax is the tax effect of timing differences.

Timing differences are the differences between taxable income and accounting income for a period that originate in one period and are capable of reversal in one or more subsequent periods.

Permanent differences are the differences between taxable income and accounting income for a period that originate in one period and do not reverse subsequently.

Key Points

- Tax expense for the period, comprising current tax and deferred tax, should be included in the determination of the net profit or loss for the period.
- Deferred tax should be recognized for all the timing differences, subject to the consideration of prudence in respect of deferred tax assets
- Deferred tax assets should be recognized and carried forward only to the extent that there is a reasonable certainty that sufficient future taxable income will be available against which such deferred tax assets can be realized.
- Where an enterprise has unabsorbed depreciation or carry forward of losses under tax laws, deferred tax assets should be recognized only to the extent that there is virtual certainty supported by convincing evidence that sufficient future taxable income will be available against which such deferred tax assets can be realized.
- Current tax should be measured at the amount expected to be paid to (recovered from) the taxation authorities, using the applicable tax rates and tax laws.

- Deferred tax assets and liabilities should be measured using the tax rates and tax laws that have been enacted or substantively enacted by the balance sheet date.
- Deferred tax assets and liabilities should not be discounted to their present value.
- The carrying amount of deferred tax assets should be reviewed at each balance sheet date. An enterprise should write-down the carrying amount of a deferred tax asset to the extent that it is no longer reasonably certain that sufficient future taxable income will be available against which deferred tax asset can be realized. Any such write-down may be reversed to the extent that it becomes reasonably certain or virtually certain.
- An enterprise should offset assets and liabilities representing current tax if the enterprise: has a legally enforceable right to set off the recognized amounts; and intends to settle the asset and the liability on a net basis.
- An enterprise should offset deferred tax assets and deferred tax liabilities if: the enterprise has a legally enforceable right to set off assets against liabilities representing current tax and the deferred tax assets and the deferred tax liabilities relate to taxes on income levied by the same governing taxation laws.
- Deferred tax assets and liabilities should be distinguished from assets and liabilities representing current tax for the period. Deferred tax assets and liabilities should be disclosed under a separate heading in the balance sheet of the enterprise, separately from current assets and current liabilities.
- The break-up of deferred tax assets and deferred tax liabilities into major components of the respective balances should be disclosed in the notes to accounts.
- The nature of the evidence supporting the recognition of deferred tax assets should be disclosed, if an enterprise has unabsorbed depreciation or carry forward of losses under tax laws.

Guidance Notes by ICAI

Besides Accounting Standards, ICAI has also issue Guidance Notes on accounting aspects to provide guidance to members and preparers of financial statements, on matters which may arise in the course of their professional work and on which they may desire assistance in resolving issues which may pose difficulty. Guidance Notes are generally recommendatory in nature. A member should ordinarily follow recommendations in a guidance note relating to an auditing matter except where he is satisfied that in the circumstances of the case, it may not be necessary to do so. Similarly, while discharging his attest function, a member should examine whether the recommendations in a guidance note relating to an accounting matter have been followed or not. The list of Guidance Notes on Accounting Issued by ICAI is as follows:

- Guidance Note on Accounting for Derivative Contracts (Revised 2021)
- Guidance Note on Accrual Basis of Accounting
- Guidance Note on Accounting by E-commerce Entities
- Guidance Note on Applicability of AS 25 and Measurement of Income Tax Expense for Interim Financial Reporting (Revised 2020)
- Guidance Note on Accounting for Share-based Payments (Revised 2020)
- Guidance Note on Accounting for Oil and Gas Producing Activities (Ind AS)
- Guidance Note on Combined and Carve–Out Financial Statements (September 2016)
- Guidance Note on Accounting for Depreciation in companies in the context of Schedule II to the Companies Act, 2013
- Guidance Note on Accounting for Expenditure on Corporate Social Responsibility Activities (Issued May 15, 2015)
- Guidance Note on Accounting for Oil and Gas Producing Activities (revised 2013)
- Guidance Note on Accounting for Corporate Dividend Tax
- Guidance Note on Accounting Treatment for Excise Duty
- Guidance Note on Accounting for State-level Value Added Tax
- Guidance Note on Accounting by Schools

- Guidance Note on Accounting for Credit Available in Respect of Minimum Alternative Tax under the Income-tax Act, 1961
- Guidance Note on Accounting for Real Estate Transactions (Revised 2012)
- Guidance Note on Accounting Treatment for MODVAT/CENVAT
- Guidance Note on Turnover in case of Contractors
- Guidance Note on Accounting for Rate Regulated Activities
- Guidance Note on Accounting for Self-generated Certified Emission Reductions (CERs) (Issued 2012)
- Guidance Note on Accounting and Auditing of Political Parties

Important Links For:

- Announcement Criteria for classification of Non-company entities for applicability of Accounting Standards dated https://resource.cdn.icai.org/64269asb51535.pdf
- Compendium of Accounting Standards: https://resource.cdn.icai.org/56169asb45450.pdf
- For Companies (Accounting Standards) Rules, 2021

  https://mca.gov.in/bin/dms/getdocument?mds=RKk43Bmg99ksfV0bUGr6XA%253D%253D&type=open

- For Ind AS: https://www.mca.gov.in/MinistryV2/Stand.html
- For ASLB https://www.icai.org/post/accounting-standards-for-local-bodies
- For Guidance Notes https://www.icai.org/post/list-of-guidance-notes-on-accounting-aspects
- http://gasab.gov.in/gasab/
- https://mca.gov.in/
- https://www.icai.org/