ADVANCED ACCOUNTING

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PREFACE

It is a matter of great pleasure for us to present this book to our esteemed readers and students. This book has been designed as standard text on 'Advanced Accounting' for Third Year B. Com.

This book comprehensively covers the entire syllabus of T. Y. B. Com. Course of University of Pune w. e. f. June-2015. It has been written to meet the requirement of students. The special features of the book are :

- Full coverage of the revised syllabus.
- Chapter outline at the beginning of each chapter to give a bird's eye view of the topics covered in the chapter.
- Point wise explanation of each topic in the chapter.
- Topics are logically arranged in numbered paragraphs exactly according to the modified syllabus.
- Proposed questions at the end of each chapter.
- Extensive use of diagrams, tables and various forms to give visual view of key concepts and techniques.
- Conversional, lucid and simple language.

Every effort has been made to provide the readers with most up-to-date and authentic material on the subject.

We are very grateful to our publisher Mr. Dattatray Pashte of Diamond Publication, Pune who have rendered all possible assistance in bringing out this book. We wish to acknowledge our deep gratitude to staff who have assisted and helped us in preparing this book.

We will consider our efforts amply rewarded in case the book proves useful to the students and Faculty Members of the subject.

Suggestions of readers are welcome and shall be acknowledged with gratitude.

With best wishes.

Prin. Dr. Kishor N. Jagtap
Dr. Sunil D. Zagade
Dr. Haribhau M. Jare
Prof. N. K. Aher

CHAPTER **1**

Accounting Standards And Financial Reporting (IFRS)

(A) Accounting Standards
Introduction
1.1 Accounting Stardard on Cash Flow Statements (AS-3)
1.2 Accounting Stardard - 7 (AS - 7)
1.3 Accounting Standard - 8 (AS - 8)
1.4 Accounting Standard - 12 (AS - 12)
1.5 Accounting Standard - 15 (AS - 15)
1.6 Accounting Standard - 17 (AS - 17)
1.7 Accounting Standard - 18 (AS - 18)
1.8 Accounting Standard - 19 (AS - 19)
1.9 Accounting Standard - 20 (AS-20)
1.10 Accounting Standard - 21 (AS - 21)
1.11 (As - 22) (Issued 2001) - Accounting for Taxes On Income
1.12 Accounting Standard (As - 23) (Issued In 2001)— Accounting for Investments in Associates in Consolidated Financial Statements (AS-23)
1.13 Accounting Standard (As - 24) (Issued 2002) - Discontinuing Operations (AS-24)
1.14 Accounting Standard 25 (As - 25) Interim Financial Reporting (AS-25)
1.15 Accounting Standards - 26 (AS - 26)
(B) IFRS (International Financial Reporting of Standards)

Introduction :

Accounting standards constitute policy procedures and accounting rules focusing on valuation, disclosure and measurement. Accounting Standards are issued by the Accounting standards Board established by The Institute of Chartered Accountants of India (ICAI). Accounting standards acts as a conflict resolving device among different accounting practices and provides a sounds framework for ideal accounting methods suitable for various types of businesses.

1.1 Accounting Stardard on Cash Flow Statements - 3 (AS - 3) :

Following are the salient features of the Revised Accounting Standard 3 (AS 3 Revised) Cash Flow Statements, issued by the Council of the Institute of Chartered Accounts of India. This Standard supersedes AS 3, Changes in Financial Position, issued in June, 1981.

The standard has been made mandatory w.e.f. accounting periods commencing on or after 1 st April 2001, in respect of the following :

(i) Enterprises whose debt or equity securities are listed or to be listed on a recognised stock exchange in India, and

(ii) All other commercial, business or industrial enterprises whose turnover for the accounting period exceeds Rs. 50 crores.

1. Objectives

Information about the cash flows of an enterprise is useful in providing users of financial statement with a basis to assess the ability of the enterprise to generate cash and cash equivalents and the needs of the enterprise to utilise those cash flows. The economic decisions that are taken by users require an evaluation of the ability of an enterprise to generate cash and cash equivalents and the timing and certainty of their generation.

The Statement deals with provision of information about the historical changes in cash and cash equivalents of an enterprise by means of a cash flow statement which classifies cash flows during the period from operating, investing and financial activities.

2. Scope

1. An enterprise should prepare a cash flow statement and should present it for each period for which financial statements are presented.
2. Users of an enterprise's financial statements are interested in how the enterprise generates and uses cash and equivalents. This is the case regardless of the nature of the enterprise's activities and irrespective of whether cash can be viewed as the product of the enterprise, as may be the case with a financial enterprise. Enterprises need cash for essentially the same reasons, however different their principal revenue-producing activities might be. They need cash to conduct their operations, to pay their obligations, and to provide returns to their investors.

3. Benefits of Cash Flow Information

1. A cash flow statement, when used in conjunction with the other financial statements, provides information that enables users to evaluate the changes in net assets of an enterprise, its financial structure (including its liquidity and solvency), and its ability to affect the amounts and timing of cash flows in order to adapt to changing circumstances and opportunities. Cash flow information is useful in assessing the ability of the enterprise to generate cash and cash equivalents and enables users to develop models to assess and compare the present value of the future cash flows of different enterprises.
2. It also enhances the comparability of the reporting of operating performance by different enterprises because it eliminates the effects of using different accounting

treatment for the same transactions and events.

3. Historical cash flow information is often used as an indicator of the amount, timing and certainty of future cash flows. It is also useful in checking the accuracy of past assessments of future cash flows and in examining the relationship between profitability and net cash flow and the impact of changing prices.

4. Definitions

The following terms are used in this Statement with the meanings specified: (1) Cash comprises cash on hand and demand deposits with banks. (2) 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. (3) Cash flows are inflows and outflows of cash and cash equivalents. (4) Operating activities are the principal revenue-producing activities of the enterprise and other activities that are not investing or financing activities. (5) Investing activities are the acquisition and disposal of long-term assets and other investments not included in cash equivalents. (6) Financing activities are activities that result in changes in the size and composition of the owner's capital (including preference share capital in the case of a company) and borrowings of the enterprise.

5. Presentation of a Cash Flow Statement

The cash flow statement should report cash flows during the period classified by operating, investing and financing activities.

(1) Operating Activities : Cash flows from operating activities are primarily derived from the principal revenue-producing activities of the enterprise. Therefore, they generally result from the transactions and other events that enter into the determination of net profit or loss. Examples of cash flows from operating activities are: (a) Cash receipts from the sale of goods and the rendering of services; (b) Cash receipt from royalties, fees, commissions and other revenue; (c) Cash payments to suppliers for goods and services; (d) Cash payments to and on behalf of employees;

(2) Investing Activities : Examples of cash flows arising from investing activities are:

(a) Cash payments to acquire fixed assets (including intangibles). These payments include those relating to capitalised research and development costs and self-constructed fixed assets;
(b) Cash receipts from disposal of fixed assets (including intangibles);
(c) Cash payments to instruments of other enterprises and interests in joint ventures (other than payments for those instruments considered to be cash equivalents and those held for dealing or trading purposes);
(d) Cash receipts from disposal of shares, warrants, or debt instruments of other enterprises and interests in joint venture (other than receipts from those instruments considered to be cash equivalents and those held for dealing or trading purposes);
(e) Cash advances and loans made to third parties (other than advances and loans made by a financial enterprise);
(f) Cash receipts from the repayment of advances and loans made to third parties (other than advances and loans of a financial enterprise);

(g) Cash payments for futures contracts, forward contracts, option contracts, and swap contracts except when the contracts are held for dealing or trading purpose, or the payments are classified as financing activities.

(3) Financing Activities : Examples of cash flows arising from financing activities are:

(a) Cash proceeds from issuing shares or other similar instruments;

(b) Cash proceeds from issuing debentures, loans, notes, bonds and other short or long-term borrowing; and

(c) Cash repayments of amounts borrowed.

(4) Reporting Cash Flows from Operating Activities

(1) 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.

(2) The direct method provides information which may be useful in estimating future cash flows and which is not available under the indirect method and is, therefore, considered more appropriate than the indirect method. Under the direct method, information about major classes of gross cash receipts and gross cash payments may be obtained either :

(a) from adjusting sales, cost of sales (interest and similar income and interest expense and similar charges for a financial enterprise) and other items in the statement of profit and loss for:

(i) changes during the period in inventories and operating receivables and payables;

(ii) other non-cash items; and

(iii) other items for which the cash effects are investing or financing cash flows.

(3) Under the indirect method, the net cash flow from operating activities is determined by adjusting net profit or loss for the effects of:

(a) changes during the period in inventories and operating receivables and payables;

(b) non-cash items such as depreciation, provisions, deferred taxes, and unrealised foreign exchange gains and losses; and

(c) all other items for which the cash effects are investing or financing cash flows.

(4) Alternatively, the net cash flow operating activities may be presented under the indirect method by showing the operating revenues and expenses, excluding non-cash items disclosed in the statement of profit and loss and the changes during the period in inventories and operating receivables and payables.

(5) Reporting Cash flows from Investing and Financing Activities : An enterprise should report separately major classes of gross cash receipts and gross cash payments arising from investing and financing activities, except to the extent that cash flows described in Paragraph (6) are reported on a net basis.

(6) Reporting Cash Flows on a Net Basis

(1) Cash flows arising from the following operating, investing on financing activities may be reported on a net basis:

(a) Cash receipts and payments on behalf of customers when the cash flows reflect activities of the customer rather than those of the enterprise,

Example of cash receipts and payments referred to above are :

(i) the acceptance and repayment of demand deposits by a bank ;

(ii) funds held for customers by an investment enterprise; and

(iii) rents collected on behalf of, and paid over to, the owners of properties.

(b) Cash receipts and payments for items in which the turnover is quick, the amounts are large, and the maturities are short.

Examples of cash receipts and payments referred to above are advances made for, and the repayments of:

(i) principal amounts relating to credit card customers;

(ii) the purchases and sales of investments; and

(iii) other short-term borrowings, for example those which have a maturity period of three months or less.

(2) Cash flows arising from each of the following activities of a financial enterprise may be reported on a net basis :

(a) cash receipts and payments for the acceptance and repayment of deposits with a fixed maturity date;

(b) the placement of deposits with and withdrawal of deposits from other financial enterprises; and

(c) cash advances and loans made to customers and the repayments of the those advances and loans.

