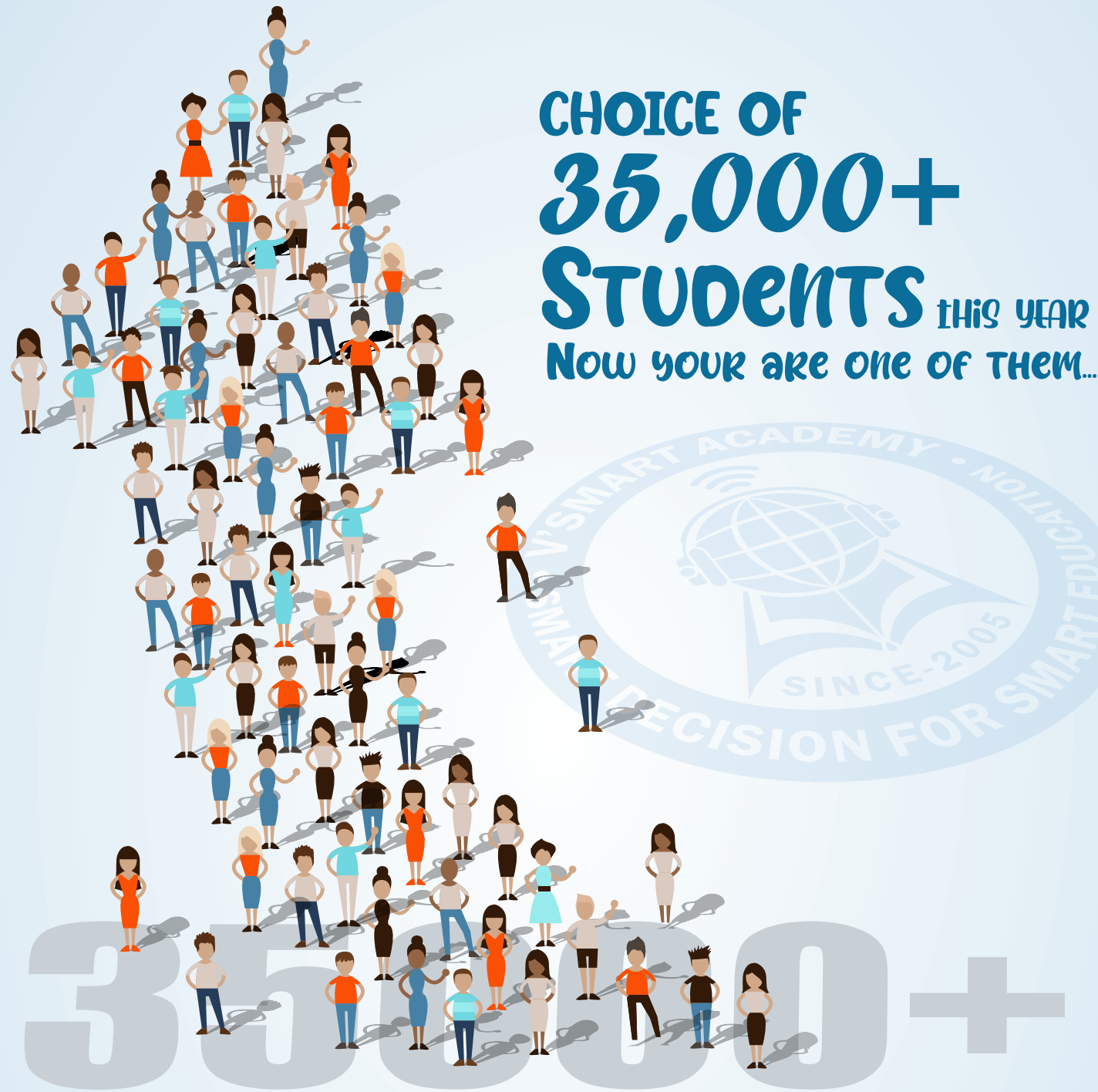


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HOW TO ASK STUDY RELATED DOUBTS ?

1. You can WhatsApp your Query/Doubt along with the image of Question and Solution if any. (7887 7887 05)
2. Normally Me & My Team will try to reply within a day or two but pls have some patience for 3-4 days, after that u can call us on the same number to remind if u haven't got any reply.
3. Doubts will be entertained only on WhatsApp or Dedicated Telegram Groups of the batch if any.

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ROADMAP OF IND AS

"The Past can-not be changed.

The Future is yet in your power"

APPLICABILITY OF IND AS (INDIAN ACCOUNTING STANDARDS)

APPLICABILITY OF IND AS FOR COMPANIES (OTHER THAN BANKS, NBFCs, INSURANCE COMPANIES)

Phase-I: Obligation to Comply with Ind AS from 1st April, 2016

In accordance with clause (ii) of sub- rule (1) of Rule 4 of the Companies (Indian Accounting Standards) Rules, 2015, the following companies shall comply with Ind AS w.e.f. April 2016:

- (a) Companies listed/in process of listing (Except companies listed on SME Exchanges) on Stock Exchanges in India or Outside India having net worth of ₹500 crore or more;
- (b) Unlisted Companies having net worth \geq ₹500crore;
- (c) Holding (Parent), subsidiary, joint venture or associate companies of above.

COMPLIANCE	CURRENT FY	COMPARATIVE PERIOD	TRANSITION DATE FOR OPENING IND AS BS
Voluntary Compliance (Optional)	FY 15-16 i.e. year ending 31 st March 2016	FY 14-15 i.e. year ending 31 st March 2015	01/04/2014
Mandatory Compliance	FY 16-17 i.e. year ending 31 st March 2017	FY 15-16 i.e. year ending 31 st March 2016	01/04/2015

Phase-II: Mandatory Compliance of Ind AS from 1st April, 2017

Clause (iii) of sub- rule (1) of Rule 4 of the Companies (Indian Accounting Standards) Rules, 2015 states that the following companies shall comply with Ind AS for the accounting periods beginning on or after 1st April, 2017:

- (a) Companies listed/in process of listing (Except companies listed on SME Exchanges) on Stock Exchanges in India or Outside India having net worth of less than Rs. 500crore;
- (b) Unlisted companies having net worth of \geq Rs.250 crore but $<$ Rs.500crore;
- (c) Holding, Subsidiary, Associate and J.V. of Above.



COMPLIANCE	IND AS CURRENT FY	IND AS COMPARATIVE PERIOD	TRANSITION DATE FOR OPENING INDAS BS
Voluntary Compliance (Optional)	FY 16-17 i.e. year ending 31 st March 2017	FY 15-16 i.e. year ending 31 st March 2016	01/04/2015
Mandatory Compliance	FY 17-18 i.e. year ending 31 st March 2018	FY 16-17 i.e. year ending 31 st March 2017	01/04/2016

NET WORTH OF COMPANIES FOR THE PURPOSE OF IND AS

The term Net Worth shall have the meaning assigned to it in clause (57) of Section 2 of the Companies Act, 2013. For the purposes of calculation of net worth of companies, the following principles shall apply, namely:-

(a) The net worth shall be calculated in accordance with:

- i) the stand-alone financial statements of the company as on **31st March, 2014**; or
- ii) the first audited financial statements for accounting period which ends after 31st March, 2014;

(b) for companies which are not in existence on 31st March, 2014 or an existing company falling under any of thresholds specified in sub-rule (1) for the first time after 31st March, 2014, the net worth shall be calculated on the basis of the first audited financial statements ending after that date in respect of which it meets the thresholds specified in sub-rule(1).

Net Worth = Total Paid-up Share Capital + Free Reserves (Excluding Revaluation Res.) + Sec. Prem A/c - Accumulated Losses - Deferred Expenditures & Misc Exp. (excluding written back of depreciation)

Note - ESOP reserve and Capital Reserve made out of Govt. Grants shall be part of Net Worth for the purpose of calculating IndAS applicability.

Note:

- Ind As once required to be complied with in accordance with Companies (Indian Accounting Standards) Rules, 2015, shall **apply to both standalone financial statements and consolidated financial statements**.
- For companies which are not in existence on 31st March, 2014 or an existing company falling under any of thresholds specified for the first time after 31st March, 2014, the net worth shall be calculated on the basis of the first audited financial statements ending after that date in respect of which it meets the thresholds specified.
- **Overseas subsidiary, associate, joint venture and other similar entities** of an Indian company may prepare its standalone financial statements in accordance with the requirements of the specific



jurisdiction, provided that such Indian company shall prepare its consolidated financial statements in accordance with Ind AS either voluntarily or mandatorily if it meets the criteria.

- Indian company which is a subsidiary, associate, joint venture and other similar entities of a foreign company shall prepare its financial statements in accordance with the Ind AS either voluntarily or mandatorily if it meets the criteria. (based on Net Worth of Individual Financial Statements of Subsidiary).
- Listing Status shall be checked only in First Year of INDAS Financial Statements. (refer case 7)
- Subsidiary/Associates/JV status shall be checked only in First Year of INDAS Financial Statements. (refer case 2)

IND AS FOR BANK, INSURANCE COMPANIES AND NBFCs

S.No.	Entities	For Accounting Period Beg. Frm 1 st April 2018 onwards	For Accounting Period Beg. Frm 1 st April 2019 Onwards
1	All India Term lending refinancing Institutions (EXIM, NABARD, SIDBI)	Mandatory	-
2	Non-Banking Financial Institutions (NBFCs)	<p style="text-align: center;">Having Net Worth of Rs. 500 Cr. or More</p> <p style="text-align: center;">Holding, Subsidiary, JV or Associates of the above</p>	<p style="text-align: center;">NBFCs whose equity/debt instruments are listed or in process of listing and having Net Worth Less than Rs. 500 Cr.</p> <p style="text-align: center;">Unlisted NBFCs, Having Net worth of Rs. 250 Cr. or more but less than Rs. 500 Cr.</p> <p style="text-align: center;">Holding, Subsidiary, JV or Associates of the Above</p>

Parent NBFC and Subsidiary is Non-Finance Company or vice versa:

- A) Case 1** - Parent NBFC prepares Consolidated Financial Statements as per AS and its Subsidiary/Associate/JV (Non-Finance Company) is preparing INDAS Financial Statements. Now such non finance company (Subs/Ass/JV) has to prepare one additional financial statement as per AS for the purpose of Preparation of Consolidated Financial Statements by its Parent NBFC.
- B) Case 2** - Parent Non-Finance Company is preparing INDAS Financial Statements wef 1/04/2016 and it has a Subsidiary/Associate/JV who is NBFC preparing Financial Statements (FY 16-17) as per AS. Since Parent has to prepare Consolidated Financial Statements as per INDAS, therefore such NBFC Subsidiary/Ass/JV has to prepare

INDAS Financial Statements for its Parent company for the purpose of Consolidation. It implies that the NBFC subsidiary, associate or a joint venture, in such case shall continue to prepare the financials under AS until IndAS are applicable to it. (Refer Case 8 below)		
3	Insurance Companies	Insurance Companies will apply Ind AS after Finalisation of IFRS 17
4	BANKS (Excluding RRBs)	Implementation of Ind AS is deferred till further Notice by RBI vide Notification dated 22/03/19
5	Mutual Fund Companies	Applicable wef 1/04/2023 as per SEBI's notification dated 25 th Jan 2022 with specific Format.

Notes:

1. Voluntary adoption is not permitted for BANKS/NBFCs/INSURERS
2. Entities not covered in the roadmap shall continue to apply Accounting Standards at present. Such as RRBs, Banks, Insurance Companies, Unlisted entities having NW less than 250 Cr., Entities listed on SME Exchanges.

IMPORTANT CASES:**Case - 1**

Company X, on standalone basis, had a net worth of above Rs. 250 crore but below Rs. 500 crore in financial year 2013-14 as well as financial year 2014-15 and is expected to exceed Rs. 500 crore in financial year 2015-16.

Whether the Company X be required to comply with Ind AS from financial year 2017-18 i.e. under Phase II, given that the net worth as on 31st March 2014 was below Rs. 500 Crore and the Company X was a company existing as on 31st March 2014 and was already falling under the threshold as on 31st March 2014 itself irrespective of the fact that the net-worth as on 31st March 2016 might be above Rs. 500crore.

(Answer: IND AS will be applicable from the financial year beginning from 1st April, 2016 - Phase I, However if expectation doesn't meet then Phase II)

Case - 2**(ITFG Clarification Bulletin 1, Issue 2)**

Company A is a listed company and has three Subsidiaries Company X, Company Y and Company Z. As on 31st March 2014, the net worth of Company A is Rs 600 Crores, net worth of Company X is Rs 100 Crores, Company Y is Rs 400 Crores and Company Z is Rs 210 Crores. All the three subsidiaries are non-listed public companies.

Sub - Case A During the financial year 2014-15, Company A has sold off its entire investment in Company X on 31st December 2014. Therefore, Company X is no longer a subsidiary of Company A for the purposes of preparation of financial statements as on 31 March 2015. Should Company X prepare its financial statements as per the Companies (Accounting Standards) Rules, 2006 or the Companies (Indian Accounting Standards) Rules, 2015?



Sub - Case B During the financial year 2015-16, Company A has sold off its investment in Company Y on 31st December, 2015. Therefore, Company Y is no longer a subsidiary of Company A for the purposes of preparation of financial statements as on 31 March 2016. Should Company Y prepare its financial statements as per the Companies (Accounting Standards) Rules, 2006 or the Companies (Indian Accounting Standards) Rules, 2015?

Sub - Case C During the financial year 2016-17, Company A has sold off its investment in Company Z on 31st December 2016, therefore company Z is no longer a subsidiary of Company A for the purposes of preparation of financial statements as on 31 March 2017. Should Company Z prepare its financial statements as per the Companies (Accounting Standards) Rules, 2006 or the Companies (Indian Accounting Standards) Rules, 2015?

(Answer: CASE A & B - NO Ind AS BS of Subsidiaries X & Y; CASE C - Subsidiary Z has to prepare its FS as per Ind AS)

Case - 3

(ITFG Clarification Bulletin 2, Issue 2)

Company X Ltd. and Company Y Ltd. registered in India having net worth of Rs 600 crores and 100 crores respectively are subsidiaries of a Foreign Company viz., ABC Inc., which has net worth of more than Rs. 500 crores in financial year 2015-16. Whether Company X Ltd. and Y Ltd. are required to comply with Ind AS from financial year 2016-17 on the basis of net worth of the parent Foreign Company or on the basis of their own net worth?

(Answer: Foreign Company - Not required to Comply with Ind AS. Company X - will follow Ind AS & Company Y will not follow Ind AS, but foreign company's net worth would not be the basis for deciding the applicability)

Case - 4

(ITFG Clarification Bulletin 12, Issue 6)

ABC & Co. incorporated in US with limited liability, has established a branch office in India, with the permission of the RBI, to provide consultancy service in India. The branch office remits the amounts earned by it to ABC & Co. (i.e. Head office) net of applicable Indian taxes and subject to RBI guidelines.

AS on April 1, 2016, it has more than 500 crore balance as "Head Office account".

Whether the India branch office of ABC Co. will be required to comply with IndAS?

(Answer: Branch office of a foreign co. is not covered under rule 6 since branch is not incorporated under the Co. Act. Therefore, branch office of ABC & Co. is not required to comply with Ind AS.)

Case - 5

(ITFG Clarification Bulletin 11, Issue 7)

A Ltd. is a first time adopter of IndAS. It has incorporated a partnership firm with B Ltd. namely, M/s A&B Associates. Whether IndAS will be applicable to M/s A&B Associates by virtue of the fact that Ind AS is applicable to A Ltd.?

(Answer: Ind AS is not applicable to Partnership entity as it is not Incorporated under the Act.)



However, partnership firm will be required to provide financial statements for the purpose of Consolidation.)

Case - 6

(ITFG Clarification Bulletin 6, Issue 2)

Company X Ltd. is being covered under Phase I of Ind AS and needs to apply Ind AS from financial year 2016-17. Company Y which is an associate company of Company X Ltd. is a charitable organization and registered under section 8 of the Companies Act, 2013.

Whether company Y is required to comply with Ind AS from financial year 2016-17?

(Answer: Section 8 companies are incorporated under Co. Act, 2013 and are required to comply with the provisions of Co. Act, 2013, therefore Co. Y will be required to apply Ind AS from the financial year 2016-17)

Case - 7

(ITFG Clarification Bulletin 3, Issue 8)

As on March 31, 2014, Company A is a listed company and has a net worth of 50 Crore. As on March 31, 2015, the company is no more a listed company. Whether Company A is required to comply with Ind AS from the FY 2017-18.

(Answer: Before the mandatory applicable date (i.e. 17-18) company A ceases to be a listed company. Accordingly, it will not be required to apply Ind AS from FY 17- 18)

Case - 8

As per the roadmap, Ind AS is applicable to Company X from the financial year 2017-18. Company X (non-finance company) is a subsidiary of Company Y (NBFC). Company Y is an unlisted NBFC company having net worth of ₹ 400 crores. What will be the date of applicability of Ind AS for company X and company Y? If Ind AS applicability date for parent NBFC is different from the applicability date of corporate subsidiary, then, how will the consolidated financial statements of parent NBFC be prepared?

Answer:

In accordance with the roadmap, it may be noted that NBFCs having net worth of less than 500 crore shall apply Ind AS from 1 April, 2019 onwards. Further, the holding, subsidiary, joint venture or associate company of such an NBFC other than those covered by corporate roadmap shall also apply Ind AS from 1 April, 2019.

Accordingly, in the given case, Company Y (NBFC) shall apply Ind AS for the financial year beginning 1 April, 2019 with comparative for the period ended 31 March, 2019 . Company X shall apply Ind AS in its statutory individual financial statements from the financial year 2017-2018 (as per the corporate roadmap). However, for the purpose of Consolidation by Company Y for financial years 2017-2018 and 2018-2019, Company X shall also prepare its individual financial statements as per AS.



02

SCHEDULE III TO THE COMPANIES ACT, 2023

"Sometimes Later becomes Never"

DIVISION II

Financial Statements for a company whose financial statements are drawn up in compliance of the Companies (Indian Accounting Standards) Rules, 2015.

Dear Students,

In this topic, I have included important points of Schedule III relevant for Examination purpose. For full annexure u can refer ICAI Module.

Name of the Company.....

Balance Sheet as at.....

(Rupees in)

	Particulars	Note No.	Figures as at the end of current reporting period	Figures as at the end of the previous reporting period
	1	2	3	4
(1)	ASSETS			
	Non-current assets			
(a)	Property, Plant and Equipment		INDAS 16	
(b)	Capital work-in-progress		INDAS 16	
(c)	Investment Property		INDAS 40	
(d)	Goodwill		INDAS 103,110,111	
(e)	Other Intangible assets		INDAS 38	
(f)	Intangible assets under development		INDAS 38	
(g)	Biological Assets other than bearer plants		INDAS 41	
(h)	Financial Assets		INDAS 32/109	
	(i) Investments			
	(ii) Trade receivables			
	(iii) Loans			
	(iv) Others, to be specified			
(I)	Deferred tax assets (net)		INDAS 12	
(J)	Other Non-current assets			

(2)	Current assets	
(a)	Inventories	INDAS 2
(b)	Financial Assets	INDAS 32/109
	(i) Investments	
	(ii) Trade receivables	
	(iii) Cash and cash equivalents	
	(iv) Bank balances other than (iii) above	
	(v) Loans	
	(vi) Others (to be specified)	
(c)	Current Tax Assets (Net)	INDAS 12
(d)	Other current assets	
	Total Assets	
	EQUITY AND LIABILITIES	
	Equity	
(a)	Equity Share capital	INDAS 32
(b)	Other Equity	INDAS 32
	LIABILITIES	
	Non-current liabilities	
(a)	Financial Liabilities	
	(ia) Lease Liabilities	INDAS 116
	(i) Borrowings	INDAS 32/109
	(ii) Trade Payables:	INDAS 32/109
	(A) Total outstanding dues of micro enterprises and small enterprises; and	
	(B) Total outstanding dues of creditors other than micro enterprises and small enterprises.	
	(iii) Other financial liabilities (other than those specified in item (b), to be specified)	
(b)	Provisions	INDAS 37
(c)	Deferred tax liabilities (Net)	INDAS 12
(d)	Other non-current liabilities	
	Current liabilities	
(a)	Financial Liabilities	
	(i) Lease Liabilities	INDAS 116
	(ii) Borrowings	INDAS 32/109
	(iii) Trade Payables:	INDAS 32/109
	(A) Total outstanding dues of micro enterprises and small enterprises; and	
	(B) Total outstanding dues of creditors other than micro enterprises and small enterprises.	
	(iv) Other financial liabilities (other than those specified in item (c))	
(b)	Other Current Liabilities	
(c)	Provisions	INDAS 37
(d)	Current Tax Liabilities (Net)	INDAS 12
	Total Equity and Liabilities	

STATEMENT OF CHANGES IN EQUITY

Name of the Company.....