(7) 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 ia 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.

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

(9) Interest and Dividends : Cash flows from interest and dividends received and paid should each be disclosed separately. Cash flows arising from interest paid and interest and

dividends received in the case of a financial enterprise should be classified as cash flows arising from operating activities. In the case of other enterprises, cash flows arising from interest paid should be classified as cash flows from financing activities while interest and dividends received should be classified as cash flows from investing activities. Dividends paid should be classified as cash flows from financing activities.

(10) Taxes on Income : Cash flows arising from taxes on income should be separately disclosed and should be classified as cash flows from operating activities unless they can be specifically identified with financing and investing activities.

(11) 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.

(12) Acquisitions and Disposals of Subsidiaries and other Business Units :

(1) 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.

(2) 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 :
   (a) the total purchase or disposal consideration ; and
   (b) the portion of the purchase or disposal consideration discharged by means of cash and cash equivalents.

(13) Non-cash Transactions : Investing and financing transactions that do not require the use of cash or cash equivalents should be excluded from a cash flow statement. Such transactions should be disclosed elsewhere in the financial statements in a way that provides all the relevant information about these investing and financing activities.

(14) Disclosure

(1) Components of cash and cash equivalents : An enterprise should disclose the components of cash and cash equivalent and should present a reconciliation of the amounts in its cash flow statement with the equivalent items reported in the balance sheet.

(2) Other Disclosures : 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.

1.2 Accounting Stardard - 7 (AS - 7)

Accounting for Construction Contracts

The salient features of AS: 7 are as follows:

1. In accounting for construction contracts in financial statements, either the percentage of completion method or the completed contract method may be used. When a contractor uses a particular method of accounting for a contract, then the same method

should be adopted for all other contracts which meet similar criteria.

2. The percentage of completion method can be used if the outcome of the contract can be reliably estimated.
   (a) In the case of fixed price contracts, this degree of reliability would be provided if the following conditions are satisfied:
      (i) total contract revenues to be received can be reliably estimated.
      (ii) both the costs to complete the contract and the stage of contract performance completed at the reporting date can be reasonably estimated; and
      (iii) the costs attributable to the contract can be clearly identified so that actual expenditure can be compared with prior estimates.
   (b) Profit in the case of fixed price contracts normally should not be recognised unless the work on a contract has progressed to a reasonable extent.
   (c) In the case of cost plus contracts, this degree of reliability would be provided only if both the following conditions are satisfied:
      (i) Costs attributable to the contract can be clearly identified; and
      (ii) costs other than those that are specifically reimbursable under the contract can be reliably estimated.
   (d) While recognising the profit under percentage of completion method, an appropriate allowance for future enforceable factors should be made on either a specific or a percentage basis.
3. The costs included in the amount at which construction contract work is stated should comprise those costs that relate directly to a specific contract and those that are attributable to the contract activity in general and can be allocated to specific contracts.
4. A foreseeable loss on the entire contract should be provided for in the financial statements irrespective of the amount of work done and the method of accounting followed.
5. There should be disclosure in the financial statements of:
   (i) the amount of construction work-in-progress;
   (ii) progress payments received and auvances and retentions on account of contracts included in construction work-in-progress; and
   (iii) the amount receivable in respect of income accrued under cost plus contracts not included in construction work-in-progress.

   If both the percentage of completion method and the completed contract method are simultaneously used by the contractor, the amount of contract work described in (i) above should be analysed to disclose separately, the amounts attributable to contracts accounted for under each method.
6. Disclosure of changes in an accounting policy used for construction contracts should be made in the financial statements giving the effect of the change and its amount. However, if a contractor changes from the percentage of completion method to the

completed contract method for contracts-in-progress at the beginning of the year, it may not be possible to quantify the effect of the changes. In such cases, disclosure should be made of the amount of attributable profits reported in prior years in respect of contracts-in-progress at the beginning of the accounting period..

The standard has become mandatory in respect of accounts for the period commencing on or after 1-4-1991.

1.3 Accounting Standard - 8 (AS - 8) (Withdrawn and Included in As 26)

Accounting for Research and Development

The salient features of AS: 8 are as follows:

1. Research and development costs should include:
   (i) salaries, wages and other related costs of personnel engaged in research and development;
   (ii) depreciation of building, equipment and facilities which have alternative economic use, to the extent they are used for research and development;
   (iii) an appropriate amortisation of the cost of building, equipment and facilities which have no alternative economic use, to the extent they are used for research and development;
   (iv) overhead costs related to research and development; and
   (v) payment to outside bodies for research and development projects related to the enterprise.
2. Amount of research and development cost described in paragraph 1 should be charged as an expense of the period in which they are incurred except where such costs may be deferred in accordance with paragraph 3.
3. Research and development costs of project may be deferred to future periods if the following criteria are satisfied :
   (i) The-product or process is clearly defined and the costs attributable to the product or process can be separately identified:
   (ii) the technical feasibility of the product or process has been demonstrated;
   (iii) the management of the enterprise has indicated its intention to produce and market, or use, the product or process;
   (iv) there is a reasonable indication that current and future research and development costs to be incurred on the project together with expected production, selling and administration costs are likely to be more than covered by related future revenues/benefits; and
   (v) adequate resources exist, or are reasonably expected to be available, to complete the project and market the product or process.
4. Wherever research and developments are deferred, the appropriate legal requirements should also be taken into account.

5. If an accounting policy of deferral of research and development costs is adopted, it should be applied to all such projects that meet the criteria in paragraph 1, given above.
6. If research and development costs of a project are deferred, they should be allocated on a systematic basis to future accounting periods by reference either to the sale or use of the product or process to the time period over which the product or process is expected to be sold or used.
7. The deferred research and development costs of a project should be reviewed at the end of each accounting period. When the criteria of paragraph 3, which previously justified the deferral of the costs, no longer apply, the unamortised balance should be charged as an expense immediately, When the criteria for deferral continue to be met but the amount of unamortised balance of the deferred research and development costs and other relevant costs exceed the expected future revenues/benefits related thereto, such expenses should be charged as an expense immediately.
8. Research and development costs once written off should not be reinstated even though the uncertainties which had led to their being written off no longer exist.
9. The total of research and development costs, including the amortised portion of deferred costs, charged as expense should be disclosed in the Profit and Loss Account for the period.
10. Deferred research and development expenditure should be separately disclosed in the balance sheet under the head "Miscellaneous Expenditure."
    This standard has become mandatory in respect of account for periods commencing on or after 1-4-1991.

1.4 Accounting Standard - 12 (AS - 12)

"Accounting for Government Grants"

The Council of the Institute of Chartered Accountants of India has issued .-AS 12: Accounting for Government Grants. The standard has come into effect in respect of accounting periods commencing on or after the 1st April 1992. It was recommendatory in nature for initial period of two years. The standard has become mandatory in respect of accounts for periods commencing on or after the 1st April, 1994.

The salient features of AS-12 are as follows:

1. Introduction : This standard deals with accounting for government grants. Government grants are sometimes, called by other names such as subsidies, cash incentives, duty drawbacks, etc.

2. Definitions : The following terms are used in this Standard with the meanings specified:

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

(ii) 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.

3. Accounting Treatment : Two broad approaches may be followed for the accounting treatment of government grants: the 'capital approach', under which a grant is treated as part of shareholders' funds, and the 'income approach', under which a grant is taken to income over one or more periods.

It is generally considered appropriate that accounting for government grant would be based on the nature of the relevant grant. Grants which have the characteristics similar to those of promoter's contribution should be treated as part of shareholders' funds. Income approach may be more appropriate in the case of other grants.

4. Recognition of Government Grants : Government grants available to the enterprise are considered for inclusion in accounts only when the following conditions are satisfied:

(i) Where there is reasonable assurance that the enterprise will comply with the conditions attached to them; and

(ii) Where such benefits have been earned by the enterprise and it is reasonably certain that the ultimate collection will be made.

Mere receipt of a grant is not necessarily a conclusive evidence that conditions attaching to the grant have been or will be fulfilled.

5. Presentation of Government Grants related to Specific Fixed Assets : Grants related to specific fixed assets are government grants whose primary condition is that an enterprise qualifying for them should purchase, construct or otherwise acquire such assets. Other conditions may also be attached restricting the type or location of the assets of the periods during which they are to be acquired or held.

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 recognised 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 nondepreciable 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 grants 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 bf separately disclosed in the financial statements.

6. Presentation of Government Grants related to Revenue : Government grants related to revenue should be recognised on a systematic basis in the Profit & 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.

7. Presentation of Government Grants of the nature of Promoter's Contribution : These are grants which are given with reference to the total investment in an undertaking or by way of contribution towards its total capital outlay (e.g. Central Investment Subsidy Scheme). No repayment is ordinarily expected in respect of such grants. Government grants of the nature of promoter's contribution should be credited to capital reserve and treated as a part of shareholders' funds.

8. Non-Monetary Government Grants : These are the grants which take the form of non-monetary assets such as land or other resources given at concessional rates. These grants should be accounted for by recording the assets so acquired at their acquisition costs. If a non-monetary asset is given free of cost, it should be recorded at a nominal value.

9. Government grants as Compensation for Expenses or Losses : 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 recognised and disclosed in the profit and loss statement of the period in which they are receivable, as an extraordinary item, if appropriate. [Accounting Standard (AS) 6: Prior Period and Extraordinary Items and Changes in Accounting Policies].

10. Contingency as to Government Grant : A contingency related to a government grant, arising after the grant has been recognised, should be treated in accordance with Accounting Standard (AS) 4: Contingencies and Events Occurring After the Balance Sheet Date.

11. Refund of Government Grants, (a) Government grants sometimes become refundable because certain conditions are not fulfilled. Such grants that become refundable should be accounted for as an extraordinary item.(Refer Accounting Standard (AS) 5: Prior Period and Extraordinary Items and Changes in Accounting Policies).