Statement of Changes in Equity for the period ended

A. Equity Share Capital

1. Current Reporting Period

Balance at the beginning of the reporting period	Changes in equity share capital due to prior period errors	Restated Balance at the beginning of the current reporting period	Changes in equity share capital during the current year	Balance at the end of the current reporting period

2. Previous Reporting Period

Balance at the beginning of the previous reporting period	Changes in equity share capital due to prior period errors	Restated Balance at the beginning of the previous reporting period	Changes in equity share capital during the previous year	Balance at the end of the previous reporting period

B. Other Equity
1) Current Reporting Period

	Share Application Money Pending Allotment	Equity Component of Comp. Fin. Instrument	Reserve & Surplus (CR, SP, R/E & Others separately)			Debt Instrument thru OCI	Equity Instrument thru OCI	Cash Flow Hedge Reserve	Revaluation Surplus	Exchange Diff.	Other Items of OCI	Money Received against Share Capital
			Capital Reserve	Securities Premium	Other Reserves (Specify Nature)							
Balance at the beginning of the current reporting period		INDAS 109 & 32	Capital Reserve	Securities Premium	Other Reserves (Specify Nature)	INDAS 109 & 32	INDAS 109 & 32	INDAS 16	INDAS 21	INDAS 19		
Changes in accounting policies or prior period errors												
Restated Balance at the beginning of the current reporting period												
Total Comprehensive income for the current year												
Dividends												
Transfer to retained earnings												
Any other change (to be specified)												
Balance at the end of the current reporting period												

2) Previous Reporting Period

	Share Application Money Pending Allotment	Equity Component of Comp. Fin. Instrument	Reserve & Surplus (CR, SP, R/E & Others separately)			Debt Instrument thru OCI	Equity Instrument thru OCI	Cash Flow Hedge Reserve	Revaluation Surplus	Exchange Diff.	Other Items of OCI	Money Received against Share Capital
			Capital Reserve	Securities Premium	Other Reserves (Specify Nature)							
Balance at the beginning of the current reporting period		INDAS 109 & 32	Capital Reserve	Securities Premium	Other Reserves (Specify Nature)	INDAS 109 & 32	INDAS 109 & 32	INDAS 16	INDAS 21	INDAS 19		
Changes in accounting policies or prior period errors												
Restated Balance at the beginning of the current reporting period												
Total Comprehensive income for the current year												
Dividends												
Transfer to retained earnings												
Any other change (to be specified)												
Balance at the end of the current reporting period												

GENERAL INSTRUCTIONS FOR PREPARATION OF BALANCE SHEET

1. ITEMS OF NON-CURRENT ASSETS

Investments	Trade Receivables	Loans	Other Non-Current Assets
<p>Investments shall be classified as Equity, Pref, Govt or trust securities, Debn, or Bonds MF, Other Investments.</p> <p>Also, details regarding Investments in Subsidiaries, Associates, JV or structured entities shall also be given from above classification.</p> <p>Disclose quoted investments & their market values separately from unquoted investments and aggregate amount of impairment in these values</p>	<p>Sub classified into -</p> <ul style="list-style-type: none"> ● Secured ● Unsecured ● Significant increase in credit Risk ● Credit Impaired <p>Provision for bad & doubtful debts shall be separately disclosed under the relevant head.</p> <p>Debts due by directors/officers of entity shall be separately disclosed.</p> <p>Ageing schedule of Disputed and undisputed TR for the mentioned periods must be given.</p>	<p>Classify loans into-</p> <ul style="list-style-type: none"> ● Security Deposits ● Loans to related Parties ● Others <p>Sub classified into -</p> <ul style="list-style-type: none"> ● Secured ● Unsecured ● Significant increase in credit Risk ● Credit Impaired <p>Provision for bad & doubtful debts shall be separately disclosed under the relevant head.</p> <p>Loans due by directors/officers of entity shall be separately disclosed.</p>	<p>Classified into-</p> <ul style="list-style-type: none"> ● Capital Advances ● Other than Capital Advances <p>Others (specify) Other than Capital Advances is sub classified as -</p> <ul style="list-style-type: none"> ● Security deposits ● Advances to related parties ● Other advances Advances to directors/ officers/ their private companies to be disclosed separately under 'Other Financial Assets'

2. Other Financial Assets

- (i) Security Deposits
- (ii) Bank deposits with more than 12 months maturity
- (iii) Others (to be specified)

3. Items of Current Assets

Inventories	Investments	Trade Receivables	Cash & Cash Equivalents	Loans
Classified into-	Investments	Sub classified	Classified	Classify loans
<ul style="list-style-type: none"> Raw Materials WIP Finished Goods Stock in Trade (acquired for trading) Stores & Spares Loose tools Others <p>GIT shall be disclosed under sub-heads separately</p> <p>Mode of valuation shall be disclosed</p>	<p>shall be classified as Equity, Pref, Govt or trust securities., Debn or MF partnerships & Others.</p> <p>Also, details regarding Investments in Subsidiaries, Associates, JV shall also be given from above classification.</p> <p>Disclose quoted investments & their market values separately from unquoted investments</p> <p>Aggregate amount of impairments in value of investments are also to be disclosed.</p>	<p>into -</p> <ul style="list-style-type: none"> Good & Secured Good but Unsecured TR with Significant increase in credit Risk Credit Impaired <p>Provision for bad & doubtful debts shall be separately disclosed under the relevant head.</p> <p>Debts due by directors/officers of entity shall be separately disclosed.</p> <p>Ageing schedule of Disputed and undisputed TR for the mentioned periods must be given.</p>	<p>into-</p> <ul style="list-style-type: none"> Balance with Banks Cheques/Drafts on hand Cash on Hand Others such as FDs lower than 12 months or short term highly liquid investments 	<p>into-</p> <ul style="list-style-type: none"> Security Deposits Loans to related Parties Others <p>Sub classified into -</p> <ul style="list-style-type: none"> Good & Secured Good but Unsecured TR With Significant increase in credit Risk Credit Impaired <p>Provision for bad & doubtful debts shall be separately disclosed under the relevant head.</p> <p>Loans due by directors/officers of entity shall be separately disclosed.</p>

For Trade Receivables outstanding, following ageing schedule shall be given:

Particulars	Outstanding for the following period from due date of payment*					Total
	Less than 6 months	6 months - 1 year	1 - 2 year	2 - 3 year	More than 3 years	
i) Undisputed Trade Receivables - Considered Good						
ii) Undisputed Trade Receivables - which have significant increase in credit risk						
iii) Undisputed Trade Receivables - Credit Impaired						
iv) Disputed Trade Receivables - Considered Good						
iv) Disputed Trade Receivables - which have significant increase in credit risk						
vi) Disputed Trade Receivables - Credit Impaired						

4. Non-Current Liabilities

BORROWINGS	PROVISIONS	OTHER NON-CURRENT
<p>Classified into:</p> <ul style="list-style-type: none"> • Bonds or debentures • Term Loans from Banks • Term Loans from Parties • Deferred payment liabilities • Deposits • Loans from related parties • Long term maturities of FL • Liability component of compound financial instruments • Other Loans (specify) <p>Borrowings shall Further Classified as Secured and Unsecured along with nature of security.</p> <p>Any guarantees by directors or</p>	<p>Classified into:</p> <ul style="list-style-type: none"> • Provision for Employee benefits • Others 	<p>Classified into-</p> <ul style="list-style-type: none"> • Advances • Others

<p>others</p> <p>Bonds or debentures in descending order of maturity or conversion</p> <p>Particulars of any redeemed bonds or debentures which the company can re-issue</p> <p>Terms of Repayments</p> <p>Period and amount of default as on BS date</p>		
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5. Current Liabilities

Borrowings	Other FL	Other CL	Provisions	Trade Payables
<p>Classified into:</p> <ul style="list-style-type: none"> • Bonds • Term Loans from Banks • Term Loans from Parties • Deferred payment liabilities • Deposits • Loans from related parties • Long term maturities of FL • Liability component of compound financial instruments • Other Loans <p>Further Classified as Secured and Unsecured along with nature of security.</p>	<p>Classified into-</p> <ol style="list-style-type: none"> a) Current maturities of long-term debt; b) Current maturities of finance lease obligations; c) Interest accrued; d) Unpaid dividends; e) Application money received for allotment of securities to the extent refundable and interest accrued thereon; f) Unpaid matured deposits and interest accrued thereon; 	<p>Classified into-</p> <ol style="list-style-type: none"> (a) revenue received in advance; (b) other advances and (c) others 	<p>Classified into:</p> <ul style="list-style-type: none"> • Provision for Employee benefits • Others 	<p>Classified into-</p> <ul style="list-style-type: none"> • Outstanding from Micro Enterprises & Small Enterprises; and • Outstanding from others

Any guarantees by directors or others	g) Unpaid matured debentures and interest accrued thereon; and h) Others			
Period and amount of default as on BS date Current Maturity of long-term debt to be disclosed separately				

Trade Payables Ageing Schedule:

Particulars	Outstanding for the following period from due date of payment*				Total
	Less than 1 year	1-2 years	2 - 3 year	More than 3 years	
I) MSME					
ii) Other					
iii) Disputed Dues - MSME					
iv) Disputed Dues - Others					

*Similar information shall be given where no due date of payment is specified in that case disclosure shall be from the date of the transaction.

Unbilled dues shall be disclosed separately.

6. Contingent Liabilities and Commitments: (to the extent not provided for)

(a) Contingent Liabilities shall be classified as-

- claims against the company not acknowledged as debt.
- guarantees excluding financial guarantees; and
- other money for which the company is contingently liable.

(ii) Commitments shall be classified as-

- (a) estimated amount of contracts remaining to be executed on capital account and not provided for;
- (b) uncalled liability on shares and other investments partly paid; and
- (c) other commitments (specify nature).

7. Following Ratios to be disclosed:

- (a) Current Ratio,
- (b) Debt-Equity Ratio,

- (c) Debt Service Coverage Ratio,
- (d) Return on Equity Ratio,
- (e) Inventory turnover ratio,
- (f) Trade Receivables turnover ratio,
- (g) Trade payables turnover ratio,
- (h) Net capital turnover ratio,
 - Net profit ratio,
- j) Return on Capital employed,
- k) Return on investment.

The company shall explain the items included in numerator and denominator for computing the above ratios. Further explanation shall be provided for any change in the ratio by more than 25% as compared to the preceding year.

PART II - STATEMENT OF PROFIT AND LOSS

Name of the Company.....

Statement of Profit and Loss for the period ended.....

	Particulars	Note No.	Figures as at the end of current reporting period	Figures for the previous reporting period
I	Revenue from operations	IndAS - 115		
II	Other Income			
III	Total Income (I + II)			
IV	EXPENSES			
a.	Cost of materials consumed (Opn. RM + Purchased - Clog. RM)			
b.	Purchases of Stock-in-Trade			
c.	Changes in inventories of finished goods, Stock-in -Trade and work-in-progress			
d.	Employee benefits expense	IndAS- 19		
e.	Finance costs	IndAS-32		
f.	Depreciation and amortization expenses	IndAS - 16 & 38		
g.	Other expenses			
	Total expenses (IV)			
V	Profit/(loss) before exceptional items and tax (I-IV)			

VI	Exceptional Items			
VII	Profit/ (loss) before Tax (V-VI)			
VIII	Tax expense: (1) Current tax (2) Deferred tax	IndAS - 12		
IX	Profit (Loss) for the period from continuing operations (VII - VIII)			
X	Profit/(loss) from discontinued operations			
XI	Tax expenses of discontinued operations			
XII	Profit/(loss) from Discontinued operations (after tax) (X-XI)			
XI II	Profit/(loss) for the period (IX+XII)			
XIV	Other Comprehensive Income A. (i) Items that will not be reclassified to profit or loss (ii) Income tax relating to items that will not be reclassified to profit or loss B. (i) Items that will be reclassified to profit or loss (ii) Income tax relating to items that will be reclassified to profit or loss			
XV	Total Comprehensive Income for the period (XIII+XIV) Comprising Profit (Loss) and Other comprehensive Income for the period)			
XVI	Earnings per equity share (for continuing operation): (1) Basic (2) Diluted	IndAS - 33		
XV II	Earnings per equity share (for discontinued operation): (1) Basic (2) Diluted	IndAS - 33		
XV III	Earning per equity share (for Discontinued & continuing operation) (1) Basic (2) Diluted	IndAS - 33		

GENERAL INSTRUCTIONS FOR PREPARING OF STATEMENT OF PROFIT AND LOSS

1. The Statement of Profit and Loss shall include:
 - (1) Profit or loss for the Period;
 - (2) Other Comprehensive Income for the period

The sum of (1) and (2) above is "Total Comprehensive Income"

2. Revenue from operations shall disclose separately in the notes
 - (i) sale of products (including Excise Duty);
 - (ii) sale of services;
 - (iii) Grant or donation received (relevant in case of section 8 companies only) and
 - (iii) Other operating revenues.

3. Finance Costs: Finance costs shall be classified as-
 - (i) interest;
 - (ii) dividend on redeemable preference shares;
 - (iii) exchange differences regarded as an adjustment to borrowing costs; and
 - (iv) Other borrowing costs (specify nature).

4. Other income: other income shall be classified as-
 - (a) interest Income;
 - (b) dividend Income; and
 - (c) other non-operating income (net of expenses directly attributable to such income)

5. Other Comprehensive Income shall be classified into-

(A) Items that will not be reclassified to profit or loss (NRPL):

 - (i) Changes in revaluation surplus;
 - (ii) Re-measurements of the defined benefit plans;
 - (iii) Equity Instruments through Other Comprehensive Income;
 - (iv) Fair value changes relating to own credit risk of financial liabilities designated at fair value through profit or loss;
 - (v) Share of Other Comprehensive Income in Associates and Joint Ventures, to the extent **not** to be classified into profit or loss; and
 - (vi) Others (specify nature).

(B) Items that will be reclassified to profit or loss (RPL):

 - (i) Exchange differences in translating the financial statements of a foreign operation;

- (ii) Debt instruments through Other Comprehensive Income;
- (iii) The effective portion of gains and loss on hedging instruments in a cash flow hedge;
- (iv) Share of other comprehensive income in Associates and Joint Ventures, to the extent to be classified into profit or loss; and
- (v) Others (specify nature)

6. Additional Information: A Company shall disclose by way of notes, additional information regarding aggregate expenditure and income on the following items:

- (a) employee Benefits expense (showing separately (i) salaries and wages, (ii) contribution to provident and other funds, (iii) share based payments to employees, (iv) staff welfare expenses).
- (b) depreciation and amortisation expense;
- (c) any item of income or expenditure which exceeds one per cent of the revenue from operations or Rs 10,00,000, whichever is higher, in addition to the consideration of 'materiality' as specified in clause 7 of the General Instructions for Preparation of Financial Statements of a Company;
- (d) interest Income;
- (e) interest Expense
- (f) dividend income;
- (g) net gain or loss on sale of investments;
- (h) net gain or loss on foreign currency transaction and translation (other than considered as finance cost);
- (i) payments to the auditor as (a) auditor, (b) for taxation matters, (c) for company law matters, (d) for other services, (e) for reimbursement of expenses;
- (j) in case of companies covered under section 135, amount of expenditure incurred on corporate social responsibility activities; and
- (k) details of items of exceptional nature;

7. Depending upon the **Total Income** of the company, the figures appearing in the Financial Statements shall be rounded off as below:

Turnover	Rounding off
a) less than one hundred crore rupees	To the nearest hundreds, thousands, lakhs or millions, or decimals thereof
b) one hundred crore rupees or more	To the nearest, lakhs, millions or crores, or decimals thereof.

Once a unit of measurement is used, it should be used uniformly in the Financial Statements.

03

FRAMEWORK FOR PREPARATION AND PRESENTATION OF FINANCIAL STATEMENTS

**“Ever tried. Ever failed. No matter.
Try Again. Fail again. Fail better.”**

1. INTRODUCTION

1. The Conceptual Framework for Financial Reporting under Indian Accounting Standards (INDAS) (hereinafter the 'Conceptual Framework under INDAS') is **not a Standard** and it **does not override any standard or any requirement in any standard**.
2. Therefore, this does not form part of a set of standards pronounced by the standard- setters.
3. While the Conceptual Framework under INDAS is primarily meant for the **standard- setter** for formulating the standards, it has relevance to the **preparers** in certain situations such as to develop consistent accounting policies for areas that are not covered by a standard or where there is choice of accounting policy, and **to assist all parties** to understand and interpret the Standards.
4. As a result, certain individual standards e.g. INDAS 1, Presentation of Financial Statements, INDAS 8, Accounting Policies, Changes in Accounting Estimates and Errors, INDAS 103, Business Combinations, etc., require the preparers to follow the guidance in the Conceptual Framework for Financial reporting under Indian Accounting Standards.
5. Nothing in the Conceptual Framework under INDAS overrides any INDAS or any requirement in an INDAS.

2. OBJECTIVES OF GENERAL PURPOSE FINANCIAL REPORTING

2.1 OBJECTIVES

To provide financial information about the reporting entity that is useful to:

- Existing and potential investors,
- Lenders and
- Other creditors

in making decisions relating to providing resources to the entity.

Those decisions involve decisions about:

- (a) Buying, selling or holding equity and debt instruments;
- (b) Providing or settling loans and other forms of credit; or
- (c) Exercising rights to vote on, or otherwise influence, management's actions that affect the use of the entity's economic resources.

2.2 LIMITATION OF GENERAL PURPOSE FINANCIAL REPORTING

General purpose financial reports:

- Do not and cannot provide all of the information that existing and potential investors, lenders and other creditors need. Those users need to consider pertinent information from other sources, for example, general economic conditions and expectations, political events and political climate, and industry and company outlooks;
- Are not designed to show the **value of a reporting entity**; but they provide information to help existing and potential investors, lenders and other creditors to estimate the value of the reporting entity; and
- Are not **primarily directed to other parties**, such as regulators and members of the public other than investors, lenders and other creditors.

2.3 INFORMATION PROVIDED BY GENERAL PURPOSE FINANCIAL REPORTS

GPFR provides Financial Information such as:

1. **Financial Information on Financial Position** – contains Economic Resources of entity (i.e. Assets) and Claims on Entity (Liabilities)
2. **Effects of transactions and other events that change entity's economic resources and claims** – contains Financial performance (Comprehensive Income), Cash Flows and Changes not resulting from financial performance.

2.3.1 Economic Resources and Claims

Information about the nature and amounts of a reporting entity's economic resources and claims can help users to identify the reporting entity's financial strengths and weaknesses. That information can help users to:

- (a) assess the reporting entity's:
 - (i) **liquidity and solvency,**
 - (ii) **its needs for additional financing and**
 - (iii) **how successful it is likely to be in obtaining that financing**
- (b) assess management's stewardship of the entity's economic resources
- (c) predict how future cash flows will be distributed among those with a claim against the reporting entity

2.3.2 Changes in Economic Resources and Claims

Changes in a reporting entity's economic resources and claims result from:

- ◆ that entity's financial performance and
- ◆ other events or transactions such as issuing debt or equity instruments

To properly assess both the prospects for future net cash inflows to the reporting entity and management's stewardship of the entity's economic resources, users need to be able to identify those two types of changes.

3. QUALITATIVE CHARACTERISTICS OF USEFUL FINANCIAL INFORMATION

3.1 QUALITATIVE CHARACTERISTICS OF USEFUL FINANCIAL INFORMATION

Sr. No.	Qualitative Characteristics	Meaning
1	Relevance	Financial information should have a predictive value or confirmatory value or both, if this is a case then financial information is considered as Relevant for decision making. Relevance also includes Materiality.
2	Faithful Representation	Financial information should be based on Substance of the Economic phenomenon if its legal form is different. Providing information only about the legal form would not faithfully represent the economic phenomenon.
3	Completeness	Financial information should be complete with all necessary descriptions and Explanations.
4	Neutral	A neutral depiction is without bias in the selection or presentation of financial information. A neutral depiction is not slanted, weighted, emphasised, de-emphasised or otherwise manipulated to increase the probability that financial information will be received favourably or unfavourably by users.
5	Free from Error	Free from error means there are no errors or omissions in the description of the phenomenon, and the process used to produce the reported information has been selected and applied with no errors in the process.
6	Comparability	Financial information should be comparable with alternatives to take decisions
7	Verifiability	Verifiability means that different knowledgeable and independent observers could reach consensus, although not necessarily complete agreement, that a particular depiction is a faithful representation.
8	Timeliness	Timeliness means having information available to decision-makers in time to be capable of influencing their decisions.
9	Understandability	Classifying, characterising and presenting information clearly and concisely makes it understandable.