(b) The amount refundable in respect of a grant related to revenue should be applied first against any unamortised credit remaining in respect of the grant. To the extent that the amount refundable exceeds any such deferred credit, or where no deferred credit exists, the amount should be charged to Profit & 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. Government grants in the nature of promoters' contribution that becomes refundable should be reduced from the capital reserve.

12. Disclosure. The following disclosures are to be made:,

(i) This accounting policy adopted for government grants, including the methods of presentation in the financial statements: and

(ii) The nature and extent of government grant recognised in the financial statements, including grants of non-monetary assets given at a concessional rate or free of cost.

1.5 Accounting Standard - 15 (AS - 15)

Accounting for Retirement Benefits in the Financial Statement of Employers1

The following are the salient features of Accounting Standard 15 (AS: 15), "Accounting for Retirement Benefits in the Financial Statements of Employers", issued by the Council of the Institute of Chartered Accountants of India.

The Standard has come into effect in respect of accounting periods commencing on or after 1.4.1995 and is of mandatory nature.

1. Introduction : Retirement benefits usually consist of:

(a) Provident fund,
(b) Superannuation/pension,
(c) Gratuity,
(d) Leave encashment benefit on retirement,
(e) Post-retirement health and welfare schemes, and
(f) Other retirement benefits.

2. Definitions :

(i) Retirement benefit schemes are arrangements to provide provident fund, superannuation or pension, gratuity, or other benefits to employees on leaving service or retiring or, after an employee's death, to his or her dependants.

(ii) Defined contribution schemes are retirement benefit schemes under which amounts to be paid as retirement benefits are determined by contributions to a fund together with earnings thereon.

(iii) Defined benefit schemes are retirement benefit schemes under which amounts to be paid as retirement benefits are determinable usually by reference to employee's earnings and/or years of service.

(iv) Actuary means an actuary within the meaning of sub-section (1) of Section (2) of the Insurance Act, 1938.

(v) Actuarial valuation is the process used by an actuary to estimate the present value of benefits to be paid under a retirement benefit scheme and the present values of the scheme assets, land, sometimes, of future contributions.

(vi) Pay-as-you-go is a method of recognising the cost of retirement benefits only at the time payments are made to employees on, or after, their retirement.

3. Accounting Standard

(i) In respect of retirement benefits in the form of provident fund and other defined contribution schemes, the contributidn payable by the employer for a year should be charged to the statement of profit and loss for the year. Thus, besides the amount of contribution paid, a shortfall of the amount of contribution paid compared to the amount payable for the year

should also be charged to the statement of profit and loss for the year. On the other hand, if contribution paid is in excess of the amount payable for the year, the excess should be treated as a pre-payment.

(ii) In respect of gratuity benefit and other defined benefit schemes, the accounting treatment will depend on the type of arrangement which the employer has chosen to make.

(a) If the employer has chosen to make payment for retirement benefits out of his own funds, an appropriate charge to the statement of profit and loss for the year should be made through a provision for the accruing liability. The accruing liability should be calculated according to actuarial valuation. However, those enterprises which employ only a few persons may calculate the accrued liability by reference to any other rational method, e.g., a method based on the assumption that such benefits are payable to all employees at the end of the accounting year.

(b) In case the liability for retirement benefits is funded through creation of a trust, the cost incurred for the year should be determined actuarially. Such actuarial valuation should normally be conducted at least once in every three years. However, where the actuarial valuations are not conducted annually, the actuarial report should specify the contributions to be made by the employer on annual basis during the inter-valuation period.

The annual contribution (which is in addition to the contribution that may be required to finance unfunded past service cost) reflects proper accrual of retirement benefit cost for each of the years during the inter-valuation period and should be charged to the statement of profit and loss for each such year. Where the contribution paid during a year is lower than the amount required to be contributed during the year to meet the accrued liability as certified by the actuary, the shortfall should be charged to the statement of profit and loss for the year. Where the contribution during a year is in excess of the amount required to be contributed during the year to meet the accrued liability as by the actuary, the excess should be treated as a pre-payment.

(c) In case the liability for retirement benefits is funded through a scheme administered by an insurer, an actuarial certificate or a confirmation from the insurer should be obtained that the contribution payable to the insurer is the appropriate accrual of the liability for the year. Where the contribution paid during a year is lower than the amount required to be contributed during the year to meet the accrued liability, as certified by the actuary or confirmed by the insurer, as the case may be, the shortfall should be charged to the statement of excess of the amount required to be contributed during the year to meet the accrued liability as certified by the actuary or confirmed by the insurer, as the case may be, the excess should be treated as a pre-payment.

(iii) Any alterations in the retirement benefit costs arising from -

(a) introduction of a retirement benefit scheme for existing employees or making of improvements to an existing scheme or

(b) changes in the actuarial method used or assumptions adopted, should be charged or credited to the statement of profit and loss as they arise in accordance with Accounting Standard-5 (AS-5), "Prior Period in Extraordinary Items and Changes in Accounting Policies".

Additionally, a change in the actuarial method used should be treated as a change in an accounting policy and disclosed in accordance with Accounting Standard (AS-5) "Prior Period and Extraordinary items and Changes in Accounting Policies."

(iv) When a retirement benefit scheme is amended with the result that additional benefits are provided to retired employees, the cost of the additional benefits should be accounted for in accordance with paragraph (iii) given above.

4. Disclosures : The financial statements should disclose the method by which retirement benefit costs for the period have been determined . In case the costs related to gratuity and other defined benefit schemes are based on an actuarial valuation, the financial statements should also disclose whether the actuarial valuation was made at the end of the period or at an earlier date. In the latter case, the date of the actuarial valuation should be specified and the method by which the accrual for the period has been determined should also be briefly described, if the same is not based on the report of the actuary.

1.6 Accounting Standard - 17 (AS - 17)

Segment Reporting

(In this Accounting Standard, the standard portions have been set in **bold italic** type. These should be read in the context of the background material which has been set in normal type, and in the context of the 'Preface to the Statements of Accounting Standards'.[1])

The following is the text of Accounting Standard 17, 'Segment Reporting', issued by the Council of the Institute of Chartered Accountants of India. This Standard comes into effect in respect of accounting periods commencing on or after 1.4.2001 and is mandatory in nature,[2] from that date, in respect of the following :

(i) Enterprises whose equity or debt securities are listed on a recognised stock exchange in India, and enterprises that are in the process of issuing equity or debt securities that will be listed on a recognised stock exchange in India as evidenced by the board of directors' resolution in this regard.

(ii) All other commercial, industrial and business reporting enterprises, whose turnover for the accounting period exceeds Rs. 50 crores.

Objective

The objective of this Statement 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. Such information helps users of financial statements :

1. Attention is specifically drawn to paragraph 4.3 of the Preface, according to which accounting standards are intended to apply only to material items.
2. This implies that, while discharging their attest function, it will be the duty of the members of the Institute to examine whether this Accounting Standard is complied with in the presentation of financial statements covered by their audit. In the event of any deviation from this Accounting Standard, it will be their duty to make adequate disclosures in their audit reports so that the users of financial statements may be aware of such deviations.

(a) better understand the performance of the enterprise;
(b) better assess the risks and returns of the enterprise; and
(c) make more informed judgements about the enterprise as a whole.

Many enterprises provide groups of products and services or operate in geographical areas that are subject to differing rates of profitability, opportunities for growth, future prospects, and risks. Information about different types of products and services of an enterprise and its operations in different geographical areas — often called segment information — is relevant to assessing the risks and returns of a diversified or multi-locatipnal enterprise but may not be determinable from the aggregated data. Therefore, reporting of segment information is widely regarded as necessary for meeting the needs of users of financial statements.

Scope

1. This Statement should be applied in presenting general purpose financial statements.
2. The requirements of this Statement are also applicable in case of consolidated financial statements.[1]
3. An enterprise should comply with the requirements of this Statement fully and not selectively.
4. If a single financial report contains both consolidated financial statements and the separate financial statements of the parent company, segment information need be presented only on the basis of the consolidated financial statements. In the context of reporting of segment information in consolidated financial statements, the references in this Statement to any financial statement items should be construed to be the relevant item as appearing in the consolidated financial statements.

Definitions

5. The following terms are used in this Statement with the meanings specified :

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

1. A separate accounting standard on 'Consolidated Financial Statements', which is being formulated, will specify the requirements relating to consolidated financial statements.

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 Statement.

Enterprise revenue is revenue from sales to external customers as reported in the statement of profit and loss.

Segment revenue is the aggregate of

(i) the portion of enterprise revenue that is directly attributable to a segment,

(ii) the relevant portion of entrprise revenue that can be allocated on a reasonable basis to a segment, and

(iii) revenue from transactions with other segments of the enterprise.

Segment revenue does not include

(a) extraordinary items as defined in AS 5, Net Profit or Loss for the Period, Prior Period Items and Changes in Accounting Policies;

(b) interest or dividend income, including interest earned on advances or loans to other segments unless the operations of the segment are primarily of a financial nature; and

(c) gains on sales of investments or on extinguishment of debt unless the operations of the segment are primarily of a financial nature.

Segment expense is the aggregate of

(i) the expense resulting from the operating activities of a segment that is directly attributable to the segment, and

(ii) the relevant portion of enterprise expense that can be allocated on a reasonable basis to the segment, including expense relating to transactions with other segments of the enterprise.

Segment expense does not include

(a) extraordinary items as defined in AS 5, Net Profit or Loss for the Period, Prior Period Items and Changes in Accounting Policies;

(b) interest expense, including interest incurred on advances or loans from other segments, unless the operations of the segment are primarily of a financial nature;

(c) losses on sales of investments or losses on extinguishment of debt unless the operations of the segment are primarily of a financial nature;
(d) income tax expense; and
(e) general administrative expenses, head-office expenses, and other expenses that arise at the enterprise level and relate to the enterprise as a whole. However, costs are sometimes incurred at the enterprise level on behalf of a segment. Such costs are part of segment expense if they relate to the operating activities of the segment and if they can be directly attributed or allocated to the segment on a reasonable basis.

Segment result is segment revenue less segment expense

Segment assets are those operating assets that are employed by a segment in its operating activities and that either are directly attributable to the segment or can be allocated to the segment on a reasonable basis.

If the segment result of a segment includes interest or dividend income, its segment assets include the related receivable, loans, investments, or other interest or dividend generating assets.