3.2 THE COST CONSTRAINT ON USEFUL FINANCIAL INFORMATION

1. Cost is a pervasive constraint on the information that can be provided by financial reporting. Reporting financial information imposes costs, and it is important that those costs are justified by the benefits of reporting that information.
2. Both the providers and users of financial information incur costs in reporting and analysing financial information. In applying the cost constraint, the ICAI assesses whether the benefits of reporting particular information are likely to justify the costs incurred to provide and use that information. When applying the cost constraint in formulating a proposed INDAS, the ICAI seeks information from providers of financial information, users, auditors, academics and others about the expected nature and quantity of the benefits and costs of that INDAS. In most situations, assessments are based on a combination of quantitative and qualitative information.
3. Because of the inherent subjectivity, different individuals' assessments of the costs and benefits of reporting particular items of financial information will vary. Therefore, the ICAI seeks to consider costs and benefits in relation to financial reporting generally, and not just in relation to individual reporting entities.

4. FINANCIAL STATEMENTS & REPORTING ENTITY

4.1 OBJECTIVE AND SCOPE OF FINANCIAL STATEMENTS

The objective of financial statements is to provide financial information about the reporting entity's:

- Assets, liabilities and equity; and
- Income and expenses

that is useful to users of financial statements in assessing:

- The prospects for future net cash inflows to the reporting entity, and
- Management's stewardship of the entity's economic resources

Such financial information is provided:

1. In the balance sheet, by recognising assets, liabilities and equity;
2. In the statement of profit and loss, by recognising income and expenses; and
3. In other statements and notes, by presenting and disclosing information about:
 - Recognised assets, liabilities, equity, income and expenses, including information about their nature and about the risks arising from those recognised assets and liabilities;
 - Assets and liabilities that have not been recognised, including information about their nature and about the risks arising from them;
 - Cash flows;
 - Contributions from holders of equity claims and distributions to them; and
 - The methods, assumptions and judgements used in estimating the amounts presented or disclosed, and changes in those methods, assumptions and judgements.

4.1.1 Reporting period

Financial statements are prepared for a specified period of time (reporting period) and to help users of financial statements to identify and assess changes and trends; financial statements also provide comparative information for at least one preceding reporting period.

4.1.2 Perspective adopted in financial statements

Financial statements provide information about transactions and other events viewed from the perspective of the reporting entity as a whole, not from the perspective of any particular group of the entity's existing or potential investors, lenders or other creditors.

4.1.3 Going concern assumption

Financial statements are normally prepared on the assumption that the reporting entity is a going concern and will continue in operation for the foreseeable future. Hence, it is assumed that the entity has neither the intention nor the need to enter liquidation or to cease trading. If such an intention or need exists, the financial statements may have to be prepared on a different basis. If so, the financial statements describe the basis used.

(Refer Practical Example 1)

4.2 THE REPORTING ENTITY

A reporting entity is an entity that is required, or chooses, to prepare financial statements.

If the reporting entity is not a legal entity and does not comprise only legal entities linked by a parent-subsidary relationship, how can the boundary of reporting entity be determined?

In such cases, determining the boundary of the reporting entity is driven by the information needs of the primary users of the reporting entity's financial statements. Those users need relevant information that faithfully represents what it purports to represent. Faithful representation requires that:

- (a) The boundary of the reporting entity does not contain an arbitrary or incomplete set of economic activities;
- (b) Including that set of economic activities within the boundary of the reporting entity results in neutral information; and
- (c) A description is provided of how the boundary of the reporting entity was determined and of what constitutes the reporting entity

4.2.1 Consolidated and unconsolidated financial statements

Consolidated financial statements provide information about the assets, liabilities, equity, income and expenses of both the parent and its subsidiaries as a single reporting entity. That information is useful for existing and potential investors, lenders and other creditors of the parent in their assessment of the prospects for future net cash inflows to the parent. This is because net cash inflows to the parent include distributions to the parent from its subsidiaries, and those distributions depend on net cash inflows to the subsidiaries.

Consolidated financial statements are not designed to provide separate information about the assets, liabilities, equity, income and expenses of any particular subsidiary. A subsidiary's own financial statements are designed to provide that information.

5. THE ELEMENTS OF FINANCIAL STATEMENTS

Broadly, a statement of financial position or balance sheet comprises three elements viz. Asset, Liability and Equity which can be described as below -

(a) ASSETS - A present economic resource **controlled** by the entity as a result of past events. An economic resource is a **right** that has the **potential to produce economic benefits**.

Right to Entity (or Obligation of Another Party)

+ **Potential for Future Economic Benefits**

+ **Control**

Example: Control over Asset (substance over form)

Due to some legal constraints in the country, Entity A holds some assets on behalf of Company B which are being used/ directed by the Company B itself, without any interfere by the Company A. All production benefits will exclusively be used by Company B.

Merely holding an asset as its legal owner will not satisfy recognition criteria for an asset, hence, Asset will be recognized in the books of Company B as all the future economic benefit which is expected to flow to Company B only.

Example: Economic Benefits Flow to the Entity

A Pharma Company incurs some expenditure which is expensed off in order to develop its new drug. The future economic benefits will not have expected to flow to the Pharma Company because research phase itself does not establish any rationale to provide any kind of benefit which will flow to the Company at this stage (as per the relevant accounting standards).

Hence all expenditures will not be eligible to recognize as asset unless its benefits are expected

(b) LIABILITY - A liability is a **present obligation** of the entity arising from past events, the settlement of which is expected to result in an **outflow** from the entity of resources embodying economic benefit



Example: Present Obligation based on Past Events

An Entity has got information about the requirement to implement new taxation system based on proposed change in legislation in the country. The amount that is expected to outflow from the entity

is not based on past events and hence this cannot be treated as present obligation.

Example: Additional Custom Duty Rate Changes

An import has been done in the past on which there is change in additional duty, as announced by the government of that country, which is to be paid in future. Since, the goods have been imported in the past period and new additional custom duty obligation arises because of this past event, hence this will result in a present obligation based on past events and therefore, a liability will be created. Settlement of such liability could be in cash, transfer of other assets, conversion of obligation into equity etc. There are liabilities, where timing and amount are not certain, but meets the recognition criteria, then the amounts are being estimated using some techniques and shown as provisions.

(c)EQUITY - Equity is the **residual interest in the assets of the entity** after deducting all its liabilities.

(d)INCOME - Income is **increases in economic benefits** during the accounting period **in the form of inflows or enhancements of assets or decreases of liabilities that result in increases in equity**, other than those relating to contributions from equity participants.

(e)EXPENSES - Expenses are **decreases in economic benefits** during the accounting period **in the form of outflows or depletions of assets or incurrences of liabilities that result in decreases in equity**, other than those relating to distributions to equity participants.

ASPECTS WHICH ARE COMMON TO ASSETS AND LIABILITIES

1. Unit of Account
2. Executory Contracts
3. Substance of Contractual Rights and Contractual Obligations

6. RECOGNITION AND DERECOGNITION

6.1 THE RECOGNITION PROCESS

- Recognition is the process of capturing for inclusion
- In the balance sheet or the statement of profit and loss
- An item that meets the definition of one of the elements of financial statements—an asset, a liability, equity, income or expenses.

The amount at which an asset, a liability or equity is recognised in the balance sheet is referred to as its 'carrying amount'

6.2 RECOGNITION CRITERIA

Only items that meet the definition of an asset, a liability or equity are recognised in the balance sheet. Similarly, only items that meet the definition of income or expenses are recognised in the statement of profit and loss. However, not all items that meet the definition of one of those elements are recognised.

An asset or liability is recognised only if recognition provides users of financial statements with information that is useful, i.e. with:

- a. Relevant information; and
- b. A faithful representation of the asset or liability and of any resulting income, expenses or changes in equity.

6.3 DERECOGNITION

Derecognition is the removal of all or part of a recognised asset or liability from an entity's balance sheet. Derecognition normally occurs when that item no longer meets the definition of an asset or of a liability

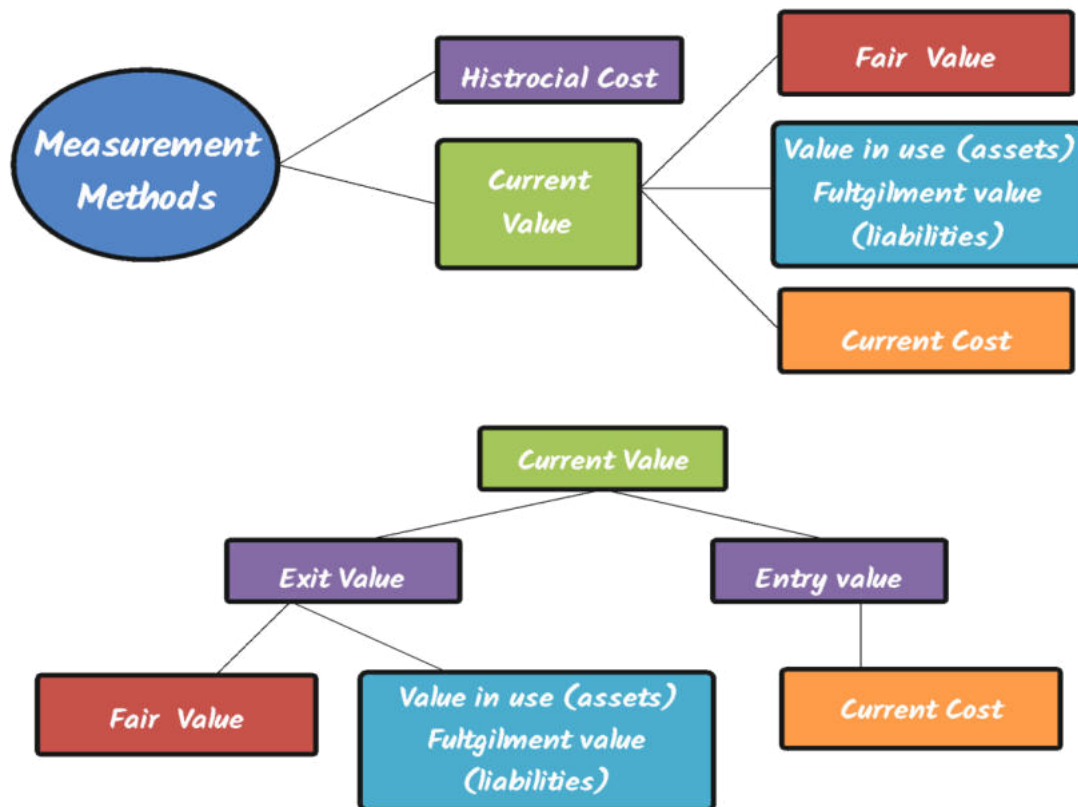
Derecognition of Asset - When the entity loses control of all or part of the recognised asset

Derecognition of Liability - When the entity no longer has a present obligation for all or part of the recognised liability

In some cases, an entity might appear to transfer an asset or liability, but derecognition of that asset or liability is not appropriate. For example,

- If an entity has apparently transferred an asset but retains exposure to significant positive or negative variations in the amount of economic benefits that may be produced by the asset, this sometimes indicates that the entity might continue to control that asset
- If an entity has transferred an asset to another party that holds the asset as an agent for the entity, the transferor still controls the asset.

7. MEASUREMENT OF THE ELEMENTS OF FINANCIAL STATEMENTS



A very broad comparison between the historical cost and current value measurement bases is given below

Factor	Historical cost	Current value
Monetary information about assets liabilities and related income and expenses	Derived at least in part, from the price of the transaction or other event that gave rise to them	Using information updated to reflect conditions at the measurement date
Changes in values	Not reflected except to the extent that those changes relate to impairment of an asset or a liability becoming onerous	Reflect changes, since the previous measurement date, in estimates of cash flows and other factors reflected in those current values

1 Historical cost

The table below summarises the concept of 'historical cost' in case of assets and liabilities:

Particulars	Assets	Liabilities
Components	Consideration paid (+) transaction costs	Consideration received (-) transaction costs
Changes	<ul style="list-style-type: none"> consumption of part or all of the economic resource that constitutes the asset (depreciation or 	

	amortisation)	
	<ul style="list-style-type: none"> • payments received that extinguish part or all of the asset (collection from trade receivables) 	<ul style="list-style-type: none"> • fulfilment of the liability, for example, by making payments that extinguish part or all of the liability or by satisfying an obligation to deliver goods
	<ul style="list-style-type: none"> • effect of events that cause the historical cost of the asset to be no longer recoverable (impairment) 	<ul style="list-style-type: none"> • effect of events that increase the value of the obligation to transfer the economic resources needed to fulfil the liability to such an extent that the liability becomes onerous. A liability is onerous if the historical cost is no longer sufficient to depict the obligation to fulfil the liability
	<ul style="list-style-type: none"> • accrual of interest to reflect any financing component 	accrual of interest to reflect any financing component

2. Exit Value - Fair Value in use/fulfilment value

The following table summarises these concepts in comparative form:

Particulars	Fair Value	Value in use/Fulfillment value
Definition	Price that would be received to sell an asset, or paid to transfer a liability, in an orderly transaction between market participants at the measurement date	Value in use present value of the cash flows, or other economic benefits, that an entity expects to derive from the use of an asset and from its ultimate disposal. Fulfilment value - present value of the cash, or other economic resources, that an entity expects to be obliged to transfer as it fulfils a liability.
Value From whose perspective?	Reflects the perspective of market participants-participants in a market to which the entity has access the assets or liability is measured using the same assumptions that market participants would use when pricing the asset or liability if those market participants act in their economic best interest	Reflect entity specific assumptions rather than assumptions by market participants
How determined?	Directly by observing prices in active market or using measurement techniques, for example cash-flow-based measurement techniques	Cannot be observed directly and are determined using cash-flow based measurement techniques
Transaction costs considered in measurement?	Neither those costs incurred on initial recognition, nor those costs to be incurred on disposal of asset or settlement of liability are considered	Those costs incurred on initial recognition are not considered, but the present value of those costs to be incurred on disposal of assets or settlement of liability are considered.

3. Entry Value - Current Cost:

Like Historical cost, current cost is also an entry value. Hence, it would be appropriate to understand the concept of 'current cost' by comparing it with 'historical cost' as below:

Particulars	Historical Cost	Current Cost
Value determined on	Date of acquisition of asset or incurrence of liability	Each measurement date.
Components	Assets: Consideration paid (+) transactions costs Liabilities: Consideration received (-) transaction costs	Assets: consideration that would be paid (+) transaction costs that would be incurred Liabilities: Consideration that would be received (-) transaction costs that would be incurred.

MEASUREMENT OF EQUITY

The total carrying amount of equity (total equity) is not measured directly. It equals the total of the carrying amounts of all recognised assets less the total of the carrying amounts of all recognised liabilities.

8. PRESENTATION AND DISCLOSURE

8.1 PRESENTATION AND DISCLOSURE OBJECTIVES AND PRINCIPLES

To facilitate effective communication of information in financial statements, when developing presentation and disclosure requirements in INDASs a balance is needed between:

- Giving entities the flexibility to provide relevant information that faithfully represents the entity's assets, liabilities, equity, income and expenses; and
- Requiring information that is comparable, both from period to period for a reporting entity and in a single reporting period across entities.

8.2 CLASSIFICATION

Classification is the sorting of assets, liabilities, equity, income or expenses on the basis of shared characteristics for presentation and disclosure purposes. Such characteristics include — but are not limited to the nature of the item, its role (or function) within the business activities conducted by the entity, and how it is measured. Classifying dissimilar assets, liabilities, equity, income or expenses together can obscure relevant information, reduce understandability and comparability and may not provide a faithful representation of what it purports to represent.

8.2.1 Profit or loss and other comprehensive income

Income and expenses are classified and included either:

- In the profit or loss section of statement of profit and loss; or
- Outside the profit or loss section of statement of profit and loss, in other comprehensive income.

8.3 AGGREGATION

Aggregation is adding together of assets, liabilities, equity, income or expenses that have shared characteristics and are included in the same classification.

Aggregation makes information more useful by summarising a large volume of detail. However, aggregation conceals some of that detail. Hence, a balance needs to be found so that relevant information is not obscured either by a large amount of insignificant detail or by excessive aggregation.

9. FINANCIAL CAPITAL MAINTENANCE VS. PHYSICAL CAPITAL MAINTENANCE

(Also Refer Practical Examples 2, 3 & 4)

The concept of capital maintenance is concerned with how an entity defines the capital that it seeks to maintain. It provides the linkage between the concepts of capital and the concepts of profit because it provides the point of reference by which profit is measured. In general terms, an entity has maintained its capital if it has as much capital at the end of the period as it had at the beginning of the period. Any amount over and above that required to maintain the capital at the beginning of the period is profit.

There are two concepts of capital maintenance:

- A. **Financial Capital maintenance** Under this concept, a profit is earned only if the financial amount of the net assets at the end of the period exceeds the financial amount of net assets at the beginning of the period, after excluding any distribution to, and contribution from, owners during the period.
- B. **Physical Capital maintenance** Under this concept, a profit is earned only if the physical productive or operating capability of the entity at the the end of the period exceeds the physical productive capacity at the beginning of the period, after excluding any distributions to, and contributions from, owners during the period .

04

IND AS 1

PRESENTATION OF FINANCIAL STATEMENTS

“The way to get Started is to
Quit Talking & Begin Doing”

1. SUMMARY OF THE STANDARD

1. Applicable for preparing and presenting *General purpose financial statements (not for any specific industry)*.
2. General purpose FS means - which intends to fulfill the need of those users who cannot require an entity to prepare tailored reports (means customized reports) for their particular needs.
3. **Not** applicable to the *Structure and Content* of condensed Interim FS (where IND AS 34 is applicable) except provisions relating to Fair presentation, compliance with IND AS and Fundamental accounting assumptions.
4. It uses terminology suitable for *Profit Oriented entities*. (Entities having non-profit activities have to amend description used for particular line item)
5. **Material (Amended definition)**
 - Information is material if omitting, misstating or *obscuring it could reasonably be expected to influence decisions* that the *primary users* of general purpose financial statements make on the basis of those financial statements, which provide financial information about a specific reporting entity.
 - Materiality depends on the *nature or magnitude (size)* of information, or both. An entity assesses whether information, either individually or in combination with other information, is material in the context of its financial statements taken as a whole.
 - *Information is obscured if it is communicated in a way that would have a similar effect for primary users of financial statements to omitting or misstating that information.*

Examples of circumstances that may result in material information being obscured:

- (a) information regarding a material item, transaction or other event is disclosed in the financial statements but the **language used is vague or unclear**;
- (b) information regarding a material item, transaction or other event is **scattered throughout** the financial statements;
- (c) **dissimilar** items, transactions or other events are **inappropriately** aggregated;
- (d) **similar** items, transactions or other events are **inappropriately** disaggregated; and



(e) the understandability of the financial statements is reduced as a result of **material information being hidden by immaterial information** to the extent that a primary user is unable to determine what information is material.

6. Notes - **Additional information, Narrative descriptions or disaggregation of items.**
7. **OCI (Other Comprehensive Income)**- Items which are not recognized in the statement of Profit or loss as per any other IND ASs. Components of OCI (examples):
- (i) Revaluation Reserve (IND AS 16 & IND AS 38)
 - (ii) Re Measurements of defined benefit Plans i.e. Actuarial Gains and Losses (IND AS19)
 - (iii) FCTR on conversion of Foreign Operations (IND AS 21)
 - (iv) Change in fair value of Equity Instruments if not HFT and designated as FVTOCI (IND AS 109)
 - (v) Change in fair value of Hedged Instrument in case of CASH FLOW HEDGE (IND AS 109)
8. **Reclassification adjustments** - amounts reclassified to Profit or Loss in current period that were recognized in OCI in the current or previous periods.
9. **Complete Set of Financial Statements**
- (a) A Balance Sheet as at the end of the Period
 - (b) A Statement of Profit and Loss for the period (two sections - P&L and OCI)
 - (c) A Statement of Changes in Equity for the period (all owner changes in equity)
 - (d) A Statement of Cash Flows for the period
 - (e) Notes, significant a/c policies and explanatory information
 - (f) Comparative information in respect of preceding period (including Notes).
 - (g) A Balance Sheet as at the beginning of preceding period **if entity applies accounting policy retrospectively or makes retrospective restatement of items or on reclassification of items and they are material.** (Notes of this Opening BS need not be presented)
10. Entity shall make an **EXPLICIT & UNRESERVED STATEMENT** of compliance if its FS are complied with in accordance with IND ASs.
However IND AS 1 allows deviation from a requirement of an Accounting Standard in case:
- The Management concludes that compliance with IND ASs will be misleading; &
 - If the regulatory framework requires such a departure OR if the regulatory framework does not prohibit such a departure.
- Else, Disclosure of non-compliance is required to be given.**
11. **Inappropriate** Accounting policies **can-not be rectified** only by Disclosure, or Notes or Explanatory statements. It should be retrospectively adjusted as per Ind AS 8
12. FS shall be prepared on the basis of **GOING CONCERN** unless there is intention to liquidate or to cease trading or has no realistic alternative but to do so.

If on the basis of *material uncertainties that may cast significant doubt upon the entity's ability to continue as a going concern* the entity shall disclose such uncertainties.

If FS are *not* prepared on Going Concern Basis then it shall disclose such fact along with the basis on which it is prepared and reasons.

Assessment of Going Concern assumption should be based on all available future information which is *at least 12 months* from the end of reporting period.

13. FS shall be prepared on **ACCRUAL** basis.
14. No offsetting of Assets and Liabilities or Incomes and Expenses unless requires by IND AS. Measuring assets net of valuation allowances — for example, obsolescence allowances on inventories and doubtful debts allowances on receivables—is not offsetting.
15. Frequency of Reporting: *at least Annual*.
16. Change in Presentation or Change in Classification of items in FS - *reclassify comparative amounts* unless it is impracticable.
17. **Consistency:** Presentation and Classification of items shall be consistent from one period to next unless:
 - (a) It is apparent that such change would be more appropriate; or
 - (b) An IND AS requires such Change.
18. **Structure and Content of FS:** Clearly identify each financial statements and notes and distinguished from other information in published documents. Disclose following information prominently and repeat it as necessary:
 - (a) Name of reporting entity and any change in the name
 - (b) Whether FS are of Individual entity or Group of Entity
 - (c) Date of end of reporting period or the period covered by FS
 - (d) Presentation currency used
 - (e) Level of rounding used.
19. Separate classification for Current and Non-Current items except when presentation on liquidity basis provides reliable and more relevant information. (Even mixed basis is allowed in diverse operations)
20. IND AS 1 does not prescribe format of FS rather prescribed minimum line items.
21. **Current Assets as per (Schedule III of Comp Act, 2013):**
 - (a) It expects to realise the asset, or intends to sell or consume it, in its normal operating cycle (receivables and inventories);
 - (b) It holds the asset primarily for the purpose of trading (Financial Instr. - HFT);

- (c) It expects to be realised within 12 months after the reporting period.
- (d) Cash and Cash equivalents, unless it is restricted for being exchanged or used to settle liability for at least 12 months after the reporting period.

22. Normal operating cycle is the **Time between** the acquisition of assets for processing and the irrealisation in cash or cash equivalents. **If not clearly identifiable** it is assumed to have a period of **12months**.

Note: To determine the operating cycle, **each business segment** shall be assessed separately. Operating cycle can be different segment wise. Hence it should not be assessed on whole business wise.

23. **Current liabilities** are those:

- expected to be settled within the entity's normal operating cycle
- held for purpose of trading
- due to be settled within 12months
- for which the entity does not have an unconditional right to defer settlement beyond 12 months (settlement by the issue of equity instruments does not impact classification).

Note:

1. Financial institutions or Entities with diverse operations may present assets and liabilities in **increasing or decreasing order of liquidity** if the presentation is reliable and more relevant than a current / non-current presentation. This is because such entity does not supply goods or services within a clearly identifiable operating cycle.
2. The need for a mixed basis of presentation might arise when an entity has diverse operations.

Example 1:

An entity produces whisky from barley, water and yeast in a 24-month distillation process. At the end of the reporting period the entity has one month's supply of barley and yeast raw materials, 800 barrels of partly distilled whisky and 200 barrels of distilled whisky.

All raw materials (barley and yeast) work in process (partly distilled whisky) and finished goods (distilled whisky) are inventories. The raw materials are expected to be realised (ie turned into cash after being processed into whisky) in the entity's normal operating cycle. Therefore, even though the realisation is expected to take place more than twelve months after the end of the reporting period, the raw materials, work in progress and finished goods are current assets.

Example 2:

An entity owns a machine with which it manufactures goods for sale. It also owns the building in which it carries out its commercial activities.

The machine and the building are non-current assets because:

- ◆ They are not cash or cash equivalents;
- ◆ They are not expected to be realised or consumed in the entity's normal operating cycle;

- ◆ They are not held for the purpose of trading; and
- ◆ They are not expected to be realised within twelve months of the end of the reporting period.

Example 3

On 31 December 20x2, an entity replaced a machine in its production line. The replaced machine was sold to a competitor for Rs. 300,000. Payment is due 15 months after the end of the reporting period. The receivable is a non-current asset because:

- ◆ It is not cash or a cash equivalent;
- ◆ It is not expected to be realised or consumed in the entity's normal operating cycle;
- ◆ It is not held for the purpose of trading; and
- ◆ It is not expected to be realised within twelve months of the end of the reporting period.

Note: If payment was due in less than twelve months from the end of the reporting period, it would have been classified as a current asset.

24. REFINANCING:

<p>Refinancing Agreement on a long term basis is completed after the reporting period but before the approval of FS - Treat FL as Current when it is due to be settled within 12 months after RP. (Non-adjusting Event)</p>	<p>At the Reporting date, if Entity Expects and has discretion to refinance/roll over the Obligation for at least 12 months - Treat FL as Non- Current even it is due to be settled within 12months.</p>
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25. BREACH OF PROVISION OF LONG TERM LOAN ARRANGMENT ON OR BEFORE REPORTING DATE:

Non - Current	Non-Current	Current
<p>If Liability become repayable on demand and if lender agreed after reporting period but before approval of FS for not demanding the payment. (Adjusting Event)</p>	<p>If lender agreed to provide grace period before end of reporting period for at least 12 months from the end of reporting date and during which lender cannot demand immediate payments.</p>	<p>If Liability becomes repayable on demand and if the lender does not agreed for not Demanding the payment.</p>

26. Statement of Profit or loss and Other Comprehensive income: Under the Single Statement only

27. Allocation of Profit or loss and OCI attributable to:

- (a) Non -controlling Interest; and
- (b) Owners of the parent

28. OCI will be grouped into the items:

- (a) Which will not be reclassified subsequently to Profit or loss; and
- (b) Which will be reclassified subsequently to Profit or Loss A/c when conditions met.



29. EXTRAORDINARY ITEM: PROHIBITED**30. Presentation of Notes normally in following order:**

- (a) Statement of compliance with IND ASs
- (b) Summary of Significant Acc. Policies applied
- (c) Supporting information for items shown in BS, P&L, Cash Flows (i.e. schedules)
- (d) Other disclosures such as Contingent liabilities and Non-financial disclosures.

31. Disclosure of **Critical Judgments made by management in applying accounting policies in summary of significant accounting policies.**

Eg. of Critical judgment: whether substantially all the significant risks and rewards of ownership of FA and Leased Assets are transferred to other entities.

32. Disclose key source of **Estimation Uncertainty at the end of reporting period that have a significant risk of causing material adjustment to the carrying amounts of A/L within the next financial year.**

(Jo assumptions or estimations liye gaye hai year-end pe unke karan next f.y. me A/L ki book value par agar koi material impact aa sakta hai to vo assumptions or estimations disclose karo)

2. CARVE OUT

When ICAI decided to converge and not to adopt IFRS issued by the IASB, certain changes have been made considering the economic environment of the country, which is different as compared to the economic environment presumed to be in existence by IFRS. These differences are due to differences in **application of accounting principles and practices and economic conditions prevailing in India**. These differences which are in deviation to the accounting principles and practices stated in IFRS, are commonly known as 'Carve-outs'.

IAS 1	IND AS 1 (CARVE OUT)
<p>It requires that in case of a loan liability, if any condition of the agreement which was classified as Non-Current is breached on the reporting date, such loan liability should be classified as Current.</p> <p>Even if the breach is rectified after the reporting date, IAS 1 requires loans to be classified as Current.</p> <p style="text-align: center;">(Non-Adjusting Event)</p>	<p>It clarifies that when there is breach of a material provision of a long term loan liability on or before the end of reporting period with the effect that the liability becomes payable on demand on the reporting date, the entity does not classify the liability as Current, if the lender agreed not to demand payment as a consequence of breach after the reporting period and before the approval of financial statements for issue. (Adjusting Event)</p>

3. DIFFERENCE BETWEEN IND AS 1 & IAS 1

BASIS	IAS 1	IND AS 1
Single or Two Statements	It permits companies to present all items of income and expenses recognised either in a single or in two statements	It does not permit the two statement approach. All items of incomes and expenses to be presented in a single statement of Profit and Loss.
Analysis of Expenses	Expenses will be presented using the classification based on either their nature or their function within the company.	IND AS 1 mandates only nature wise classification of expenses.
Statement of Changes in Equity	It requires the statement to be presented as a separate statement.	Requires the statement to be presented as a part of the Balance Sheet.



05

IND AS 16 PROPERTY, PLANT & EQUIPMENT

Dream Big and Dare to Fail.....

(1) NON APPLICABILITY OF IND AS 16

1. When any other Standard specifically applied to a particular item or transaction such as **IND AS 116** on Leases of Fixed Assets.
2. Biological Assets related to Agricultural activity (IND AS 41 is applicable on such assets)
However, **IND AS 16 - PPE is applicable on Bearer Plants.**
3. PPE classified as "Held for Sale" (**IND AS 105**)
4. Recognition and Measurement of Exploration and Evaluation Assets (**IND AS 106**)
5. Mineral rights and mineral reserves such as oil, natural gas and similar non regenerative resources

(2) IMPORTANT DEFINITIONS

1. PROPERTY PLANT AND EQUIPMENT

Any **Tangible item** will be called as PPE if it satisfies the following Conditions:

Condition - 1	Condition - 2
Held for Use in <ul style="list-style-type: none"> • Production or Supply of goods and services • For Rental to Others • For Administrative Purposes 	Expected to be Used for more than 12 Months.
Renting should be the main business activity of the entity to Qualify tangible item as PPE otherwise it would be qualified as an Investment Property under IND AS 40	

Items of PPE may also be acquired for safety or environmental reasons:

Although not directly increasing the future economic benefits, Such items of PPE qualify for recognition as assets because they enable an enterprise to derive future economic benefits from related assets in excess of what could be derived had those items not been acquired.

2. BIOLOGICAL ASSETS

It means Living Plants and Animals. IND AS 16 applies on Bearer Plants only.

3. BEARER PLANT: a plant that satisfies all the 3 conditions:

Bearer Plant is a plant which	is used in the production or supply of Agricultural produce
	is expected to bear produce for more than a period of 12 months
	Has a remote likelihood of being sold as Agricultural produce Except for incidental scrap sales



Note: When bearer plants are no longer used to bear produce they might be cut down and sold as scrap. For example - use as firewood. Such incidental scrap sales would not prevent the plant from satisfying the definition of a Bearer Plant.

Example of bearer plant is Mango Tree, Coconut Tree etc

(3) RECOGNITION CRITERIA FOR PPE

The cost of an item of PPE should be recognized as an asset if, and only if:

- (a) It is probable that **future economic benefits** associated with the item will flow to the enterprise, and
- (b) The **cost** of the item can be **measured reliably**.

Treatment of Spare Parts, Standby Equipment and Servicing Equipment

Case I: If they meet the definition of PPE as per IND AS 16: Recognised as PPE as per IND AS 16

Case II: If they do not meet the definition of PPE as per IND AS 16: Such items are classified as Inventory as per IND AS 2.

- Treat Expense First as a part of Purchase of Goods
- if at the end of Reporting Period, these items are not yet fully consumed then treat them as Inventory (Closing Stock)

(4) MEASUREMENT OF PPE

At Initial Recognition	Subsequent measurement on Balance sheet date
COST MODEL	COST MODEL (Or) REVALUATION MODEL

Note: Selection of Any Model at BS date is an Accounting Policy.

INITIAL RECOGNITION

Cost of an item of PPE comprises:

COST Includes	COST Excludes
(a) Purchase Price including Import duties and Non-refundable Taxes	<ul style="list-style-type: none"> • Cost of Opening new business such as inauguration cost
(b) Any Directly attributable Costs bringing the Asset to its 'location and condition'	<ul style="list-style-type: none"> • Startup Costs (i.e. Legal Expenses) • Cost of introducing a new product including advertising
Eg. <ul style="list-style-type: none"> • Cost of Employee benefits on construction or acquisition of PPE • Installation Cost 	<ul style="list-style-type: none"> • Initial operating losses



- Cost of Testing the PPE
- Professional Fees
- Initial delivery Cost etc

(c) Decommissioning Restoration and Similar Liabilities

This cost is to be estimated using appropriate discounting rate i.e. it should be recognised initially at PV of future outflow.

- Cost of relocating or reorganizing part or all the operations of an enterprises.
- Administrative and other general overheads
- Abnormal Cost/Losses (eg. Loss due to strike)
- Staff Training Costs
- Income earned from incidental operations eg. Income from Car Park.

Excess of Net Proceeds from Sale of Items produced during testing will be **deducted from the Cost** of Item of PPE.

Carve Out: However IAS 16 prohibits this deduction and requires to transfer to P&L

(5) MEASUREMENT OF COST AT INITIAL RECOGNITION

Case - 1

If Payment is deferred beyond Normal Credit Terms:

Cost of an item of PPE is the **CASH PRICE EQUIVALENT (PV of agreed price)** at the recognition date. Total payment - Cash price equivalent = Deemed Interest, charged to P&L over the period of Credit unless such interest is capitalised in accordance with IND AS 23

Case - 2

PPE acquired in Exchange for a Non-monetary Asset or Assets or a combination of Monetary and Non-monetary Assets:

Cost of such an item of PPE is measured at fair value of Asset Given Up (1st Priority) or Asset Received (2nd Priority) unless:

- (i) Exchange transaction lacks commercial substance; Or
- (ii) Fair value of neither the asset(s) received nor the asset(s) given up is reliably measurable.

If the PPE acquired is not measured at Fair Value, its cost is measured at the carrying amount of the asset given up. (Refer Practical Examples 1 to 3)

Case - 3

PPE purchased for a Consolidated Price:

Where several items of PPE are purchased for a consolidated price, the consideration is apportioned to the various items on the basis of their respective fair values at the date of acquisition.

Note: In case the fair values of the items acquired cannot be measured reliably, these values are estimated on a fair basis as determined by competent valuer.

Case - 4

Government Grant related to PPE:

If Govt. Grant is received in Kind (i.e. PPE received at Free of Cost or at Concessional Price) then it should be recognised at Fair Value or Nominal Value as per IND AS 20.

Case - 5

Cost of Self Constructed Assets:

Construction Cost excluding Internal profit generated if any but including borrowing Costs.

Case - 6

Cost of Bearer Plants:

Bearer plants are accounted for in the same way as self-constructed items of property, plant and equipment before they are in the location and condition necessary to be capable of operating in the manner intended by management. Consequently, references to 'construction' in this Standard should be read as covering activities that are necessary to cultivate the bearer plants before they are in the location and condition necessary to be capable of operating in the manner intended by management.



(6) SUBSEQUENT MEASUREMENT AT BALANCE SHEET DATE

An enterprise should choose,

- ◆ Either Cost model,
- ◆ Or Revaluation model

as its accounting policy (IND AS 8) and should apply that policy to an entire class of PPE.

Any change in Accounting Policy shall have Retrospective effect.

Class of PPE: A class of PPE is a grouping of assets of a similar nature and use in operations of an enterprise.

Examples of separate classes:

- 1) Land
- 2) Land and Buildings
- 3) Machinery
- 4) Ships
- 5) Aircraft
- 6) Motor Vehicles
- 7) Furniture and Fixtures
- 8) Office Equipment
- 9) Bearer plants

Example:

Venus Ltd. is a large manufacturing group. It owns a considerable number of industrial buildings, such as factories and warehouses, and office buildings in several capital cities. The industrial buildings are located in industrial zones whereas the office buildings are in central business districts of the cities. Venus's Ltd. management wants to apply the Ind AS 16 revaluation model to subsequent measurement of the office buildings but continue to apply the historical cost model to the industrial buildings. Is this acceptable under Ind AS 16, Property, Plant and Equipment?

SOLUTION:

Venus's Ltd. management can apply the revaluation model only to the office buildings. The office buildings can be clearly distinguished from the industrial buildings in terms of their function, their nature and their general location. Ind AS 16 permits assets to be revalued on a class-by-class basis. The different characteristics of the buildings enable them to be classified as different PPE classes.

Cost Model

After recognition as an asset, an item of PPE should be carried at:

Cost - Any Accumulated Depreciation - Any Accumulated Impairment losses

Revaluation Model

After recognition as an asset, an item of PPE whose fair value can be measured reliably should be carried at a revalued amount.

Fair value at the date of revaluation

-

Less: Any subsequent accumulated depreciation

(-)

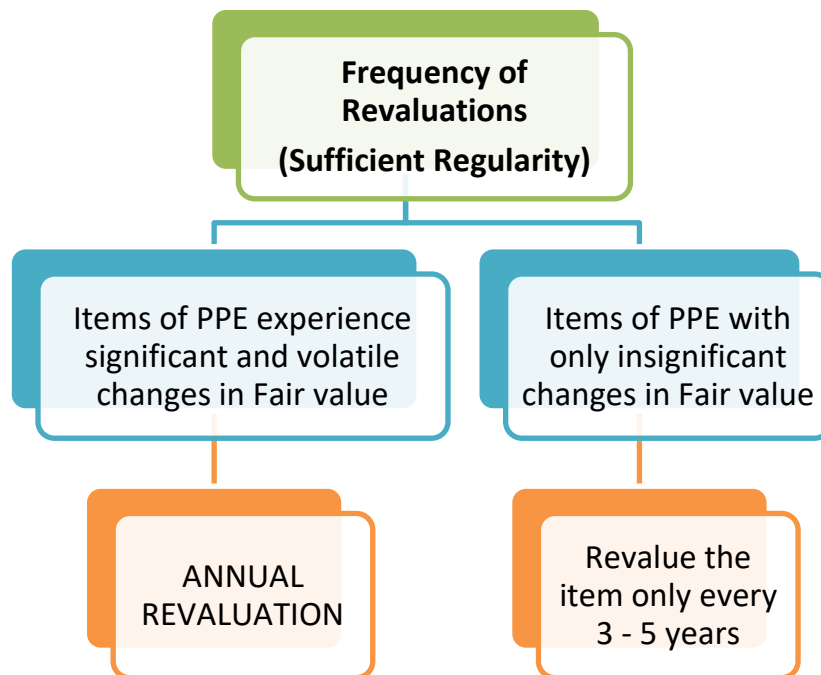


Less: Any subsequent accumulated impairment losses (-)

Carrying value =

Revaluation for entire class of PPE

If an item of PPE is revalued, **the entire class of PPE** to which that asset belongs should be revalued.



(7) ACCOUNTING TREATMENT OF REVALUATIONS

When an item of PPE is revalued, the carrying amount of that asset is adjusted to the revalued amount. At the date of the revaluation, the asset is treated in one of the following ways:

Technique 1:

Accumulated depreciation is eliminated against the gross carrying amount of the asset

Step 1 - Eliminate the Accumulated Depreciation balance from Gross Carrying amount of PPE (Debit Acc. Dep A/c and Credit PPE A/c)

Step 2 - Now Compare the Net Carrying Amount of PPE with Fair Value of PPE and determine the Revaluation Profit/Loss

Step 3 - Increase or Decrease the Net Carrying Amt. of PPE with the Revaluation Profit/Loss by either Debiting or Crediting the PPE.