Segment assets do not include income tax assets

Segment assets are determined after deducting related allowances/provisions that are reported as direct offsets in the balance sheet of the enterprise.

Segment liabilities are those operating liabilities that result from the operating activities of a segment and that either are directly attributable to the segment or can be allocated to the segment on a reasonable basis.

If the segment result of a segment includes interest expense, its segment liabilities include the related interest-bearing liabilities.

Segment liabilities do not include income tax liabilities.

1.7 Accounting Standard - 18 (A S - 18)

Related Party Disclosures

(In this Accounting Standard, the standard portions have been set in **bold italic** type. These should be read in the context of the background material which has been set in normal type, and in the context of the 'Preface to the Statements of Accounting Standards'.)[1]

The following is the text of Accounting Standard (AS) 18, 'Related Party Disclosures', issued by the Council of the Institute of Chartered Accountants of India. This Standard comes into effect in respect of accounting periods commencing on or after 1-4-2001 and is mandatory in nature.[2]

1. Attention is specifically drawn to paragraph 4.3 .of the Preface, according to which accounting standards are intended to apply only to material items.
2. This implies that, while discharging their attest function, it will be the duty of the members of the Institute to examine whether this Accounting Standard is complied with in the presentation of financial statements covered by their audit. In the event of any deviation from this Accounting Standard, it will be their duty to make adequate disclosures in their audit reports so that the users of financial statements may be aware of such deviations.

Objective

The objective of this Statement is to establish requirements for disclosure of:

(a) related party relationships; and

(b) transactions between a reporting enterprise and its related parties.

Definitions

10. For the purpose of this Statement, the following terms are used with the meanings specified :

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.

Control -

(a) ownership, directly or indirectly, 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, or

(c) a substantial interest in voting power and the power to direct, by statute or agreement, the financial and/or operating policies of the enterprise.

Significant influence — participation in the financial and or operating policy decisions of an enterprise, but not control of those policies.

An Associate — an enterprise in which an investing reporting party has significant influence and which is neither a subsidiary not a joint venture of that party.

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

Joint control — the contractually agreed sharing of power to govern the financial and operating policies of an economic activity so as to obtain benefits from it.

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.

Holding company — a company having one or more subsidiaries.

Subsidiary — a company :

(a) in which another company (the holding company) holds, either by itself and/or through one or more subsidiaries, more than one-half in nominal value of its equity share capital; or

(b) of which another company (the holding company) controls, either by itself and/or through one or more subsidiaries, the composition of its board of directors.

Fellow subsidiary — a company is considered to be a fellow subsidiary of another company if both are subsidiaries of the same holding company.

State-controlled enterprise — an enterprise which is under the control of the Central Government and/or any State Govemment(s).

11. For the purpose of this Statement, an enterprise is considered to control the composition of

(i) the board of directors of a company, if it has the power, without the consent or concurrence of any other person, to appoint or remove all or a majority of directors of that company. An enterprise is deemed to have the power to appoint a director if any of the following conditions is satisfied:
   (a) a person cannot be appointed as director without the exercise in his favour by that enterprise of such a power as aforesaid; or
   (b) a person's appointment as director follows necessarily from his appointment to a position held by him in that enterprise; or
   (c) the director is nominated by that enterprise; in case that enterprise is a company, the director is nominated by that company/subsidiary thereof.

(ii) the governing body of an enterprise that is not a company, if it has the power, without the consent or the concurrence of any other person, to appoint or remove all or a majority of members of the governing body of that other enterprise. An enterprise is deemed to have the power to appoint a member if any of the following conditions is satisfied :
   (a) a person cannot be appointed as memberof the governing body without the exercise in his favour by that other enterprise of such a power as aforesaid; or
   (b) a person's appointment as member of the governing body follows necessarily from his appointment to a position held by him in that other enterprise; or
   (c) the member of the governing body is nominated by that other enterprise.

12. An enterprise is considered to have a substantial interest in another enterprise if that enterprise owns, directly or indirectly, 20 percent or more interest in the voting power of the other enterprise. Similarly, an individual is considered to have a substantial interest in an enterprise, if that individual owns, directly or indirectly, 20 percent or more interest in the voting power of the enterprise.

13. Significant influence may be exercised in several ways, for example, by representation on the board of directors, participation in the policy making process, material inter-company

transactions, interchange of managerial personnel, or dependence on technical information. Significant influence may be gained by share ownership, statute or agreement. As regards share ownership, if an investing party holds, directly or indirectly through intermediaries, 20 percent or more of the voting power of the enterprise, it is presumed that the investing party does have significant influence, unless it can be clearly demonstrated that this is not the case. Conversely, if the investing party holds, directly or indirectly through intermediaries, less than 20 percent of the voting power of the enterprise, it is presumed that the investing party does not have significant influence, unless such influence can be clearly demonstrated. A substantial or majority ownership by another investing party does not necessarily preclude an investing party from having significant influence.

Summary : Disclosure

1. The statutes governing an enterprise often require disclosure in financial statements of transactions with certain categories of related parties. In particular, attention is focussed on transactions with the directors or similar key management personnel of an enterprise, especially their remuneration and borrowings, because of the fiduciary nature of their relationship with the enterprise.

2. 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.

3. Where the reporting enterprise controls, or is controlled by, another party, this information is relevant to the users of financial statements irrespective of whether or not transactions have taken place with that party. This is because the existence of control relationship may prevent the reporting enterprise from being independent in making its financial and/or operating decisions. The disclosure of the name of the related party and the nature of the related party relationship where control exists may sometimes be at least as relevant in appraising an enterprise's prospects as are the operating results and the financial position presented in its financial statements. Such a related party may establish the enterprise's credit standing, determine the source and price of its raw materials, and determine to whom and at what price the product is sold.

4. If there have been transactions between related parties, during the existence of a related party relationship, the reporting enterprise should disclose the following :

(i) the name of the transacting related party;
(ii) a description of the relationship between the parties;
(iii) a description of the nature of transactions;
(iv) volume of the transactions either as an amount or as an appropriate proportion;
(v) any other elements of the related party transactions necessary for an understanding of the financial statements;
(vi) 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

(vii) amounts written-off or written-back in the period in respect of debts due from or to related parties.

5. The following are examples of the related party transactions in respect of which disclosures may be made by a reporting enterprise :

- purchases or sales of goods (finished or unfinished); .
- purchases or sales of fixed assets;
- rendering or receiving of services;
- agency arrangements;
- leasing or hire-purchase arrangement;
- transfer of research and development;
- licence agreements;
- finance (including loans and equity contributions in cash or in kind);
- guarantees and collaterals; and
- management contracts including for deputation of employees.

6. Paragraph 23(v) requires disclosure of any other elements of the related party transactions necessary for an understanding of the financial statements'. An example of such a disclosure would be an indication that the transfer of a major asset had taken place at an amount materially different from that obtainable on normal commercial terms.

7. Items of a similar nature may be disclosed in aggregate by type of related party.

1.8 Accounting Standard - 19 (AS - 19)

Leases

(In this Accounting Standard, the standard portions have been set in bold italic type. These should be read in the context of the background material which has been set in normal type, and in the context of the 'Preface to the Statements of Accounting Standards'.[1])

The following is the text of Accounting Standard (AS) 19, 'Leases', issued by the Council of the Institute of Chartered Accountants of India. This Standard comes into effect in respect of all assets leased during accounting periods commencing on or after 1.4.2001 and is mandatory in nature[2] from that date. Accordingly, the 'Guidance note on Accounting for Leases' issued by the Institute in 1995, is not applicable in respect of such assets. Earlier application of this Standard is, however, encouraged.

1. Attention is specifically drawn to paragraph 4.3 of the Preface, according to which accounting standards are intended to apply only to material items.
2. This implies that, while discharging their attest function, it will be the duty of the members of the Institute to examine whether this Accounting Standard is complied with in the presentation of financial statements covered by their audit. In the event of any deviation from this Accounting Standard, it will be their duty to make adequate disclosures in their audit reports so that the users of financial statements may be aware of such deviations.

Objective

The objective of this Statement is to prescribe, for lessees and lessors, the appropriate accounting policies and disclosures in relation to finance leases and operating leases.

Definitions

The following terms are used in this Statement with the meanings specified :

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 :

  (i) by or on behalf of the lessee; or

  (ii) by an independent third party financially capable of meeting this guarantee.

However, if the lessee has an option to purchase the asset at a price which is expected to be sufficiently lower than the fair value at the date the option becomes exercisable that, at the inception of the lease, is reasonably certain to be exercised, the minimum lease payments comprise minimum payments payable over the lease term and the payment required to exercise this purchase option.

Fair value is the amount for which an asset could be exchanged or a liability settled between knowledgeable, willing parties in an arm's length transaction.

Economic life is either :

(a) the period over which an asset is expected to be economically usable by one or more users; or

(b) the number of production or similar units expected to be obtained from the asset by one or more users.

Useful life of a leased asset is either :

(a) the period over which the leased asset is expected to be used by the lessee; or

(b) the number of production or similar units expected to be obtained from the use of the asset by the lessee.

Residual value of a leased asset is the estimated fair value of the asset at the end of the lease term.

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 guarantee by or on behalf of the lessee, or by an independent third party who is financially capable of discharging the obligations under the guarantee.

Unguaranteed residual value of a leased asset is the amount by which the residual value of the asset exceeds its guaranteed residual value.

Gross investment in the lease is the aggregate of the minimum lease payments under a finance lease from the standpoint of the lessor and any unguaranteed residual value accruing to the lessor.

Unearned finance income is the difference between :

(a) the gross investment in the lease; and

(b) the present value of

  (i) the minimum lease payments under a finance lease from the standpoint of the lessor; and

  (ii) any unguaranteed.residual value accruing to the lessor, at the interest rate implicit in the lease.

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, market rates of interest).

The definition of a lease includes agreements for the hire of an asset which contain a provision giving the hirer an option to acquire title to the asset upon the fulfillment of agreed conditions. These agreements are commonly known as hire-purchase agreements. Hire-purchase agreements include agreements under which the property in the asset is to pass to the hirer on the payment of the last instalment and the hirer has a right to terminate the agreement at any time before the property so passes.