Technique 2:

Restatement Approach (No elimination of Accumulated Depreciation)

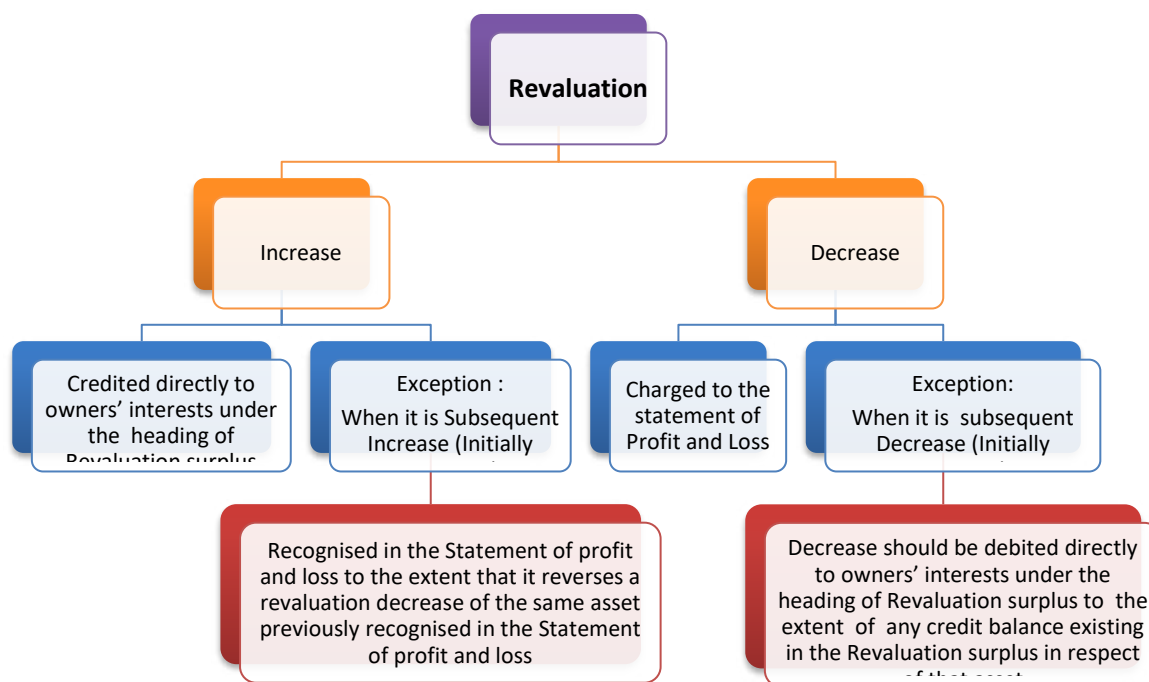
Gross carrying amount and Accumulated Depreciation is adjusted in a manner that is consistent with the revaluation of the carrying amount of the asset.

- **No need to eliminate** Accumulated Depreciation.
- Calculate the Revaluation Gain/Loss and its "**% of Change**" (Gain (loss) / WDV)
- **Increase/Decrease** the Original Cost and Accumulated Depreciation with above % and pass following journal entry:

PPE A/c Dr.
 To Accumulated Depreciation A/c
 To Revaluation Surplus A/c

(Refer Practical Example 4)

(7.1) Revaluation - Increase or Decrease - Treatment



(Refer Practical Example 5)

(7.2) Utilisation of Revaluation Surplus

The revaluation surplus included in owners' interests in respect of an item of PPE maybe transferred to the Revenue Reserves (i.e. Retained Earnings) when the asset is de-recognised.

Case I: Mandatory transfer of Revaluation Reserve to Retained Earnings (GR):

When the asset is:

- ◆ Retired; or
- ◆ Disposed of

Case II: Option to Transfer Revaluation Reserve to Retained Earnings (GR)

- When the asset is still used by an enterprise not yet sold.
- Transfer the amount equal to the excess depreciation due to Upward Revaluation.

Note:

Transfers from Revaluation Surplus to the Revenue Reserves are not made through the Statement of Profit and Loss.

(8) TREATMENT OF DIFFERENT SUBSEQUENT EXPENDITURE ON PPE

1. **Cost of day to day Servicing:** This cost is directly recognised in the Statement of Profit and Loss because it does not increase the earning efficiency of PPE.
2. **Replacement of parts of PPE:** Capitalise in the carrying amount of PPE if the recognition criteria are met. (i.e. Future Economic Benefits + Cost Reliable)

Examples:

- a) Aircraft interiors such as seats and galleys may require replacement several times during the life of the air frame.
- b) Replacing the interior walls of a building, or to make a non-recurring replacement.

3. **Regular Major Inspection or Overhaul:** When each major inspection is performed, its cost is recognised in the carrying amount of the item of PPE as a replacement, if the recognition criteria are satisfied.

Any remaining carrying amount of the cost of the **previous inspection** (as distinct from physical parts) is **derecognized**.

Example:

A shipping company is required by law to bring all ships into dry dock every five years for a major inspection and overhaul. Overhaul expenditure might at first sight seem to be a repair to the ships but it is actually a cost incurred in getting the ship back into a seaworthy condition. As such the costs must be capitalised. A ship which cost ₹ 20 million with a 20 year life must have major overhaul in every five years. The estimated cost of the overhaul at the five-year point is ₹ 5 million.

The depreciation charge for the first five years of the assets life will be as follows:

	Overhaul Component (Million)	Ship (other than overhaul component) Million
Cost	5	15
Years	5	20
Depreciation per year	1	0.75

Total accumulated depreciation for the first five years will be Rs. 8.75, and the carrying amount of the ship at the end of year 5 will be Rs. 11.25 million.

The actual overhaul costs incurred at the end of year 5 are Rs. 6 million. This amount will now be capitalised into the costs of the ship, to give a carrying amount of Rs. 17.25 million.

The depreciation charge for years 6 to 10 will be as follows:

	Overhaul Component (Million)	Ship (other than overhaul component) Million
Cost	6	11.25
Years	5	15
Depreciation per year	1.2	0.75

Annual depreciation for years 6 to 10 will now be Rs.1.95 million. This process will be continued for years 11 to 15 and years 16 to 20. By the end of year 20, the capital cost of ₹ 20 million will have been depreciated plus the actual overhaul costs incurred at years 5, 10 and 15.

(9) DEPRECIATION

Component Method of Depreciation:

Each part of an item of PPE with a cost that is **significant in relation to the total cost** of the item with **significant useful life different from other components** should be depreciated separately.

Example:

It may be appropriate to depreciate separately the airframe and engines of an aircraft, whether owned or subject to a finance lease.

Is Grouping of Components possible?

Yes.

A significant part of an item of PPE may have a useful life and a depreciation method that are the same as the useful life and the depreciation method of another significant part of that same item. Such parts **may be grouped** in determining the depreciation charge.

(a) Accounting Treatment:

Depreciation charge for each period should be recognized in the Statement of Profit and Loss unless it is included in the carrying amount of another asset for example -

- **IND AS 2:** Depreciation of manufacturing plant and equipment is included in the costs of conversion of inventories as per IND AS 2.
- **IND AS 38:** Depreciation of PPE used for development activities may be included in the cost of an intangible asset recognised in accordance with IND AS 38 on Intangible Assets.
- **IND AS 16:** Depreciation of PPE used for construction and development of another self-generated PPE may be included in the cost of self-generated asset in accordance with IND AS 16 on PPE.

(b) Depreciable Amount and Depreciation Period

What is "Depreciable Amount"?

Depreciable amount is:

Cost of an asset (or other amount substituted for cost i.e. revalued amount) - Residual value

The depreciable amount of an asset should be **allocated on a systematic basis over its useful life.**

(c) Review of Residual Value and Useful Life of an Asset

Residual value and the useful life of an asset should be reviewed **at least at each financial year-end** and, if expectations differ from previous estimates, the change(s) should be accounted for as a **change in an accounting estimate** in accordance with IND AS 8 'Accounting Policies, Changes in Accounting Estimates and Errors'.

(d) Commencement of period for charging Depreciation

Depreciation of an asset begins when it is **available for use**, i.e., when it is in the location and condition necessary for it to be capable of operating in the manner intended by the management. **(i.e. Ready to use)**



Depreciation in Case the asset is Not Working/ lying idle (in case of situations like covid):

Depreciation of an asset ceases, at the earlier of the date that the asset is classified as held for sale and the date the asset is de-recognised. Therefore, the asset continues to be depreciated even if it remains idle, unless the asset is fully depreciated.

Apart from the above, it may be noted that as per Ind AS 16, one of the factors in determining useful life of an asset is technical or commercial obsolescence. Therefore, even when the asset is idle, the same should be depreciated due to technical or commercial obsolescence and wear and tear during that period.

(e) Cessation of Depreciation

I. Depreciation ceases to be charged when asset's residual value exceeds its carrying amount; or

II. Depreciation of an asset ceases at the earlier of:

- ◆ The date that the asset is retired from active use and is held for disposal, and
- ◆ The date that the asset is derecognized

Therefore, depreciation does not cease when the asset becomes idle or is retired from active use (but not held for disposal) unless the asset is fully depreciated.

(f) Depreciation on Land and Buildings

Land and buildings are separable assets and are accounted for separately, even when they are acquired together.

A. Land: Land has an unlimited useful life and therefore is not depreciated.

Exceptions: Quarries and sites used for landfill.

Depreciation on Land:

I. If land itself has a limited useful life:

It is depreciated in a manner that reflects the benefits to be derived from it.

II. If the cost of land includes the costs of site dismantlement, removal and restoration:

That portion of the land asset is depreciated over the period of benefits obtained by incurring those costs.

B. Buildings:

Buildings have a limited useful life and therefore are depreciable assets.

An increase in the value of the land on which a building stands does not affect the determination of the depreciable amount of the building.

(g) Depreciation Method

The depreciation method used should reflect the pattern in which the future economic benefits of the asset are expected to be consumed by the enterprise.

The method selected is applied consistently from period to period unless:

- There is a change in the expected pattern of consumption of those future economic benefits; or



- That the method is changed in accordance with the statute to best reflect the way the asset is consumed.

Note: A depreciation method which is based on Revenue generated from the use of an asset, is not appropriate. Revenue generation includes other factors also such as selling activities; changes in sales volumes and prices. The price component of revenue may be affected by inflation, which has no bearing upon the way in which an asset is consumed.

(h) Review of Depreciation method:

The depreciation method applied to an asset should be reviewed at least at each financial year-end and, if there has been a significant change in the expected pattern of consumption of the future economic benefits embodied in the asset, the method should be changed to reflect the changed pattern.

Note:

Such a change should be accounted for as a change in an accounting estimate in accordance with IND AS 8.

(10) RETIREMENTS

According to IND AS 105 - Items of PPE retired from active use and held for disposal should be stated at the lower of:

- ◆ Carrying Amount, and
- ◆ Fair Value less cost of disposal

Note: Any write-down in this regard should be recognised immediately in the Statement of Profit and Loss.

(11) DE-RECOGNITION

The carrying amount of an item of PPE should be de-recognised:

- On disposal
- By sale
- By entering into a finance lease, or
- By donation, or
- When no future economic benefits are expected from its use or disposal

Accounting Treatment:

- Gain or loss arising from de-recognition of an item of PPE should be included in the **Statement of Profit and Loss when the item is derecognized** unless IND AS 116 on Leases, requires otherwise on a sale and leaseback (IND AS 116 on Leases, applies to disposal by a sale and leaseback.)
- **Compensation** from third parties for items of PPE that were Impaired, Lost or Given up shall be included in Profit and Loss when such compensation becomes receivable.
- Gain or loss arising from de-recognition of an item of PPE =

$$\text{Net disposal proceeds (if any)} - \text{Carrying Amount of the item}$$

Note: Gains should **not** be classified as revenue, as defined in IND AS 115. (Rather it can be shown under exceptional items of Statement of P&L)

Exception:

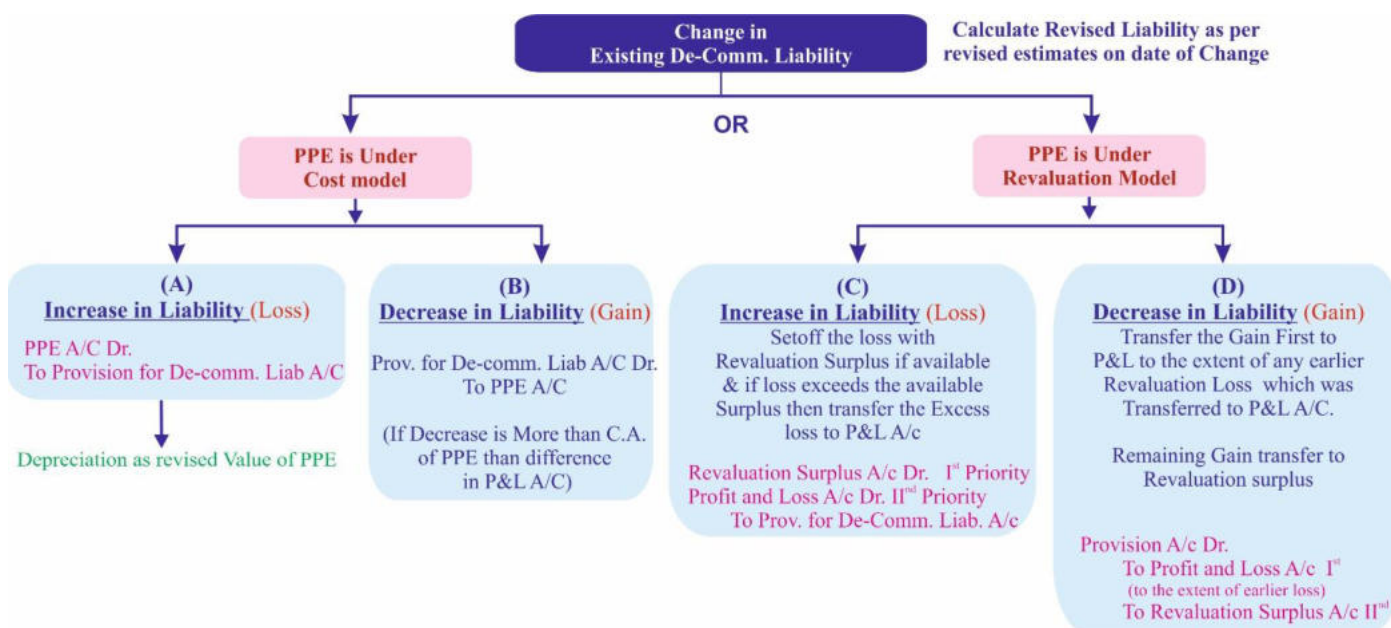
An enterprise that in the course of its ordinary activities, **routinely sells items of PPE** that it had held for rental to others should transfer such assets to inventories at their carrying amount when they cease to be rented and become held for sale.

The proceeds from the sale of such assets **should be recognised in revenue** in accordance with IND AS 115. **(Refer Practical Example 6)**

Example:

Jai Chawla is in the business of Renting cars to his customers. Jai owns 20 luxury Cars. Jai's Policy is to purchase a new car, use it in business of rental and then sell it after every 5 years. Now, Jai will not calculate Gain on sale of Car under INDAS 16, rather the entire sale proceeds shall be treated as Revenue from Operation and Carrying Amount of car after 5 years is treated as Inventory.

(12) CHANGES IN EXISTING DECOMMISSIONING, RESTORATION AND OTHER LIABILITIES



(Refer Practical Example No. 7)

06

IND AS 2 INVENTORIES

**“It Doesn't Matter How Slowly you
go as long as you do not Stop”**

1. DEFINITION OF INVENTORY - IND AS 2

Inventories are **Assets**:

- (a) **Held for sale** in the ordinary course of business (Finished Goods)
- (b) In the **process of Production** for Such Sale (WIP) or
- (c) In the **form of materials or supplies to be consumed** in the production process or in the rendering of services (Raw Material).

2. NON - APPLICABILITY OF IND AS 2

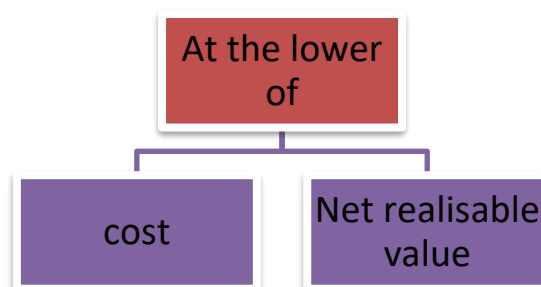
(A) IND AS-2 is not applicable to following cases.

- **Any financial instruments** held as stock in trade which includes shares, debentures, bonds etc. (INDAS 32, 109)
- **Biological Assets** (i.e. living plants and animals) **related to agriculture activity** and agriculture produce at the point of harvest (IND AS 41)

(B) This Standard also does not apply to the measurement of inventories held by:

- Producers of agricultural and forest products, agricultural produce after harvest, and minerals and mineral products, **to the extent that they are measured at Net Realisable value** in accordance with well-established practices in those industries.
- **Commodity broker-traders** who measure their inventories at fair value less costs to sell.

3. HOW TO MEASURE INVENTORY:



4. WHAT IS NET REALISABLE VALUE?

The actual transaction price (i.e. customer order price) **after the balance sheet date** could be the best available evidence to identify NRV of Finished Goods or Stock in Trade.

In Respect of Finished goods:

Normal selling price of the Finished Goods	XXX
Less - Estimated Expenditure to sale such goods	XXX
Net Realisable Value	XXX

In Respect of WIP:

Normal selling price of the Finished Goods	XXX
Less - Estimated Expenditure to sale such goods	XXX
Less - Estimated further Cost to Make Finished Goods	XXX
Net Realisable Value of WIP	XXX

Measurement of Raw Material:

If Finished goods sold at Cost or Above	If Finished goods sold at below Cost
Estimated Realisable value of Raw material and supplies is considered more than cost. Therefore, Raw Material should be measured at Cost .	Estimated Realisable value of Raw material or supplies may be less than Cost. Therefore, Raw Material should be measured at Replacement Cost or Original Cost whichever is Lower .

Note:-

- Estimates of Net Realisable Value also take into consideration **the purpose for which the inventory is held**. For example, the net realizable value of the quantity of inventory held to satisfy firm sales or service contracts is based on the contract price.
- If the sales contract are for less than inventory quantities held, the net realizable value of the **excess quantity is based on general selling prices**.
- If there is a firm contract to sell quantities in excess of inventory quantities that the entity holds or is able to obtain under a firm purchase contract, this may give rise to a **onerous contract**

liability that should be provided for in accordance with INDAS 37 "Provisions, Contingent liabilities, Contingent Assets".

(Also Refer Practical Example 1)

Example:

Computers and laptops on 31/03/20X1 :- 150 units

Normal Selling Price :- Rs.1,20,000/- per unit

On 30/04/20X1, customer order for supply of 100 units @ Rs.95000/-per unit

Calculate the NRV of total 150 units.

Solution:-

Sr. No.	Particulars	Amounts
1	100units X 95,000	9,50,000
2	50units X 1,20,000	60,00,000
	Total NRV	1,55,00,000

5. COST OF INVENTORY

There can be three types of cost are included in the inventory which are as follow.

1. PURCHASE COST:

- Invoice price at which goods are purchased
- Duties and taxes paid
- Transport, Handling and Freight inward
- Any other expenditure directly relating to acquiring goods or services

Above cost should be reduced by following:

- Duties and taxes received or receivable back from the tax authority
- Trade discount
- Rebate
- Duty drawback

Note :-

- Primary packing charges of material is included in cost.
- Secondary packing and publicity charges of material is recorded as Selling expense in Statement of P&L

2. COST OF CONVERSION (Labour + Production Overhead)

- Direct Material, Labour and other direct expense.
- Plus a systematic allocation of fixed and variable production overheads that are incurred in converting materials into finished goods.

Following things should be considered for conversion cost of the inventory.

(a) FIXED PRODUCTION OVERHEAD -

For example - depreciation and maintenance of factory building.

Allocation of fixed expense should be made on the bases of normal capacity

If production levels are abnormally low	Unallocated overheads are recognized as an expense (P&L)
If production levels are abnormally high	Amount of Fixed O/H allocated to each unit is decreased so that inventory should not be measured above cost.

(Also Refer Practical Example 2 for Fixed OH Cost)

(b) VARIABLE OVERHEAD -

Variable production overheads are allocated to each unit of production on the basis of the actual use of the production facilities.

3. OTHER COST:

It includes any other expenditure incurred to bring inventory in the present location and condition. For eg. Transportation cost from factory to warehouse for storage of goods.

But rent for such warehouse is not other cost & not a part of cost measurement. **Exclusion in Cost of Inventory** - But it should not include abnormal wastage relating to material and labour, storage cost, administrative expenses & selling and distribution expenses, finance element in case of deferred settlement.

Example:

The production of whiskey involves the distilling of aged whiskey in a cask prior to bottling should be capitalized, as aging is integral to making the finished product saleable.

IMPORTANT ISSUE IN RELATION TO COST OF INVENTORY:

Issue 1:

Whether borrowing costs should become part of cost of Inventory?

Answer:

The extent to which borrowing cost is included in the cost of inventories is determined on the basis of the requirement of Ind AS 23 Borrowing Costs.

It means if borrowing costs are directly attributable to Acquisition, Construction or Production of Inventory being Qualifying Asset (i.e. takes substantial period of time to get ready for sale) then borrowing costs shall become part of Cost of Such Inventory.

Issue 2:

If payment for Cost of Inventory is to be made beyond Credit Terms then what should be the Cost of Inventory?

Answer:

An entity may acquire inventories on deferred settlement terms. When the arrangement effectively contains a financing element, that element, for example a difference between the purchase prices for normal credit terms and the amount paid, is recognised as interest expense over the period of the financing.

Issue 3:

What should be the Treatment of Spare Parts, Standby Equipment and Servicing Equipments purchased and used in PPE?

Answer:

Case I: If they meet the definition of PPE as per INDAS 16: Recognised as PPE as per INDAS 16.

PPE a/c Dr.

To Bank a/c

Case II: If they do not meet the definition of PPE as per INDAS 16: Such items are classified as Inventory as per AS 2.

Purchase a/c Dr.

To Bank a/c

(At balance sheet date, if they are not yet fully consumed then shall be included under Inventory and Measured accordingly as per INDAS 2)

Issue 4:

What should be the treatment of Cost of dismantling/removing/restoring site on which the item (PPE) is located and such item (PPE) is used for Manufacturing of goods and such restoring is required due to manufacturing of goods?

Answer:

Such Cost should be Added to the Cost of Inventory only and not to the Cost of PPE because restoring the site is required due to Manufacturing of Goods.

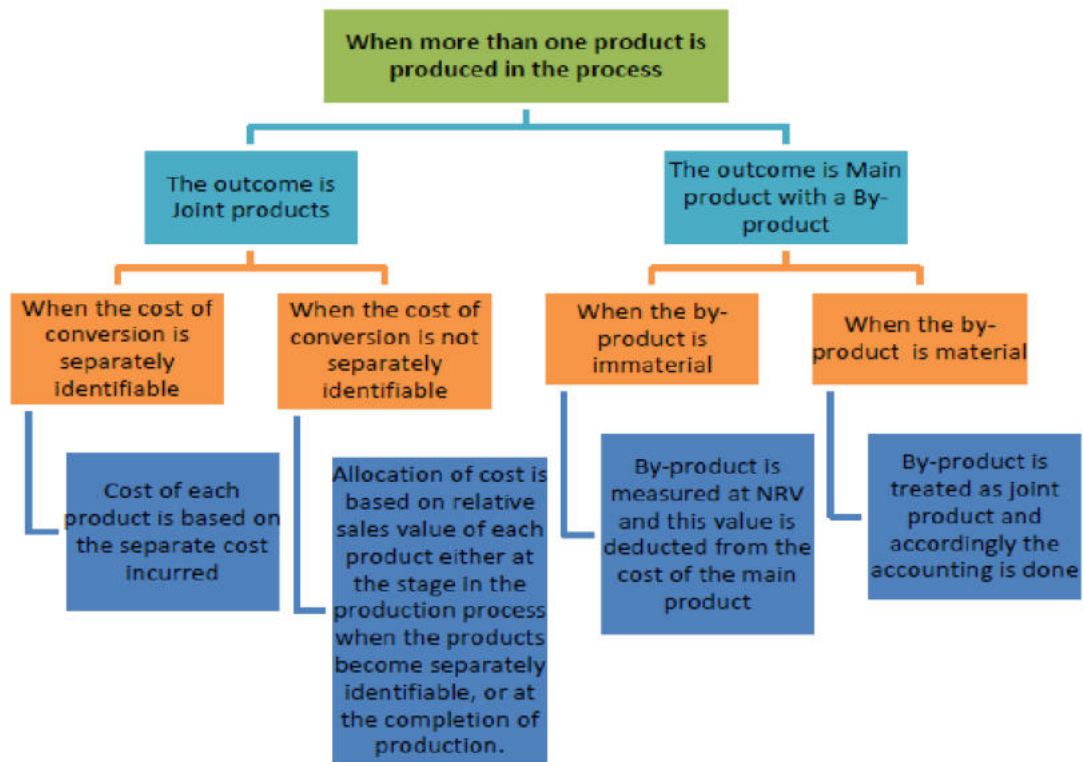
However, if dismantling is required due to Installation of item of PPE then such Cost of dismantling shall be added to the Cost of PPE.

Issue 5 - Transfers of rental assets to inventory

An entity may, in the course of its ordinary activities, **routinely sell items** that had previously been held for rental and classified as property, plant and equipment.

For example, Entity A is car rental companies that acquires cars with the intention of giving them on rent for a limited period and then sell them. Ind AS 16 requires that when such items become held for sale rather than rental they be transferred to inventory at their carrying value. Revenue from the subsequent sale is then recognised gross rather than net.

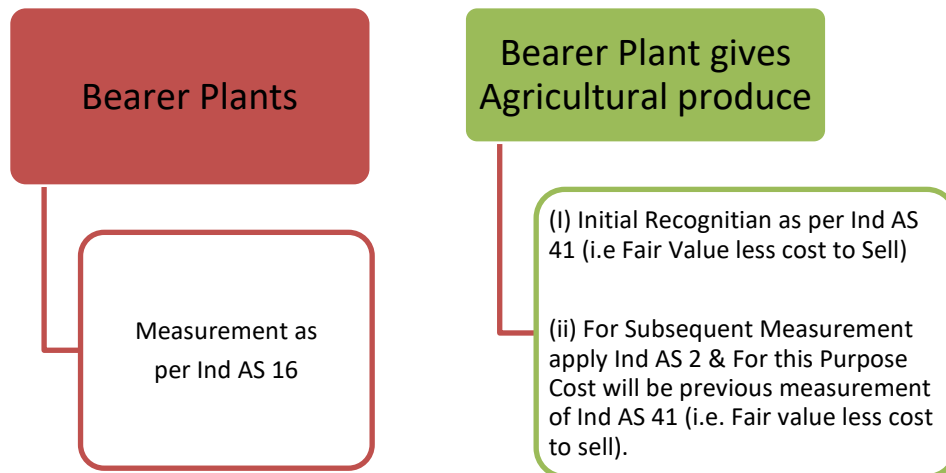
6. ALLOCATION OF COST TO JOINT PRODUCTS AND BY-PRODUCTS



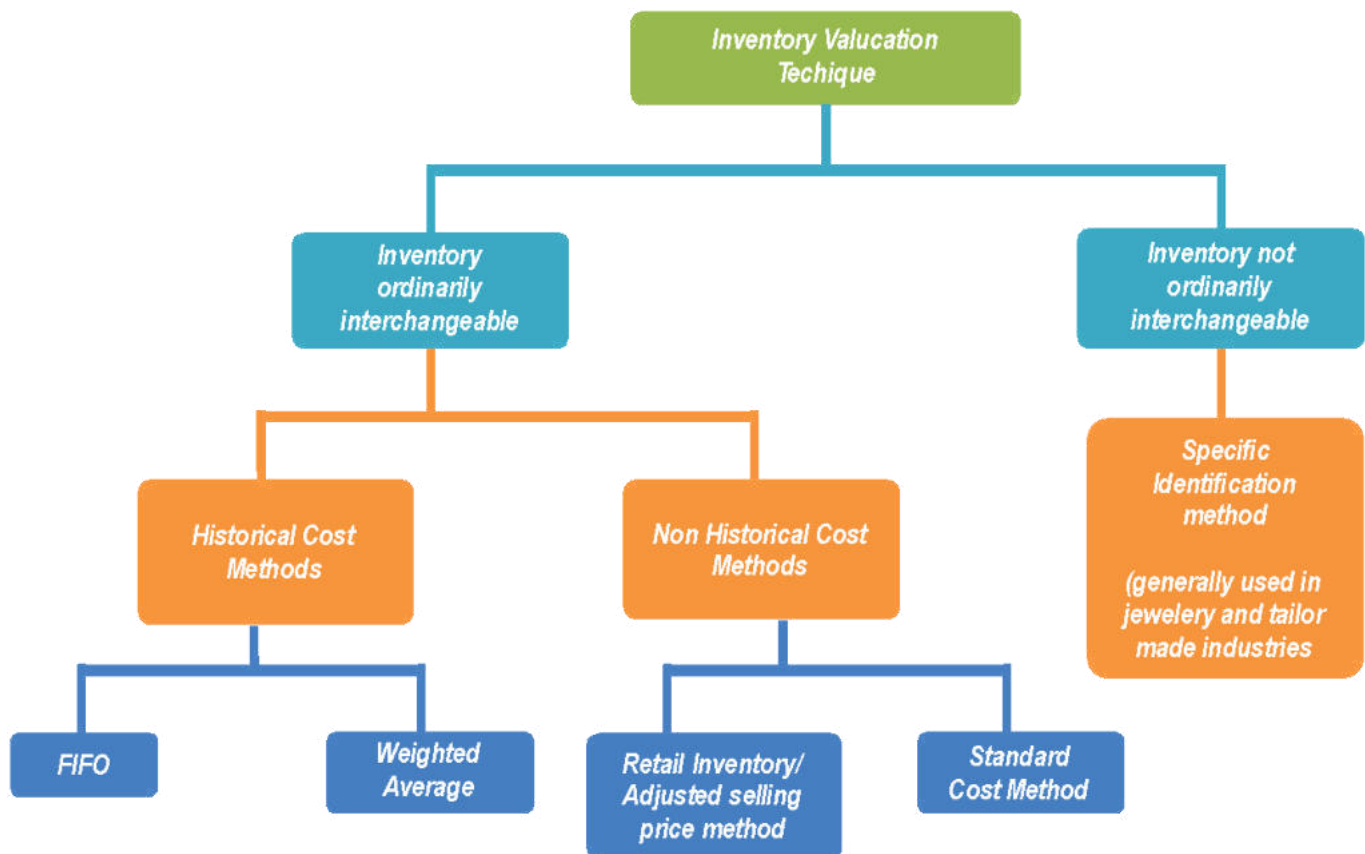
7. COST OF AGRICULTURAL PRODUCE HARVESTED FROM BIOLOGICAL ASSETS

In accordance with Ind AS 41, Agriculture, inventories comprising agricultural produce that an entity has harvested from its biological assets are measured on initial recognition at their fair value less costs to sell at the point of harvest.

This is the cost of the inventories at that date for application of this Standard.



8. TECHNIQUES FOR THE MEASUREMENT OF COST



- (i) **Standard Cost Method:** Cost is based on normal levels of materials and supplies, labour efficiency and capacity utilization. They are regularly reviewed and revised where necessary.
- (ii) **Retail Method:** Cost is determined by reducing the sales value of the inventory by the appropriate percentage gross margin. The percentage used takes into consideration inventory that has been marked down to below its original selling price. This method is often used in the retail industry for measuring inventories of rapidly changing items that have similar margins.

Note: Ind AS 2 Inventories *does not permit using LIFO (last-in-first-out)*.

Imp Issue: Whether an entity can use different cost formulae for the inventories held at different geographical locations?

Answer:

Ind AS 2 states that an entity shall use the same cost formula for all inventories having a similar nature and use to the entity. For inventories with a different nature or use, different cost formulas may be justified.

Also, difference in geographical location of inventories does not justify the use of a different cost formula, if the inventories are of similar nature and use to the entity.

9. RECOGNITION OF INVENTORY AS AN EXPENSE

The amount of inventories recognised as an expense in the period will generally be:

- a) Carrying Amount of the inventories sold in the period in which related revenue is recognized (i.e. COGS); and
- b) The amount of any write-down of inventories to net realisable value and all losses of inventories shall be recognised as an expense in the period the write-down or loss occurs; reduced by
- c) The amount of any Reversal in the period of any write-down of inventories, arising from an increase in net realisable value.
- d) Some inventories may be allocated to other asset accounts, for example, inventory used as a component of self-constructed property, plant or equipment. Inventories allocated to another asset in this way are recognised as an expense during the useful life of that asset through charging of depreciation on that asset.

Example:

A whisky distiller would not write down an inventory of grain because of a fall in the grain price, so long as it expects to sell the whisky at a price which is sufficient to recover cost.

Example:

XYZ is an electronics dealer mainly in LCD television sets. Due to technology change, the LCDs televisions are no longer in demand and the new LED version of television sets are now in demand. XYZ has an inventory of LCD television sets worth Rs 5,00,000. However, due to low demand, there has been significant drop in the sale prices of LCD television sets. If XYZ were to dispose off the inventory in the market, it would fetch Rs 3,00,000 at current market prices.

In such a situation, assuming the costs of disposals to be insignificant, the NRV will be taken to be Rs 3,00,000. Hence, the carrying amount of the LCD television sets should be reduced to its NRV.

Example:

An item of inventory costing ₹ 20,000 as covered under Ind AS 2 is consumed in the construction of self-constructed property to be accounted as Property, plant and equipment under Ind AS 16. The cost of such property, plant and equipment other than inventories is ₹ 80,000. Such Inventory needs to be capitalized in the cost of Property, plant and equipment. The useful life of the property is 5 years. The depreciation on such property charged to profit and loss account is ₹ 20,000 per annum (i.e. 1,00,000/5)

10. DIFFERENCE BETWEEN NRV AND FAIR VALUE

- NRV is the estimated selling price in the ordinary course of business less the estimated costs of completion and the estimated costs necessary to make the sale.
- Fair Value, is the price that would be received to sell assets or paid to transfer a liability in an orderly transaction between market participants at the measurement date.
- The former is an entity-specific measurement; the latter is a market-based measurement. NRV for inventories may not be equal to fair value less costs to sell.

Example:

An entity holds inventories of 10,000 units and it could sell the same in the market at Rs. 10 each. The entity has an order in hand to sell the inventories at Rs. 11. The incremental selling cost per unit is Rs. 0.50 per unit. In this situation, fair value is Rs. 10 each, but net realizable value is Rs.10.5 each.

Example:

Manufacture of LCD TVs can sell each unit in the market for Rs 1,00,000 (after incurring selling expense). The manufacture has a confirmed order on hand to sell the LCD TVs for Rs 1,25,000 each. In this situation, fair value is Rs 1,00,000, but NRV is Rs 1,25,000.

11. TRADE DISCOUNT & CASH DISCOUNT

- Trade discount should be deducted to determine the Cost of Inventory.
- Cash discounts are incurred to recover the sale proceeds immediately or before the end of the specified period or credit period allowed to the customer. Therefore, the same should not be considered while determining NRV.

07

IND AS 38 INTANGIBLE ASSETS

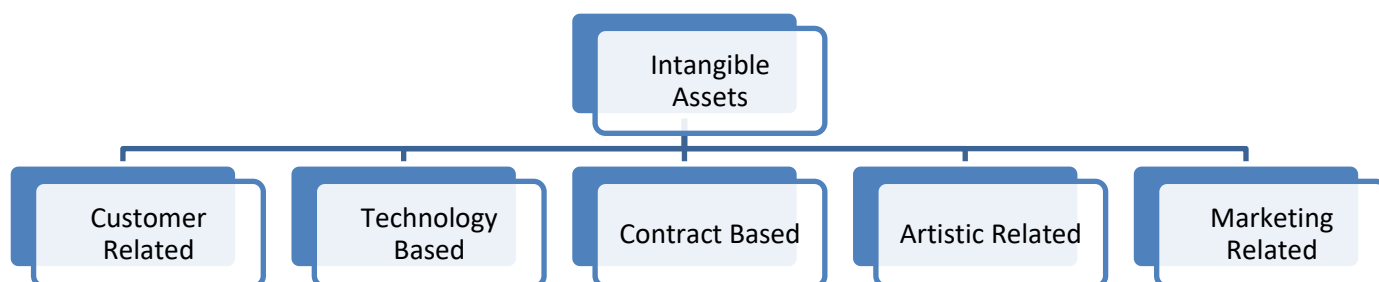
1. MEANING of an ASSET

- Any Resource which is **Controlled** by the enterprise as a result of **past events** and,
- From which **Future Economic Benefits** are expected to flow to the enterprise.

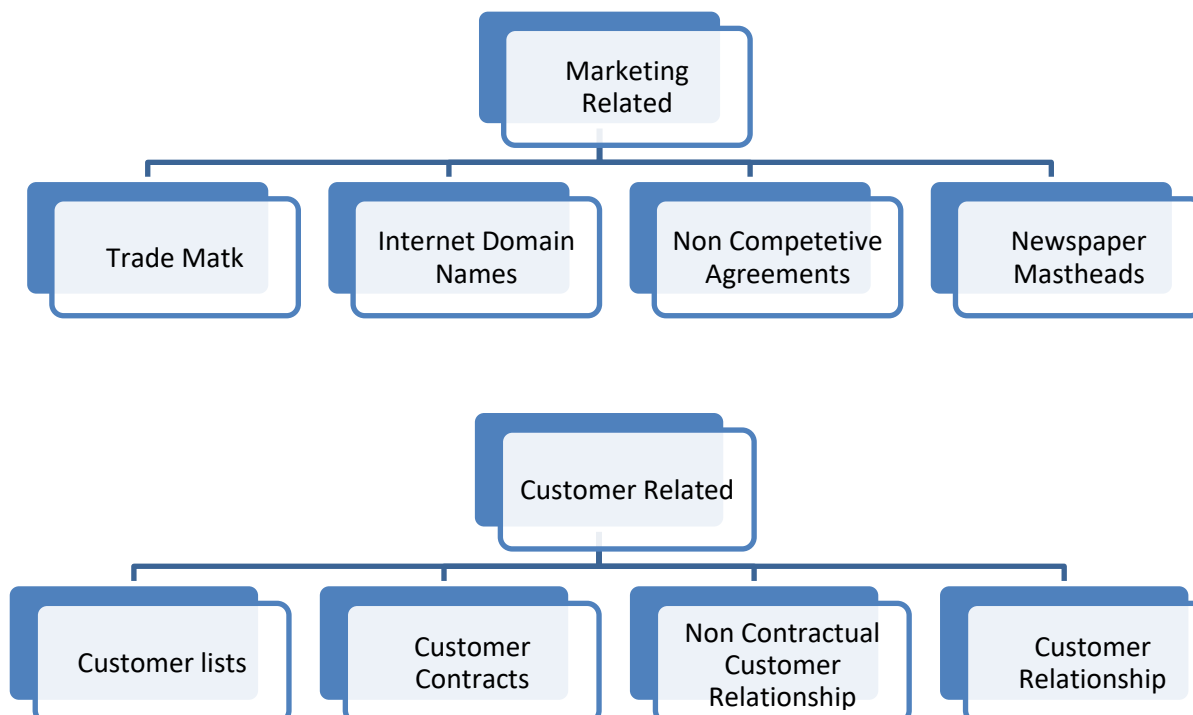
2. MEANING OF INTANGIBLE ASSETS

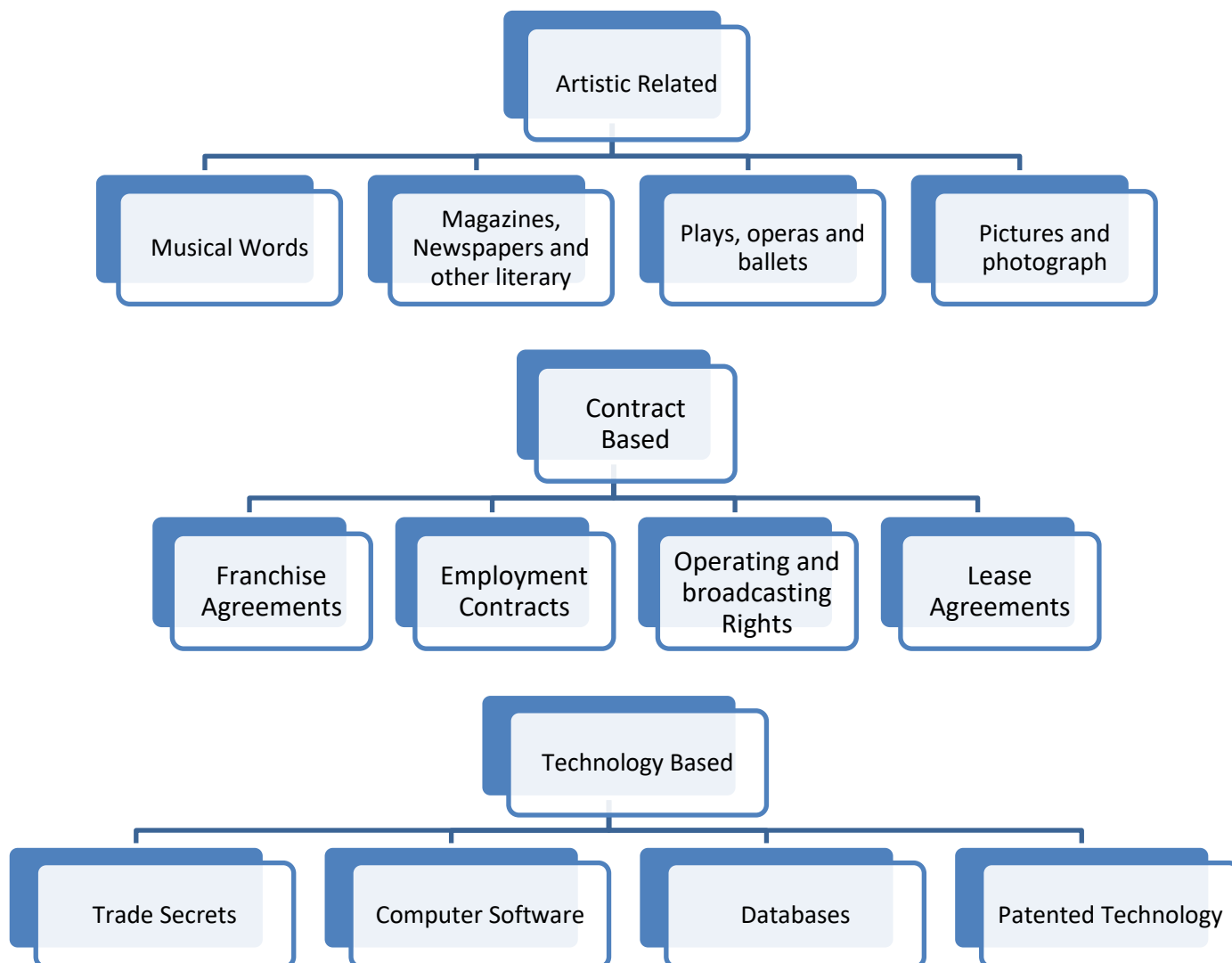
An Intangible asset is:

- An identifiable
- Non - Monetary item
- Without physical substance



Let's run through some examples of each broad category listed above:





Note: If an item within the scope of this Standard **does not meet the definition** of an intangible asset, expenditure to acquire it or generate it internally is recognised **as an expense** when it is incurred. However, if the item is acquired in a business combination, it forms part of the goodwill recognised at the acquisition date.