Classification of Leases

The classification of leases adopted in this Statement is based on the extent to which risks and rewards incident to ownership of a leased asset lie with the lessor or the lessee. Risks include the possibilities of losses from idle capacity or technological obsolescence and of variations in return due to changing economic conditions. Rewards may be represented by the expectation of profitable operation over the economic life of the asset and of gain from appreciation in value or realisation of residual value.

A lease is classified as a finance lease if it transfers substantially all the risks and rewards incident to ownership. Title may or may not eventually be transferred. A lease is classified as an operating lease if it does not transfer substantially all the risks and rewards incident to ownership.

Since the transaction between a lessor and a lessee is based on a lease agreement common to both parties, it is appropriate to use consistent definitions. The application of these definitions to the differing circumstances of the two parties may sometimes result in the same lease being classified differently by the lessor and the lessee.

Whether a lease is a finance lease or an operating lease depends on the substance of the transaction rather than its form. Examples of situations which would normally lead to a lease being classified as a finance lease are :

(a) the lease transfers ownership of the asset to the lessee by the end of the lease term;
(b) the lessee has the option to purchase the asset at a price which is expected to be sufficiently lower than the fair value at the date the option becomes exercisable such that, at the inception of the lease, it is reasonably certain that the option will be exercised;
(c) the lease term is for the major part of the economic life of the a'sset even if title is not transferred;
(d) at the inception of the lease the present value of the minimum lease payments amounts to at least substantially all of the fair value of the leased asset; and

(e) the leased asset is of a specialised nature such that only the lessee can use it without major modifications being made.

Indicators of situations which individually or in combination could also lead to.a lease being classified as a finance lease are :

(a) if the lessee can cancel the lease, the lessor's losses associated with the cancellation are borne by the lessee;
(b) gains or losses from the fluctuation in the fair value of the residual fall to the lessee (for example in the form of a rent rebate equalling most of the sales proceeds' at the end of the lease); and
(c) the lessee can continue the lease for a secondary period at a rent which Is substantially lower than market rent.

Lease classification is made at the inception of the lease. If at any time the lessee and the lessor agree to change the provisions of the lease, other than by renewing the lease, in a manner that would have resulted in a different classification of the lease under the criteria in paragraphs 5 to 9 had the changed terms been in effect at the inception of the lease, the revised agreement is considered as a new agreement over its revised term. Changes in estimates (for example, changes in estimates of the economic life or of the residual value of the leased asset) or changes in circumstances (for example, default by the lessee), however, do not give rise to a new classification of a Jease for accounting purposes.

Disclosures for finance leases

(a) assets acquired under finance lease as segregated from the assets owned;
(b) for each class of assets, the net carrying amount at the balance sheet date;
(c) a reconciliation between the total of minimum lease payments at the balance sheet date and their present value. In addition, an enterprise should disclose the total of minimum lease payments at the balance sheet date, and their present value, 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;
(d) contingent rents recognised as expense in the statement of profit and loss for the period;
(e) the total of future minimum sublease payments expected to be received under non-cancellable subleases at the balance sheet date; and
(f) 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.

Disclosures for operating leases

(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;
(c) lease payments recognised in the statement of profit and loss for the period, with separate amounts for minimum lease payments and contingent rents;
(d) sub-lease payments received (or receivable) recognised in the statement of profit and loss for the period;
(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.

Sale and Leaseback Transactions

A sale and leaseback transaction involves the sale of an asset by the vendor and the leasing of the same asset back to the vendor. The lease payments and the sale price are usually interdependent as they are negotiated as a package. The accounting treatment of a sale and leaseback transaction depends upon the type of lease involved.

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 recognised as income or loss in the financial statements of a seller-lessee. Instead, it should be deferred and amortised over the lease term in proportion to the depreciation of the leased asset.

If the leaseback is a finance lease, it is not appropriate to regard an excess of sales proceeds over the carrying amount as income. Such excess is deferred and amortised over the lease term in proportion to the depreciation of the leased asset. Similarly, it is not appropriate to regard a deficiency as loss. Such deficiency is deferred and amortised over the lease term.

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 recognised immediately. If the sale price is below fair value, any profit or loss should be recognised immediately except that, if the loss is compensated by future lease payments at below market price, it should be deferred and amortised 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 amortised over the period for which the asset is expected to be used.

If the leaseback is an operating lease, and the lease payments and the sale-price are established at fair value, there has in effect been a normal sale transaction and any profit or loss is recognised immediately.

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 recognised immediately.

For finance leases, no such adjustment is necessary unless there has been an impairment in value, in which case the carrying amount is .reduced to recoverable amount in accordance with the Accounting Standard dealing with impairment of assets.

Disclosure requirements for lessees and lessors apply equally to sale and leaseback transactions. The required description of the significant leasing arrangements leads to disclosure of unique or unusual provisions of the agreement or terms of the sale and leaseback transactions.

Sale and leaseback transactions may meet the separate disclosure criteria set out in paragraph 12 of Accounting Standard (AS) 5, Net Profit or Loss for the Period, Prior Period Items and Changes in Accounting Policies.

1.9 Accounting Standard - 20 (AS - 20)

Earnings per Share

(In this Accounting Standard, the standard portions have been set in bold italic type. These should be read in the context of the background material which has been set in normal type, and in the context of the 'Preface to the Statements of Accounting Standards'.[1])

Accounting Standard (AS) 20, 'Earnings Per Share', issued by the Council of the Institute of Chartered Accountants of India, comes into effect in respect of accounting periods commencing on or after 1.4.2001 and is mandatory in nature[2] , from that date, in respect of enterprises whose equity shares or potential equity shares are listed on a recognised stock exchange in India. An enterprise which has neither equity shares not potential equity shares which are so listed but which discloses earnings per share, should calculate and disclose earnings per share in accordance with this Standard from the aforesaid date. The following is the text of the Accounting Standard.

Objective

The objective of this Statement-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

1. Attention is specifically drawn to paragraph 4.3 of the Preface, according to which accounting standards are intended to apply only to material items.
2. This implies that, while discharging their attest'function, it will be the duty of the members of the Institute to examine whether this Accounting Standard is complied with in the presentation of financial statements covered by their audit. In the event of any deviation from this Accounting Standard, it will be their duty to make adequate disclosures in their audit reports so that the users of financial statements may be aware of such deviations.

enterprise. The focus of this Statement is on the denominator of the earnings per share calculation. Even though earnings per share data has limitations because of different accounting policies used for determining 'earnings', a consistently determined denominator enhances the quality of financial reporting.

Definitions

For the purpose of this Statement, the following terms are used with the meanings specified : 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 financial instrument is any contract that gives rise to both a financial asset of one enterprise and a financial liability or equity shares of another enterprise.

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

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

Fair value is the amount for which an asset could be exchanged, or a liability settled, between knowledgeable, willing parties in an arm's length transaction.

Presentation

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.

This Statement requires an enterprise to present basic and diluted earnings per share, even if the amounts disclosed are negative (a loss per share).

Measurement : Basic Earnings Per Share

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.

Earnings - Basic

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.

All items of income and expense which are recognised in a period, including tax expense and extraordinary items, are included in the determination of the net profit or loss for the period unless an Accounting Standard requires or permits otherwise (see Accounting Standard (AS) 5, Net Profit or Loss for the Period, Prior Period Items and Changes in Accounting Policies). The amount of preference dividends and any attributable tax thereto for the period is deducted from the net profit for the period (or added to the net loss for the period) in order to calculate

the net profit or loss for the period attributable to equity shareholders.

The amount of preference dividends for the period that is deducted from the net profit for the period is:

(a) the amount of any preference dividends on non-cumulative preference shares provided for in respect of the period; and

(b) the full amount of the required preference dividends for cumulative preference shares for the period, whether or not the dividends have been provided for. The amount of preference dividends for the period does not include the amount of any preference dividends for cumulative preference shares paid or declared during the current period in respect of previous periods.

If an enterprise has more than one class of equity shares, net profit or loss for the period is apportioned over the different classes of shares in accordance with their dividend rights.

Per Share - Basic

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 reflects the fact that the amount of shareholders' capital may have varied during the period as a result of a larger or lesser number of shares outstanding at any time. It is the number of equity shares outstanding at the beginning of the period, adjusted by the number of equity shares bought back or issued during the period multiplied by the time-weighting factor. The time-weighting factor is the number of days for which the specific shares are outstanding as a proportion of the total number of days in the period; a reasonable approximation of the weighted average is adequate in many circumstances.

Diluted Earnings Per Share

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 dilative potential equity shares.

In calculating diluted earnings per share, effect is given to all dilutive potential equity shares that were outstanding during the period, that is :

(a) the net profit for the period attributable to equity shares is :

  (i) increased by the amount of dividends recognised in the period in respect of the dilutive potential equity shares as adjusted for any attributable change in tax expense for the period;

  (ii) increased by the amount of interest recognised in.the period in respect of the dilutive potential equity shares as adjusted for any attributable change in tax expense for the period; and

  (iii) adjusted for the after-tax amount of any other changes in expenses or income that would result from the conversion of the dilutive potential equity shares.

(b) the weighted average number of equity shares outstanding during the period is increased by the weighted average number of additional equity shares which would have been outstanding assuming the conversion of all dilutive potential equity shares.

For the purpose of this Statement, share application money pending allotment or any advance share application money as at the balance sheet date, which is not statutorily required to be kept separately and is being utilised in the business of the enterprise, is treated in the same manner as dilutive potential equity shares for the purpose of calculation of diluted earnings per share.

Dilutive Potential Equity Shares

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.

An enterprise uses net profit from continuing ordinary activities as "the control figure" that is used to establish whether potential equity shares are dilutive or anti-dilutive. The net profit from continuing ordinary activities is the net profit from ordinary activities (as defined in AS 5) after deducting preference dividends and any attributable tax thereto and after excluding items relating to discontinued operations.[1]

Potential equity shares are anti-dilutive when their conversion to equity shares would increase earnings per share from continuing ordinary activities or decrease loss per share from continuing ordinary activities. The effects of anti-dilutive potential equity shares are ignored in calculating diluted earnings per share.