2.1 IDENTIFIABILITY

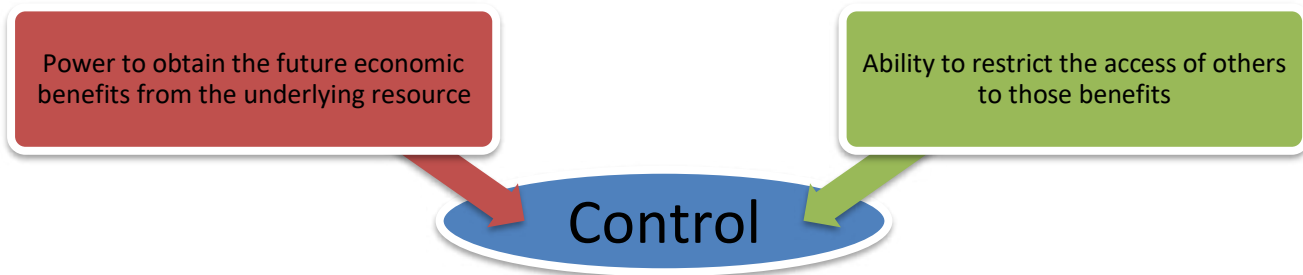
An asset is identifiable if it either:

- is **separable**, ie is capable of being separated or divided from the entity and **sold, transferred, licensed, rented or exchanged, either individually or together with a related contract**, identifiable asset or liability, regardless of whether the entity intends to do so; or
- **arises from contractual or other legal rights**, regardless of whether those rights are transferable or separable from the entity or from other rights and obligations.

Author's Note:

Goodwill is not identifiable if it is internally generated. Therefore, this is not an intangible asset within the scope of IND AS 38

2.2 CONTROL



EXAMPLES ON CONTROL

Example:

Specific management or technical talent is unlikely to meet the definition of an intangible asset, unless it is protected by legal rights to use it and to obtain the future economic benefits expected from it, and it also meets the other parts of the definition.

Example:

An entity may have a portfolio of customers or a market share and expect that, because of its efforts in building customer relationships and loyalty, the customers will continue to trade with the entity. However, in the absence of legal rights to protectors other ways to control, the relationships with customers or the loyalty of the intangible assets.

2.3 FUTURE ECONOMIC BENEFITS

The future economic benefits flowing from an intangible asset may include:

- (a) **Revenue** from the sale of products or services;
- (b) **Cost savings**; or

For clarification, following are not Intangible Assets as per IND AS - 38, hence they should be written off in P&L immediately:

- (a) Preliminary expenses (non - identifiable)
- (b) Pre-Operating expenses (non - identifiable)
- (c) Staff Training
- (d) Heavy Advertisement expenses

3. RECOGNITION OF INTANGIBLE ASSETS

If the following conditions are satisfied then, an intangible asset should be recognized/ recorded in the books of accounts, otherwise treated as an expense:

- It is **probable that future economic benefits** from the intangible asset **will flow to the enterprise**; and
- The **COST** of intangible can be measured reliably.

Author's Note:

Internally generated brands, mastheads, publishing titles, customer lists (if not acquired) and items similar in substance are not recognised as intangible assets.

4. MEASUREMENT OF COST AT INITIAL RECOGNITION

INITIAL MEASUREMENT

Intangible Assets should be recognized only at **COST**.

Case - 1

If Separately Acquired - Cost will be Purchase price including non-refundable duties and taxes and any other directly attributable cost (DAC) of preparing the asset for its intended use.

- Cost of Employee Benefits,
- Professional & Legal Fees,
- Cost of Testing

Cost Excludes: Cost of introducing a new product or brand or service including advertising and promotional activities, Cost of conducting business in a new location or with a new class of customers, Administration and General overhead costs.

(Refer Practical Example 1)

Case - 2

If payment is deferred beyond normal credit terms:

Cost of Intangible Asset is the **CASH PRICE EQUIVALENT** at the recognition date.

Remaining Amount is **Interest** which is Total payment - Cash price equivalent.

Case - 3

Business Combination:

In accordance with IND AS 103, Business Combinations, if an intangible asset is acquired in a business combination, the cost of that intangible asset is **its fair value** at the acquisition date.

An acquirer recognises at the acquisition date, **separately from goodwill**, an intangible asset of the acquiree, irrespective of whether the asset had been recognised by the acquiree before the business combination.

This means that the acquirer recognises as an asset separately from goodwill **an in-process research and development project of the acquiree** if the project meets the definition of an intangible asset.

(Refer Practical Example 2)

Case - 4

Exchange of Assets:

Intangible Assets acquired in Exchange for a Non-monetary Asset or Assets or a combination of Monetary and Non-monetary Assets:

Cost of Intangible Asset is measured at fair value of Asset Given (1st Priority) or Asset Received (2nd Priority) unless:

- (i) Exchange transaction lacks commercial substance; Or
- (ii) Fair value of neither the asset(s) received nor the asset(s) given up is reliably measurable.

If the PPE acquired is not measured at Fair Value, its cost is measured at the carrying amount of the asset given up.

Case - 5

Acquisition by way of Govt. Grants -

In accordance with Ind AS 20, Accounting for Government Grants and Disclosure of Government Assistance, an entity should recognise both the intangible asset and the grant initially at Fair Value (or) Nominal Value

Example:

Government transfers or allocates to an entity intangible assets such as airport landing rights, licences to operate radio or television stations, import licences or quotas or rights to access other restricted resources.

Case - 6

Internally Generated Goodwill - Cost cannot be measured reliably hence, not recognized.

Case - 7

Internally generated Intangible assets - like Brands, Customer Lists; Good and Trained employees should not be recognized as intangible assets. Publishing Titles such as "India Today", "Champak" cannot be recorded as IA. (Cost can-not be measured reliably).

5. MEASUREMENT OF EXPENDITURE ON RESEARCH & DEVELOPMENT

(a) Research is original and planned investigation undertaken with the prospect of gaining new scientific or technical knowledge and understanding i.e. Gaining of scientific or technical knowledge.

Cost of Research activity should not be capitalized as an intangible asset, it should be treated as expense and transfer to P&L a/c as par IND AS 38.

Here Entity cannot demonstrate that an intangible asset exists that will generate probable future economic benefits. Therefore, this expenditure is recognised as an expense when it is incurred.

Examples of research activities are:

- a) Activities aimed at obtaining new knowledge;
- b) The search for, evaluation and final selection of, applications of research findings or other knowledge;

- c) The search for alternatives for materials, devices, products, processes, systems or services; and
- d) The formulation, design, evaluation and final selection of possible alternatives for new or improved materials, devices, products, processes, systems or services.

Author's Note:

In process research project of Acquiree company can be recognised as an Intangible Asset under Business Combination (IND AS 103)

(b) Development: It is the activity which converts the result of the research to a marketable product (Gained knowledge is applied).

An intangible asset arising from development (or from the development phase of an internal project) should **be recognised if, and only if, an** entity can demonstrate all of the following:

1. **Technical feasibility of completion** of Intangible asset to make it available for use or sale
2. **Intention to complete** the intangible asset and use or sell it
3. **Ability** to use or sell the intangible asset.
4. **How the intangible asset will generate probable future economic benefits.** Among other things, **the entity can demonstrate the existence of a market** for the output of the intangible asset or the intangible asset itself or, if it is to be used internally, the usefulness of the intangible asset.
5. **Adequate resources** (like technical, financial or others) to complete the development.
6. Ability to measure **reliably the expenditure** attributable to the intangible asset during its development.
7. **Cost of Development Phase or Internally Generated Intangible Assets comprises** all directly attributable costs necessary to create, produce, and prepare the asset to be capable of operating in the manner intended by management.

Examples of directly attributable costs are:

- Cost of materials and services used or consumed in generating the intangible assets.
- Costs of employee benefits arising from the generation of the intangible assets
- Fees to register a legal rights

6. SUBSEQUENT EXPENDITURE

Subsequent Expenditure on already recognized Intangible Asset should be **capitalized** if the following **two conditions** are fulfilled:

1. Subsequent Expense **increases the future economic benefits** of Intangible Assets.
2. Such expense can be **measured reliably**.

If the above two conditions are not fulfilled than the subsequent expense should be **transferred to P&L A/c**.

7. MEASUREMENT AFTER INITIAL RECOGNITION

(on Balance Sheet)

An enterprise should choose

- ◆ Either COST model,
- ◆ Or REVALUATION model

COST MODEL

After recognition as an asset, an item of PPE should be carried at:

Cost - Any Accumulated Amortisation - Any Accumulated Impairment losses =

Carrying value

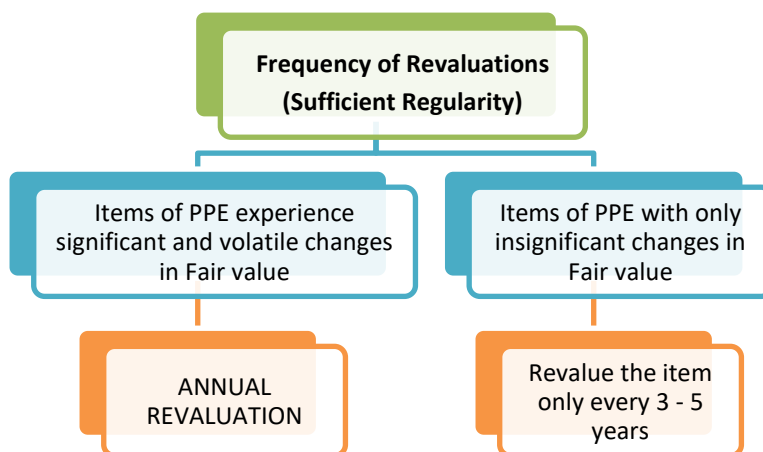
REVALUATION MODEL

After recognition as an asset, an item of PPE whose fair value can be measured reliably should be carried at a revalued amount.

Fair value at the date of revaluation	-
Less: Any subsequent accumulated amortisation	(-)
Less: Any subsequent accumulated impairment losses	(-)
Carrying value	=

Revaluation for entire class of IA

If an item of Intangible is revalued, the entire class of IA to which that asset belongs should be revalued unless there is no active market for those Assets.



8. ACCOUNTING TREATMENT OF REVALUATIONS

When IA is revalued, the carrying amount of that asset is adjusted to the revalued amount. At the date of the revaluation, the asset is treated in one of the following ways:

Technique 1:

Accumulated Amortisation is eliminated against the gross carrying amount of the asset

Step 1 - Eliminate the Accumulated Amortisation balance from Gross Carrying amount of PPE (Debit Acc. Amortisation A/c and Credit Intag. Asset A/c)

Step 2 - Now Compare the Net Carrying Amount of Intangible Asset with Fair Value of Intangible Asset and determine the Revaluation Profit/Loss

Step 3 - Increase or Decrease the Net Carrying Amt. of Intangible Asset with the Revaluation Profit/Loss by either Debiting or Crediting the Intangible Asset.

Technique 2:

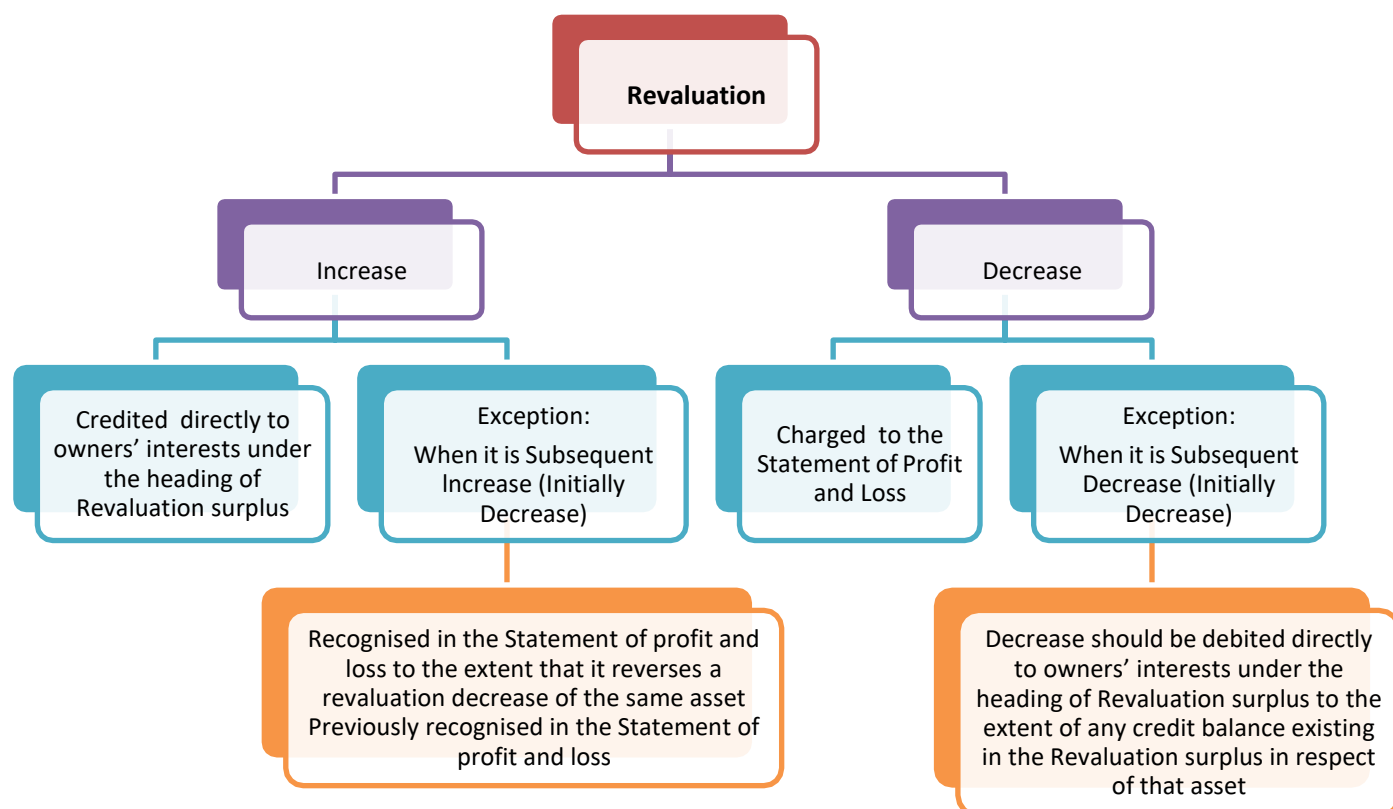
Restatement Approach (No elimination of Accumulated Amortisation)

Gross carrying amount and Accumulated Amortisation is adjusted in a manner that is consistent with the revaluation of the carrying amount of the asset.

- No need to eliminate Accumulated Amortisation.
- Calculate the Revaluation Gain/Loss and its "% of Change" (Gain (loss) / WDV)
- Increase/Decrease the Original Cost and Accumulated Amortisation with above % and pass following journal entry:

Intangible Asset A/c Dr.
 To Accumulated Amortisation A/c
 To Revaluation Surplus A/c

Revaluation - Increase or Decrease - Treatment



9. USEFUL LIFE OF INTANGIBLE ASSETS

The accounting for an intangible asset is based on its useful life. An intangible asset with a finite useful life is amortised, and **an intangible asset with an indefinite useful life** is not amortised and tested for impairment. **(Also Refer Practical Example 3)**

EXAMPLE OF AN INTANGIBLE ASSET WITH AN INDEFINITE USEFUL LIFE

Example:

The trademark has a remaining legal life of five years but is renewable every 10 years at little cost. The acquiring entity intends to renew the trademark continuously and evidence supports its ability to do so. An analysis of (1) product life cycle studies, (2) market, competitive and environmental trends, and (3) brand extension opportunities provides evidence that the trademarked product will generate net cash inflows for the acquiring entity for an indefinite period. The trademark would be treated as having an indefinite useful life because it is expected to contribute to net cash inflows indefinitely.

When the entity shall treat an Intangible Asset as Indefinite Useful Life:

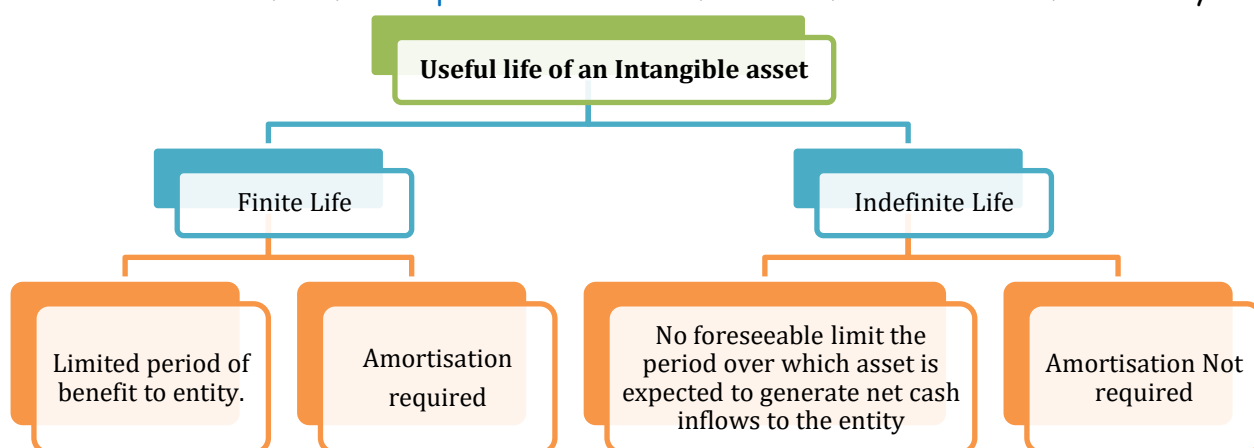
When there is **no foreseeable limit** to the period over which the asset is expected to generate net cash inflows for the entity.