In considering whether potential equity shares are dilutive or antidilutive, each issue or series of potential equity shares is considered separately rather than in aggregate. The sequence in which potential equity shares are considered may affect whether or not they are dilutive. Therefore, in order to maximise the dilution of basic earnings per share, each issue or series of potential equity shares is considered in sequence from the most dilutive to the lest dilutive. For the purpose of determining the sequence from most dilutive to least dilutive potential equity shares, the earnings per incremental share is the least, the potential equity share is considered most dilutive and vice-versa.

Disclosure

In addition to disclosures as required by paragraphs 8, 9 and 44 of this Statement, an enterprise should disclose the following :

(a) the amounts used as the numerators in calculating basic and diluted earnings per share, and a reconciliation of those amounts to the net profit or loss for the period;

(b) the weighted average number of equity shares used as the denominator in calculating basic and diluted earnings per share, and a reconciliation of these denominators to each other; and

(c) the nominal value of shares along with the earnings per share figures.

1. A separate accounting standard on 'Discontinuing Operations', which is being formulated, will specify the requirements in respect of discontinued operations.

Contracts generating potential equity shares may incorporate terms and conditions which, affect the measurement of basic and diluted earnings per share. These terms and conditions may determine whether or not any potential equity shares are dilutive and, if so, the effect on the weighted average number of shares outstanding and any consequent adjustments to the net profit attributable to equity shareholders. Disclosure of the terms and conditions of such contracts is encouraged by this Statement.

If an enterprise discloses, in addition to basic and diluted earnings per share, per share amounts using a reported component of net profit other than net profit or loss for the period attributable to equity shareholders, such amounts should be calculated using the weighted average number of equity shares determined in accordance with this Statement. If a component of net profit is used which is not reported as a line item in the statement of profit and loss, a reconciliation should be provided between the component used and a line item which is reported in the statement of profit and loss. Basic and diluted per share amounts should be disclosed with equal prominence.

An enterprise may wish to disclose more information than -this Statement requires. Such information may help the users to evaluate the performance of the enterprise and may take the form of per share amounts for various components of net profit, e.g., profit from ordinary activities. Such disclosures are encouraged. However, when such amounts are disclosed, the denominators need to be calculated in accordance with this Statement in order to ensure the comparability of the per share amounts disclosed.

1.10 Accounting Standard - 21 (AS - 21)

Consolidated Financial Statements

(In this Accounting Standard, the standard portions have been set in bold italic type. These should be read in the context of the background material which has been set in normal type, and in the context of the 'Preface to the Statements of Accounting Standards'.[2])

Accounting Standard (AS) 21, 'Consolidated Financial Statements', issued by the Council of the Institute of Chartered Accountants of India, comes into effect in respect of accounting periods commencing on or after 1.4.2001.

An enterprise that presents consolidated financial statements should prepare and present these statements in accordance with this Standard. The following is the text of the Accounting Standard.

Objective

The objective of this Statement is to lay down principles and procedures for preparation and presentation of consolidated financial statements. Consolidated financial statements are presented by a parent (also known as holding enterprise) to provide financial information about the economic activities of its group. These statements are intended to present financial

2. Attention is specifically drawn to paragraph 4.3 of the Preface, according to which accounting standards are intended to apply only to material items.

information about a parent and its subsidiary(ies) as a single economic entity to show the economic resources controlled by the group, the obligations of the group and results the group achieves with its resources.

Definitions

For the purpose of this Statement, the following terms are used with the meanings specified Control :

(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.

Consolidated financial statements normally include consolidated balance sheet, consolidated statement of profit and loss, and notes, other statements and explanatory material that form an integral part thereof. Consolidated cash flow statement is presented in case a parent presents its own cash flow statement. The consolidated financial statements are presented, to the extent possible, in the same format as that adopted by the parent for its separate financial statements.

Presentation of Consolidated. Financial Statements :

A parent which presents consolidated financial statements should present these statements in addition to its separate financial statements.

Users of the financial statements of a parent are usually concerned with, and need to be informed about, the financial position and results of operations of not only the enterprise itself but also of the group as a whole. This need is served by providing the users -

(a) separate financial statements of the parent; and

(b) consolidated financial statements, which present financial information about the group as that of a single enterprise without regard to the legal boundaries of the separate legal entitles.

Consolidation Procedures

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, the following steps should be taken :

(a) the cost to the parent of its investment in each subsidiary and the parent's portion of equity of each subsidiary, at the date on which investment in each subsidiary is made, should be eliminated;

(b) any excess of the cost to the parent of its investment in a subsidiary over the parent's portion of equity of the subsidiary, at the date on which investment in the subsidiary is made, should be described as goodwill to be recognised as an asset in the consolidated financial statements;

(c) when the cost to the parent of its investment in a subsidiary is less than the parent's portion of equity of the subsidiary, at the date on which investment in the subsidiary is made, the difference should be treated as a capital reserve in the consolidated financial statements;

(d) minority interests in the net income of consolidated subsidiaries for the reporting period should be identified and adjusted against the income of the group in order to arrive at the net income attributable to the owners of the parent; and

(e) minority interests in the net assets of consolidated subsidiaries should be identified and presented in the consolidated balance sheet separately from liabilities and the equity of the parent's shareholders. Minority interests in the net assets consist of:
   (i) the amount of equity attributable to minorities at the date on which investment in a subsidiary is made and
   (ii) the minorities' share of movements in equity since the date the parent-subsidiary relationship came in existence.

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.

The parent's portion of equity in a subsidiary, at the date on which investment is made, is determined on the basis of information contained in the financial statements of the subsidiary as on the date of investment. However, if the financial statements of a subsidiary, as on the date of investment, are not available and if it is impracticable to draw the financial statements of the subsidiary as on that date, financial statements of the subsidiary for the immediately preceding period are used as a basis for consolidation. Adjustments are made tp these financial statements for the effects of significant transactions or other events that occur between the date of such financial statements and the date of investment in the subsidiary.

If an enterprise makes two or more investments in another enterprise at different dates and eventually obtains control of the other enterprise, the consolidated financial statements are presented only from the date on which holding-subsidiary relationship comes in existence. If

two or more investments are made over a period of time, the equity of the subsidiary at the date of investment, for the purposes of paragraph 13 above, is generally determined on a step.-by-step basis; however, if small investments are made over a period of time and then an investment is made that results in control, the date of the latest investment, as a practicable measure, may be considered as the date of investment.

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.

Intragroup balances and intragroup transactions, including sales, expenses and dividends, are eliminated in full. Unrealised profits resulting from intragroup transactions that are included in the carrying amount of assets, such as inventory and fixed assets, are eliminated in full. Unrealised losses resulting from intragroup transactions that are deducted in arriving at the carrying amount of assets are also eliminated unless cost cannot be recovered.

The financial statements used in the consolidation should be drawn up to the same reporting date, fit is not practicable to draw up the financial statements of one or more subsidiaries to such date and, accordingly, those financial statements are drawn up to different reporting dates, adjustments should be made for the effects of significant transactions or other events that occur between those dates and the date of the parent's financial statements. In any case, the difference between reporting dates should not be more than six months.

The financial statements of the parent and its subsidiaries used in the preparation of the consolidated financial statements are usually drawn up to the same date. When the reporting dates are different, the subsidiary often prepares, for consolidation purposes, statements as at the same date as that of the parent. When it is impracticable to do this, financial statements drawn up to different reporting dates may be used provided the difference in reporting dates is not more than six months. The consistency principle requires that the length of the reporting periods and any difference in the reporting dates should be the same from period to period.

Consolidated financial statements should be prepared using uniform accounting policies for like transactions and other events in similar circumstances. If it is not practicable to use uniform accounting policies in preparing the consolidated financial statements, that fact should be disclosed together with the proportions of the items in the consolidated financial statements to which the different accounting policies have been applied.

If a member of the group uses accounting policies other than those adopted in the consolidated financial statements for like transactions and events in similar circumstances, appropriate adjustments are made to its financial statements when they are used in preparing the consolidated financial statements.

The results of operations of subsidiary are included in the consolidated financial statements as from the date on which parent-subsidiary relationship came in existence. The results of operations of a subsidiary with which parent-subsidiary relationship ceases to exist are included in the consolidated statement of profit and loss until the date of cessation of the relationship. The difference between the proceeds from the disposal of investment in a subsidiary and the carrying amount of its assets less liabilities as of the date of disposal is recognised in

the consolidated statement of profit and loss as the profit or loss on the disposal of the' investment in the subsidiary. In order to ensure the comparability of the financial satements from one accounting period to the next, supplementary information is often provided about the effect of the acquisition and disposal of subsidiaries on the financial position at the reporting date and the results for the reporting period and on the corresponding amounts for the preceding period.

An investment in an enterprise should be accounted for in accordance with Accounting Standard (AS) 13, Accounting for Investments, from the date, that the enterprise ceases to be a subsidiary and does not become an associate .

The carrying amount of the investment at the date that it ceases to be a subsidiary is regarded as cost thereafter.

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.

The losses applicable to the minority in a consolidated subsidiary may exceed the minority interest in the equity of the subsidiary. The excess, and any further losses applicable to the minority, are adjusted against the majority interest except to the extent that the minority has a binding obligation to, and is able to, make good the losses. If the subsidiary subsequently reports profits, all such profits are allocated to the majority interest until the minority's share of losses previously absorbed by the majority has been recovered.

If a subsidiary has outstanding cumulative preference shares which are held outside the group, the parent computes its share of profits or losses after adjusting for the subsidiary's preference dividends, whether or not dividends have been declared.

Accounting for Investments in Subsidiaries in a Parent's Separate Financial Statements

In a parent's separate financial statements, investments in subsidiaries should be accounted for in accordance with Accounting Standard (AS) 13, Accounting for Investments.

Disclosure

In addition to disclosures required by paragraphs 11 and 20, following disclosures should be made :

(a) in consolidated financial statements a list of all subsidiaries including the name, country of incorporation or residence, proportion of ownership interest and, if different, proportion of voting power held:

(b) in consolidated financial statements, where applicable :

  (i) the nature of the relationship between the parent and a subsidiary, if the parent does not own, directly or indirectly through subsidiaries, more than one-half of the voting power of the subsidiary;

  (ii) the effect of the acquisition and disposal of subsidiaries on the-financial position at the reporting date, the results for the reporting period and on the corresponding amounts for the preceding period; and

  (iii) the names of the subsidiary(ies) of which exporting date(s) is/are different from that of the parent and the difference in reporting dates.

Transactional Provisions

On the first occasion that consolidated financial statements are presented, comparative figures for the previous period need not be presented. In all subsequent years full comparative figures for the previous period should be presented in the consolidated financial statements.

1.11 (AS - 22) (issued 2001) - Accounting for Taxes on Income :

Accounting Standard (AS) 22, 'Accounting for Taxes on Income', issued by the Council of the Institute of Chartered Accountants of India, comes into effect in respect of accounting periods commencing on or after 1-4-2001. It is mandatory in nature for:

(a) All the accounting periods commencing on or after 01.04.2001, in respect of the following:
   i) Enterprises whose equity or debt securities are listed on a recognised stock exchange in India and enterprises that are in the process of issuing equity or debt securities that will be listed on a recognised stock exchange in India as evidenced by the board of directors' resolution in this regard.
   ii) All the enterprises of a group, if the parent presents consolidated financial statements and the Accounting Standard is mandatory in nature in respect of any of the enterprises of that group in terms of (i) above.

(b) All the accounting periods commencing on or after 01.04.2002, in respect of companies not covered by (a) above.

(c) All the accounting periods commencing on or after 01.04.2003, in respect of all other enterprises.

The Guidance Note on Accounting for Taxes on Income, issued by the Institute of Chartered Accountants of India in 1991, stands withdrawn from 1.4.2001. The following is the text of the Accounting Standard.

Objective

The objective of this Statement is to prescribe accounting treatment for taxes on income. Taxes on income is one of the significant items in the statement of profit and loss of an enterprise. 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. This divergence between taxable income and accounting income arises due to two main reasons. Firstly, there are differences between items of revenue and expenses as appearing in the statement of profit and loss and the items which are considered as revenue, expenses or deductions for tax purposes. Secondly, there are differences between the amount in respect of a particular item of revenue or expense as recognised in the statement of profit and loss and the corresponding amount which is recognised for the computation of taxable income.

Scope

1. This Statement should be applied in accounting for taxes on income. This includes the determination of the amount of the expense or saving.related to taxes on income in respect of an accounting period tyd the disclosure of such an amount in the financial statements.
2. For the purposes of this Statement, taxes on income include all domestic and foreign taxes which are based on taxable income.
3. This Statement does not specify when, or how, an enterprise should'account for taxes that are payable on distribution of dividends and other distributions made by the enterprise.

Definitions

4. For the purpose of this Statement, the following terms are used with the meanings specified: 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 (he statement of profit and toss 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 defferences 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.
5. Taxable income is calculated in accordance with tax laws. In some circumstances, the requirements of these laws to compute taxable income differ from the accounting policies applied to determine accounting income. The effect of this difference is that the taxable income and accounting income may not be the same.
6. The differences between taxable income and accounting income can be classified into permanent differences and timing differences. Permanent differences are those differences between taxable income and accounting income which originate in one period and do not reverse subsequently. For instance, if for the purpose of computing taxable income, the tax laws allow only a part of an item of expenditure, the disallowed amount would result in a permanent difference.
7. Timing differences are those 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. Timing differences arise because the period in which some items of revenue and expenses are included in taxable income do not coincide with the period in which such items of revenue and expenses are included or considered in arriving at accounting income. For example, machinery purchased for scientific research related to business is fully allowed as deduction in the first year for tax purposes whereas the same would be charged to the statement of profit and loss as depreciation over its useful life. The total depreciation charged on the machinery for accounting purposes and the amount allowed as deduction for tax purposes will ultimately be the same, but periods over which the depreciation is charged and the deduction is allowed will differ. Another example of timing difference is a situation where, for the purpose of computing taxable income, tax laws allow depreciation on the basis of the written down value method, whereas for accounting purposes, straight line method is used. Some other examples of timing differences arising under the Indian tax laws are given in Appendix 1.

8. Unabsorbed depreciation and carry forward of losses which can be set-off against future taxable income are also considered as timing differences and result in deferred tax assets, subject to consideration of prudence (see paragraphs 15-18)

Recognition

9. 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.
10. Taxes on income are considered to be an expense incurred by the enterprise in earning income and are accrued in the same period as the revenue and expenses to which they relate. Such matching may result into timing differences. The tax effects of timing differences are included in the tax expense in the statement of profit and loss and as deferred tax assets (subject to the consideration of prudence as set out in paragraphs 15-18) or as deferred tax liabilities, in the balance sheet.
11. An example of tax effect of a timing difference that results in a deferred tax asset is an expense provided in the statement of profit and loss but not allowed as a deduction under Section 43B of the Income-tax Act, 1961. This timing difference will reverse when the deduction of that expense is allowed under Section 43B in subsequent year(s). An example of tax effect of a timing difference resulting in a deferred tax liability is the higher charge of depreciation allowable under the Income-tax Act, 1961, compared to the depreciation provided in the statement of profit and loss. In subsequent years, the differential will reverse when comparatively lower depreciation will be allowed for tax purposes.
12. Permanent differences do not result in deferred tax assets or deferred tax liabilities.
13. Deferred tax should be recognised for all the timing differences, subject to the consideration of prudence in respectof deferred tax assets as set out in paragraphs 15-18.

14. This Statement requires recognition of deferred tax for all the timing differences. This is based on the principle that the financial statements for a period should recognise the tax effect, whether current or deferred, of all the transactions occurring in that period.
15. Except in the situations stated in paragraph 17, deferred tax assets should be recognised 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 realised.
16. While recognising the tax effect of timing differences, consideration of prudence cannot be ignored. Therefore, deferred tax assets are recognised and carried forward only to the extent that there is a reasonable certainty of their realisation. This reasonable level of certainty would normally be achieved by examining the past record of the enterprise and by making realistic estimates of profits for the future.
17. Where an enterprise has unabsorbed depreciation orcarry forward of losses under tax laws, deferred tax assets should be recognised only to the extent that there is virtual certainty supported by convincing evidence that sufficient future taxable income wiUbe available against which such deferred tax assets can be realised.
18. Theexistence of unabsorbed depreciation or carry forward of losses under tax laws is strong evidence, that future taxable income may not be available. Therefore, when an enterprise has a history of recent losses, the enterprise recognises deferred tax assets only to the extent that it has timing differences the reversal of which will result in sufficient income or there is other convincing evidence that sufficient taxable income will be available against which such deferred tax assets can be realised. In such circumstances, the nature of the evidence supporting its recognition is disclosed.

Re-assessment of Unrecognised Deferred Tax Assets

19. At each balance sheet date, an enterprise re-assesses unrecognised deferred tax assets. The enterprise recognises previously unrecognised deferred tax assets to the extent that it has become reasonably certain or virtually certain, as the case may be, that sufficient future taxable income will be available against which such deferred tax assets can be realised. For example, an improvement in trading conditions may make it reasonably certain that the enterprise will be able to generate sufficient taxable income in the future.

Measurement

20. 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.
21. 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.
22. Deferred tax assets and liabilities are usually measured using the tax rates and tax laws that have been enacted. However, certain announcements of tax rates and tax

laws by the government may have the substantive effect of actual enactment. In these circumstances, deferred tax assets and liabilities are measured using such announced tax rate and tax laws.

23. When different tax rates apply to different levels of taxable income, deferred tax assets and liabilities are measured using average rates.
24. Deferred tax assets and liabilities should not be discounted to their present value.
25. The reliable determination of deferred tax assets and liabilities on a discounted basis requires detailed scheduling of the timing of the reversal of each timing difference. In a number of cases such scheduling is impracticable or highly complex. Therefore, it is inappropriate to require discounting of deferred tax assets and liabilities. To permit, but not to require, discounting would result in deferred tax assets and liabilities which would not be comparable between enterprises. Therefore, this statement does not require or permit the discounting of deferred tax assets and liabilities.

Review of Deferred Tax Assets

26. 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 or virtually certain, as the case may be (see paragraphs 15 to 18), that sufficient future taxable income wittbe available against which deferred tax asset can be realised. Any such write-down may be reversed to the extent that it becomes reasonably certain or virtually certain, as the case may be, that sufficient future taxable income win be available.

Presentation and Disclosure

27. An enterprise should offset assets and liabilities representing current tax if the enterprise:
    (a) has a legally enforceable right to set off the recognised amounts; and
    (b) intends to settle the asset and the liability on a net basis.
28. An enterprise will normally have a legally enforceable right to set off an asset and liability representing current tax when they relate to income taxes levied under the same governing taxation laws and the taxation laws permit the enterprise to make or receive a single net payment.
29. An enterprise should offset deferred tax assets and deferred tax liabilities if :
    (a) the enterprise has a legally enforceable right to set off assets against liabilities representing currentax and
    (b) the deferred tax assets and the deferred tax liabilities relate to taxes on income levied by the same governing taxation laws.
30. 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.

31. 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.
32. 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.

Transitional Provisions

33. On the first occasion that the taxes on income are accounted for in accordance with this Statement, the enterprise should recognise, in the financial statements, the deferred tax balance that has accumulated prior to the adoption of this Statement as deferred tax asset/liability with a corresponding credit/charge to the revenue reserves, subject to the consideration of prudence in case of deferred tax assets (see paragraphs 15-18). The amount so credited/charged to the revenue reserves should be the same as that which would have resulted if this Statement had been in effect from the beginning.
34. For the purpose of determining accumulated deferred tax in the period in which this Statement is applied for the first time, the opening balances of assets and liabilities for accounting purposes and for tax purposes are compared and the differences, if any, are determined. The tax effects of these differences, if any, should be recognised as deferred tax assets or liabilities, if these differences are timing differences. For example, in the year in which an enterprise adopts this Statement, the opening balance of a fixed asset is Rs. 100 for accounting purposes and Rs. 60 for tax purposes. The difference is because the enterprise applies written down value method of depreciation for calmlatine taxable income whereas for accounting purposes straight line method is used. This difference will reverse in future when depreciation for tax purposes will be lower as compared to the depreciation for accounting purposes. In the above case, assuming that enacted tax rate for the year is 40% and that there are no other timing differences, deferred tax liability of Rs. 16 [(Rs. 100 - Rs. 60) x 40%] would be recognised. Another example is an expenditure that has already been written off for accounting purposes in the year of its incurrance but is allowable for tax purposes over a period of time. In this case, the asset representing that expenditure would have a balance only for tax purposes but not for accounting purposes. The difference between balance of the asset for tax purposes and the balance (which is nil) for accounting purposes would be a timing difference which will reverse in future when this expenditure would be allowed for tax purposes. Therefore, a deferred tax asset would be recognised in respect of this difference subject to the consideration of prudence (see paragraphs 15-18).

4.12 Accounting Standard (AS - 23) (issued in 2001)— Accounting for Investments in Associates in Consolidated Financial Statements :

(In this Accounting Standard, the standard portions have been set in bold italic type. These should be read in the context of the background material which has been set in normal type, and in the context of the 'Preface to the Statements of Accounting Standards'.1)

Accounting Standard (AS) 23, 'Accounting for Investments in Associates in Consolidated Financial Statements', issued by the Council of the Institute of Chartered Accountants of India, comes into effect in respect of accounting peridds commencing on or after 1 -4-2002. An enterprise that presents consolidated financial statements should account for investments in associates in the consolidated financial statements in accordance with this Standard.2 The following is the text of the Accounting Standard.

Objective

The objective of this Statement 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.

Scope

1. This Statement should be applied in accounting for investments in associates in the preparation and presentation of consolidated financial statements by an investor.
2. This Statement does not deal with accounting for investments in associates in the preparation and presentation of separate financial statements by an investor.3

Definitions

3. For the purpose of this Statement, the following terms are used with the meanings specified:
   An associate is an enterprise in which the investor has significant influence and which is neither a subsidiary nor a joint venture4 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.

Control :

(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.

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.

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

4. For the purpose of this Statement, significant influence does not extend to power to govern the financial and/or operating policies of an enterprise. Significant influence may be gained by share ownership, statute or agreement. As regards share ownership, if an investor holds, directly or indirectly through subsidiary(ies), 20% or more of the voting power of the investee, it is presumed that the investor has significant influence, unless it can be clearly demonstrated that this is not the case. Conversely, if the investor holds, directly or indirectly through subsidiary(ies), less than 20% of the voting power of the investee, it is presumed that the investor does not have significant influence, unless such influence can be clearly demonstrated.6 A substantial or majority ownership by another investor does not necessarily preclude an investor from having significant influence.
5. The existence of significant influence by an investor is usually evidenced in one or more of the following ways:
   (a) Representation on the board of directors or corresponding governing body of the investee;
   (b) participation in policy making processes;
   (c) material transactions between the investor and the investee;
   (d) interchange of managerial personnel; or
   (e) provision of essential technical information.
6. Under the equity method, the investment is initially recorded at cost, identifying any goodwill/capital reserve arising at the time of acquisition and the carrying amount is increased or decreased to recognise the investor's share of the profits or losses of the investee after the date of acquisition. Distributions received from an investee reduce the carrying amount of the investment. Adjustments to the carrying amount may also be necessary for alterations in the investor's proportionate interest in the investee arising from changes in the investee's equity that have not been included in the statement of profit and loss. Such changes include those arising from the revaluation of fixed assets and investments, from foreign exchange translation differences and from the adjustment of differences arising on amalgamations.

Accounting for Investments - Equity Method

7. An investment in an associate should be accounted for in consolidated financial statements under the equity method except when;
   (a) the investment is acquired and held exclusively with a view to Us subsequent disposal in the nearfuture; or

(b) the associate operates under severe long-term restrictions that significantly impair its ability to transfer funds to the investor. investments in such associates should be accounted for in accordance with Accounting Standard (AS) 13, Accounting for Investments. The reasons for not-applying the equity method in accounting for investments in an associate should be disclosed in the consolidated financial statements.

8. Recognition of income on the basis of distributions received may not be an adequate measure of the income earned by an investor on an investment in an associate because the distributions received may bear little relationship to the performance of the associate. As the investor has significant influence over the associate, the investor has a measure of responsibility for the associate's performance and, as a result, the return on its investment. The investor accounts for this stewardship by extending the scope of its consolidated financial statements to include its share of results of such an associate and so provides an analysis of earnings' and investment from which more useful ratios can be calculated. As a result, application of the equity method in consolidated financial statements provides more informative reporting of the net assets and net income of the investor.
9. An investor should discontinue the use of the equity method from the date that:
   (a) It ceases to have significant influence in an associate but retains-, either in whole or in part, its investment; or
   (b) the use of the equity method is no longer appropriate because the associateoperates under severe long-term restrictions that significantly impair its ability to transfer funds to the investor.

   From the date of discontinuing the use of the equity method, investments in such associates should be accounted for in accordance with Accounting Standard (AS) 13, Accounting for Investments. For this purpose, the carrying amount of the investment at that date should be regarded as cost thereafter.

Application of the Equity Method

10. Many of the procedures appropriate for the application of the equity method are similar to the consolidation procedures set out in Accounting Standard (AS) 21, Consolidated Financial Statements. Furthermore, the broad concepts underlying the consolidation procedures used in the acquisition of a subsidiary are adopted on the acquisition of an investment in an associate.
11. An investment in an associate is accounted for under the equity method from the date on-which it falls within the definition of an associate. On acquisition of the investment any difference between the cost of acquisition and the investor's share of the equity of the associate is described as goodwill or capital reserve, as the case may be.
12. 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.

13. In using equity method for accounting for investment in an associate, unrealised profits and losses resulting from transactions between the investor (or its consolidated subsidiaries) 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.
14. The most recent available financial statements of the associate are used by the investor in applying the equity, method; they are usually drawn up to the same date as the financial statements of the investor. When the reporting dates of the investor and the associate are different, the associate often prepares, for the use of the investor, statements as at the same date as the financial, statements of the investor. When it is impracticable to do this, financial statements drawn up to a different reporting date may be used. The consistency principle requires that the length of the reporting periods, and any difference in the reporting dates, are consistent from period to period.
15. When financial statements with a different reporting date are used, adjustments are made for the effects of any significant events or transactions between the investor (or its consolidated subsidiaries) and the associate that occur between the date of the associate's financial statements and the date of the investor's consolidated financial statements.
16. The investor usually prepares consolidated financial statements using uniform accounting policies for the like transactions and events in similar circumstances. In case an associate uses accounting policies other than those adopted for the consolidated financial statements for like transactions and events in similar circumstances, appropriate adjustments are made to the associate's financial statements when they are used by the investor in applying the equity method. If it is not practicable to do so, that fact is disclosed along with a brief description of the differences between the accounting policies.
17. If an associate has outstanding cumulative preference shares held outside the group, the investor computes its share of profits or losses after adjusting for the preference dividends whether or not the dividends have been declared.
18. If, under the equity method, an investor's share of losses of an associate equals or exceeds the carrying amount of the investment, the investor ordinarily discontinues recognising its share of further losses and the investment is reported at nil value. Additional losses are provided for to the extent that the investor has incurred obligations or made payments on behalf of the associate to satisfy obligations of the associate that the investor has guaranteed or to which the investor is otherwise committed. If the associate subsequently reports profits, the investor resumes including its share of those profits only after its share of the profits equals the share of net losses that have not been recognised.

19. Where an associate presents consolidated financial statements, the results and net assets to be taken into account are those reported in that associate's consolidated financial statements.
20. 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.

Contingencies

21. In accordance with Accounting Standard (AS) 4, Contingencies and Events Occurring After the Balance Sheet, Date, the investor discloses in the consolidated financial statements:
    (a) its share of the contingencies and capital commitments of an associate for which it is also contingently liable; and
    (b) those contingencies that arise because the investor is severally liable for the liabilities of the associate.

Disclosure

22. In addition to the-disclosures required by paragraph 7 and 12, 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.
23. 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.
24. The name(s) of the associate(s) of which reporting date(s) is/are different from that of the financial statements of an investor and the differences in reporting dates should be disclosed in the consolidated financial statements.
25. In case an associate uses accounting policies other than those adopted for the consolidated financial statements for like transactions and events in similar circumstances and it is not practicable to make appropriate adjustments to the associate's financial statements, the fact should be disclosed along with a brief description of the differences in the accounting policies.

Transitional Provisions

26. On the first occasion when investment in an associate is accounted for in consolidated financial statements in accordance with this Statement, the carrying amount of investment in the associate should be brought to the amount that would have resulted had the equity method of accounting been followed as per this Statement since the acquisition of the associate. The corresponding adjustment in this regard should be made in the retained earnings in the consolidated financial statements.

1.13 Accounting Standard (AS - 24) (issued 2002) - Discontinuing Operations :

(In this Accounting Standard, the standard portion have been set in bold italic type. These should be read in the context of the background material which has been set in normal type, and in the context of the 'Preface to the Statements of Accounting Standards'.[1])

Accounting Standard (AS) 24, 'Discontinuing Operations', issued by the Council of the Institute of Chartered Accountants of India, is recommendatory in nature2 at present. The following is the text of the Accounting Standard.

Objective

The objective of this Statement is to establish principles for reporting information about discontinuing operations, thereby enhancing the ability of users of financial statements to make projections of an enterprise's cash flows, earnings-generating capacity, and financial position by segregating information about discontinuing operations from information about continuing operations.

Scope

1. This Statement applies to all discontinuing operations of an enterprise.
2. The requirements related to cash flow statement contained in this Statement are applicable where an enterprise prepares and presents a cash flow statement.

Definitions

Discontinuing Operation

3. 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 tine of business or geographical area of operations; and
   (c) that can be distinguished operationally' and for financial reporting purposes.
4. Under criterion (a) of the definition (paragraph 3 (a)), a discontinuing operation may be disposed of in its entirety or piecemeal, but always pursuant to an overall plan to discontinue the entire component.
5. If an enterprise sells a component substantially in its entirety, the result can be a net gain or net loss. For such a discontinuance, a binding sale agreement is entered into on a specific date, although the actual transfer of possession and control of the discontinuing operation may occur at a later date. Also, payments to the seller may