Note: In accordance with Ind AS 36, an entity is required to test an intangible asset with **an indefinite useful life** for impairment by comparing its recoverable amount with its carrying amount

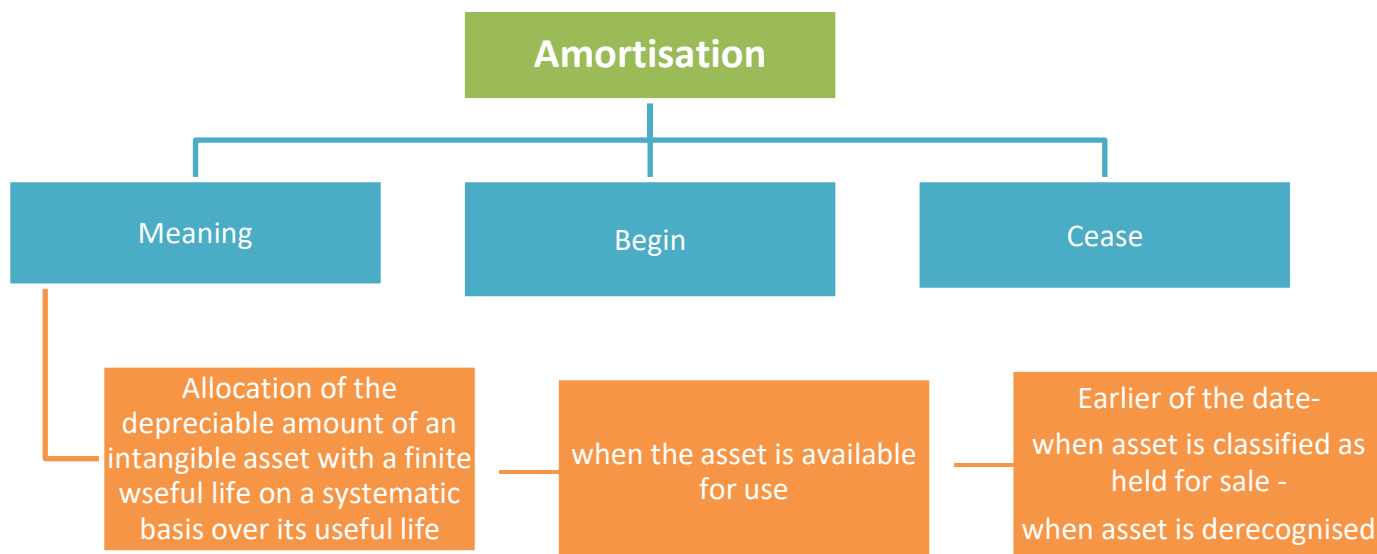
- Annually; and
- Whenever there is an indication that the intangible asset may be impaired.

Factors for consideration in determining useful life

- Expected **usage**.
- Technological, Technical, Commercial and other **obsolescence**.
- Typical **Product life cycle** for the Asset
- Industrial Stability** and Change in Market demand.
- Period of control over the asset** and legal or similar limits on the use of assets.
- Whether the useful life is **dependent** on the useful lives of other assets of the entity.



10. AMORTIZATION PERIOD & AMORTIZATION METHOD



AMORTIZATION METHOD:

- The amortization method used should reflect the pattern in which the asset's economic benefits are consumed by the enterprise.
- If that pattern cannot be determined reliably the Straight Line Method (SLM) should be used.

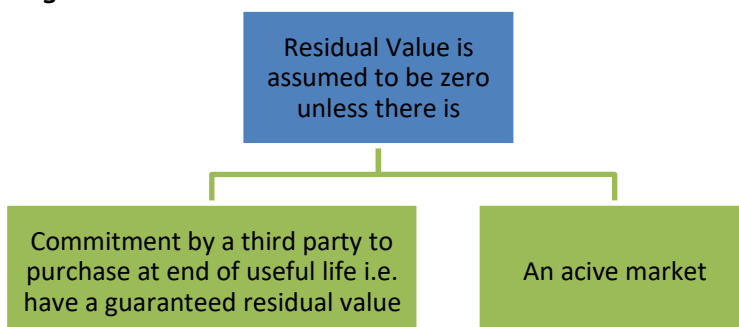
Rebuttable Presumption: A depreciation method which is based on Revenue generated from the use of an asset, is not appropriate. Revenue generation includes other factors also such as selling activities; changes in sales volumes and prices. The price component of revenue may be affected by inflation, which has no bearing upon the way in which an asset is consumed.

REVIEW OF AMORTIZATION PERIOD AND METHOD:

- The amortization period and method should be reviewed at least at each financial year end.
- If the expected useful life or expected pattern of Economic benefits are significantly different from the previous estimates, the amortization period should be changed accordingly.

11. RESIDUAL VALUE

The residual value of intangibles should be assumed to be Zero unless:



12. IMPAIRMENT OF INTANGIBLE ASSETS

- Intangible Asset should be impaired as per Ind AS 36
- For an intangible asset with **indefinite useful lives**, an **impairment review** is required at **least annually**.

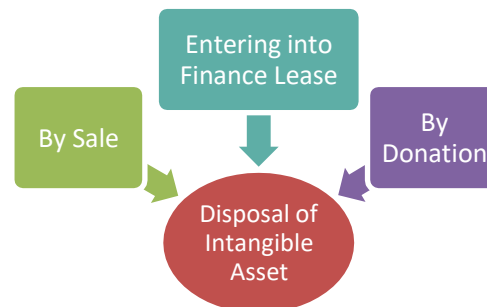
13. RETIREMENT AND DISPOSAL OF INTANGIBLE ASSETS:

An intangible asset should be derecognized (eliminated from the Balance sheet) if:

- It is disposed; or
- No future economic benefits are expected from its use.

Gain/Loss arising on retirement or disposal of intangibles should be recognized as income or expense in P&L A/c.

The disposal of an intangible asset may occur in a variety of ways (e.g. by sale, by entering into a finance lease, or by donation).



SOME IMPORTANT POINTS

1. **Acquired Customer list** may be recognized as Intangible Asset if entity expects to derive benefit from the information on the list **for at least one year**.
2. The product protected by the patented technology is expected to be a source of net cash inflows for at least 15 years. The entity has a **commitment from a third party to purchase** that patent in five years for 60 per cent of the fair value of the patent and the entity intends to sell the patent in five years.
The patent would be **amortised over its five-year useful life** to the entity, with a residual value equal to the present value of 60 per cent of the patent's fair value at the date it was acquired.
3. Intangible Assets should be amortised based on the **useful life instead of the legal life** (if legal life is different).
4. **Assets that incorporate both Tangible & Intangible elements should be treated as under:**
The entity uses judgement to assess which element is more significant i.e. **"Which one is more dominating?"**

For example, computer software for a computer-controlled machine tool that cannot operate without that specific software is an integral part of the related hardware and it is treated as property, plant and equipment. The same applies to the operating system of a computer. When the software is not an integral part of the related hardware, computer software is treated as an intangible asset.

14. Appendix A: Intangible Assets - Web Site Costs

Accounting principles:

The nature of each activity for which expenditure is incurred (eg training employees and maintaining the web site) and the web site's stage of development or post-development shall be evaluated to determine the appropriate accounting treatment:

Expenditure - Not to be Treated as Intangible Asset	Expenditure - To be treated as Intangible Asset
<p>Planning Stage - It is similar to research phase.</p> <p>Content development Expenditure - if it is developed to advertise and promote entity's own product.</p> <p>Operating Expenses on website - these are incurred once website is complete, they are recurring in nature.</p>	<p>Expenditure on Application and Infrastructure, graphical design and content development - if content development is not for promotion.</p>

Useful life

The best estimate of a web site's useful life shall be short.

Student Notes:-



Student Notes:-



08

IND AS 40 INVESTMENT PROPERTY

Walk a Path that will make you Better and make you Proud!

Why there is need to develop separate standard when we already have IND AS 16 PPE?

Investment property is held to earn rentals or for capital appreciation or both. Therefore, an investment property generates cash flows largely independently of the other assets held by an entity. This distinguishes investment property from owner-occupied property.

1. MEANING OF INVESTMENT PROPERTY

The investment property is a **LAND** or a **BUILDING** (or a part of it), or both, held by:

- (a) Owner; or
- (b) Lessee as a right of use asset

for the following specific purposes:

- To earn **Rentals**;
- For **Capital Appreciation**; or
- **Both**

Rather than for:

- a) use in the production or supply of goods or services or for administrative purposes; or
- b) sale in the ordinary course of business.

Author's Note:

Rental should not be the main revenue generating source of activity from that Land & Building.

Understand the above definition in a simple manner:

Here, the strong impact is on purpose. If you hold a building or a land for any of the following purposes, then it cannot be classified as investment property:

- For production or supply of goods or services (i.e. Business Purpose)
- For administrative purposes (i.e. Business Purpose), or
- For sale in ordinary course of business (i.e. Inventory), or
- Property leased to another entity under a Finance Lease.

Note:

- 1) **Owner-occupied property** is property held (by the owner or by the lessee as a right-of-use asset) for use in the production or supply of goods or services or for administrative purposes.
- 2) This standard also deals with the measurement in the lessee's financial statements of investment property interests held as **Right of Use Asset** (as per IND AS 116) and

- 3) The standard applied to lessor's financial statements of investment property provided to a lessee under an **operating lease**.

2. EXAMPLES OF INVESTMENT PROPERTY

- Land held as an investment for **long-term capital appreciation** rather than short term sale in the ordinary course of business.
- Land held **for future undetermined use** (i.e. you don't know yet what you'll use it for. Whether it will be used as owner occupied property or for short-term sale in the ordinary course of business, it is not yet decided.).
- However, if you buy land and you intend to build some production hall for your own purposes sometime in the future, then this land is **NOT** an investment property.
- A building owned by the entity (or held by the entity as right of use asset) and leased out under one or more operating leases. This includes a building that is still vacant, but you plan to lease it out.
- Any property that you actually construct or develop for future use as investment property.

Be careful here again, because when you construct a building for some third party, this is **NOT** an investment property, but you should apply - **IND AS 115 - Revenue from Contracts with Customers**.

Land held as Short Term Investment and Planning to Sale in Near Future within 12 Months, then **IND AS 105** will be applicable and not **IND AS 40**

Jai Sir has taken Building on Lease for 99 years from Govt. Authorities

Apply Ind AS 116 First, Jai Sir shall record ROU Asset.

Now, if Same Building is being used in Jai's Business -> Ind AS 16 will be applied on ROU Asset

Now, if Building is not being used in Jai's Business -> Jai has leased it to other Party on:-

Finance Lease

ROU Asset will be de-recognised

No Question of Applicability of Ind AS 40 & 16

Operating Lease

Ind AS 40 will be applicable on ROU Asset

**Jai sir took a Building on Lease. Building is not to be Used in Jai Sir Business. Jai Sir has Sub-let the same Building under operating Lease (Sub-letting is not Business Activity of Jai Sir)
Which Ind AS Jai Sir should apply?**

Jai Sir First will apply Ind AS 116 & Record "Right of Use Asset" & Such ROU Asset is treated as Investment Property Under Ind AS 40

Important Conclusions:-

1. Assets owned by Entity but given on Finance Lease - **Ind AS 40 shall not apply**
2. Asset taken on Finance Lease by Entity and given on Operating Sub - Lease - **Ind AS 40 shall apply.**
3. Asset owned by Entity and given on Operating Lease - **Ind AS 40 shall apply.**
4. Asset taken by Entity on Operating Lease (i.e. Short Term Period) (High chances to use in business) - **Ind AS 40 may not apply** because there are high chances to use the asset in Business.

3. SPECIAL CASES

A. PROPERTY HELD FOR MORE THAN ONE PURPOSE (Dual Use Property)

In circumstances when property is held partly for capital appreciation and/or rentals, and partly for production or supply of goods or services or for administrative purposes, **the two parts are accounted for separately if they could be sold, or leased out separately under a finance lease, separately.**

If the two portions could not be sold separately:

- The property is treated as owner-occupied if a significant portion is held for own use.
- The property is treated as investment property only if an insignificant portion is held for own use.

Case 1)

Lets assume we have a property with 1200 sq feet of space out of which 700 sq feet space is used for business purposes and the remaining 500 sq feet is vacant and intended to be given on operating lease. Both the parts can be separately sold or leased out.

Answer:

As both parts can be separately sold or leased out, hence 700 sq feet of space shall be recognized as **Owner Occupied Property** and 500 sq feet shall be recognized as **Investment Property**.

Case 2)

Lets assume we have a property with 1200 sq feet of space out of which 1100 sq feet space is used for business purposes and the remaining 100 sq feet is vacant and intended to be given on operating lease. Both the parts can-not be separately sold or leased out.

Answer:

As significant part of property is used for business purpose and both the parts can-not be separately sold or leased out, hence whole 1200 sq feet of space shall be recognized as **Owner Occupied Property**.
(Record PPE)

Case 3)

Lets assume we have a property with 1200 sq feet of space out of which 100 sq feet space is used for

business purposes and the remaining 1100 sq feet is vacant and intended to be given on operating lease. Both the parts can-not be separately sold or leased out.

Answer:

As insignificant part of property is used for business purpose and both the parts can-not be separately sold or leased out hence whole 1200 sq feet of space shall be recognized as **Investment Property**.

Case 4)

Lets assume we have a property with 1200 sq feet of space out of which 300 sq feet space is used for business purposes and the remaining 900 sq feet is vacant and intended to be given on operating lease. Both the parts can-not be separately sold or leased out. Property with business part is having significant use.

Answer:

As significant part of property is used for business purpose and both the parts can-not be separately sold or leased out hence whole 1200 sq feet of space shall be recognized as **Owner Occupied Property**.
(Record PPE)

Dual use property (Business / Capital appreciation)	
Separable	Non-Separable
One Part - PPE Other Part - Investment Property (Ignore Significant/ Insignificant parts)	<ul style="list-style-type: none"> • Treat full property as Investment Property when insignificant part of property is used for business purpose. • Otherwise full property is PPE in all other cases.

Example 1

Sun Ltd owns a building having 15 floors of which it uses 5 floors for its office; the remaining 10 floors are leased out to tenants under operating leases. According to law company could sell legal title to the 10 floors while retaining legal title to the other 5 floors. In the given scenario, the remaining 10 floors should be classified as investment property, since they are able to split the title between the floors.

Example 2

Moon Ltd uses 35% of the office floor space of the building as its head office. It leases the remaining 65% to tenants, but it is unable to sell the tenant's space or to enter into finance leases related solely to it. Therefore, the company should not classify the property as an investment property as the 35% of the floor space used by the company is significant.

Example 3

An entity owns a hotel, which includes a health and fitness centre, housed in a separate building that is part of the premises of the entire hotel. The owner operates the hotel and other facilities on the hotel with the exception of the health and fitness centre, which can be sold or leased out under a finance lease. The health and fitness centre will be leased to an independent operator.

The entity has no further involvement in the health and fitness centre. In this scenario, management should classify the hotel and other facilities as property, plant and equipment and the health and fitness centre as investment property.

If the health and fitness centre could not be sold or leased out separately on a finance lease, then because the owner-occupied portion is not insignificant, the whole property would be treated as an owner-occupied

property.

B. ANCILLARY SERVICES

In some cases, an entity provides ancillary services to the occupants of a property it holds. An entity treats such a property as investment property **if the services are insignificant to the arrangement as a whole**. An example is when the owner of an office building provides security and maintenance services to the lessees who occupy the building.

In other cases, the services provided are significant. For example, if an entity owns and manages a hotel, services provided to guests are significant to the arrangement as a whole.

C. PROPERTY LEASED TO OTHER GROUP MEMBERS

In some cases, an entity owns property that is leased to, and occupied by, its parent or another subsidiary. The property does not qualify as investment property in the consolidated financial statements, because the property is owner-occupied from the perspective of the group. **The end use of the property is to be checked to record property accordingly**. Therefore, the lessor treats the property as investment property in its individual financial statements.

TABULAR SUMMARISATION

S. No.	Property	Does it meet definition of Inv. Prop?	Which Ind AS is app.?
1	Owned by a company and leased out under an operating lease	YES	Ind AS 40
2	Held under Right of Use Asset and leased out under an Operating Lease	YES	Ind AS 40
3	Held under Right of Use Asset and leased out under an Finance Lease	No	Ind AS 116
4	Property acquired with a view for development or resale	No	Ind AS 2 & Ind AS 115
5	Property developed on behalf of 3 rd Party	No	Ind AS 115
6	Property partly owner occupied and partly leased out under Operating Lease	Depends	Ind AS 16 Ind AS 40
7	Land held for Currently Undetermined use	YES	Ind AS 40
8	Property occupied by Employees paying rent at less than market rate	No	Ind AS 16
9	Investment Property held for Sale	No	Ind AS 105
10	Existing Investment Property that is being redeveloped for continued use as Investment Property.	Yes	Ind AS 40

4. INITIAL RECOGNITION

The rules for recognition of investment property are essentially the same as stated in IND AS 16 for property, plant and equipment, i.e. you recognize an investment property as an asset only if 2 conditions are met:

1. It is probable that **future economic benefits** associated with the item will flow to the entity; and
2. The **cost** of the item can be **measured reliably**.

An investment property held by a lessee as a right-of-use asset shall be recognised in accordance with Ind AS 116.

How to Measure Investment Property Initially

Investment property shall be initially measured **at cost, including the transaction cost**.

The cost of investment property includes:

- Its **purchase price** and
- Any **directly attributable expenditure (DAC)**, such as legal fees or professional fees, property taxes, etc.

We **should NOT** include:

- **Start-up expenses** whatsoever.
However, if these start-up expenses are directly attributable to the item of investment property, then you can include them. But do NOT include any general start-up expenses.
- **Operating losses** that you incur before planned occupancy level is achieved, and
- **Abnormal waste** of material, labor or other resources incurred at construction.

Deferred Payments

If payment for an investment property is deferred, **its cost is the cash price equivalent**. The difference between this amount and the total payments is recognised as **interest expense** over the period of credit.

Investment Property acquired through Exchange of another Asset

Investment Property acquired in Exchange for a Non-monetary Asset or Assets or a combination of Monetary and Non-monetary Assets:

Cost of Investment Property is **measured at Fair Value of Asset Given (1st Priority) or Asset Received (2nd Priority) unless:**

- (i) Exchange transaction lacks commercial substance; Or
- (ii) Fair value of neither the asset(s) received nor the asset(s) given up is reliably measurable.

If the PPE acquired is **not** measured at Fair Value, its cost is measured at the **carrying amount of the asset given up**.

Example 4

Sun Ltd acquired a building in exchange of a warehouse whose fair value is Rs. 5,00,000 and payment of cash is Rs. 2,00,000. The fair value of the building received by the Company is Rs. 8,00,000. The company decided to

keep that building for rental purposes.

The Building is acquired with the purpose to earn rentals. Hence, it is a case of Investment Property acquired in exchange for a combination of monetary and non-monetary asset.

Therefore, Journal entry at the time of acquisition is:

Investment Property (Building) (5,00,000 + 2,00,000)	Dr.	7,00,000	
To Cash			2,00,000
To PPE (Property, Plant and Equipment) i.e. Warehouse			5,00,000

Note: When the fair value of both the asset given up and acquired is mentioned, it is presumed that both the fair values are equally evident. In such a case, the fair value of the asset given up is considered as the cost of the asset purchased.

However, if the fair value of property acquired is more clearly evident, then the fair value of the asset acquired is considered. In such a situation, the Journal Entry at the time of acquisition (taking information given in the above example) would be

Investment Property (Building)	Dr.	8,00,000	
To Cash A/c			2,00,000
To PPE (Warehouse)			5,00,000
To Gain on Sale of PPE			1,00,000

5. SUBSEQUENT COSTS

Do Not Capitalised	Can be Capitalised
Cost of Day to Day servicing of a property	Replacement cost incurred for the parts of Investment property if it meets the recognition criteria. In this case, carrying amount of old replaced parts are derecognized.

6. SUBSEQUENT MEASUREMENT OF INVESTMENT PROPERTY

After initial recognition, we have only one choice for measuring our investment property i.e. at **COST Model**

Here, IND AS 40 does not describe it in details, but refers to the standard **IND AS 16 Property, Plant and Equipment**. It means you need to take the same methodology as in IND AS 16. Investment property is **depreciated** and **impaired** same as in **IND AS 16**.

(a) Fair value only for disclosure

Entities are required to **measure the fair value of investment property, for the purpose of disclosure** even though they are required to follow the cost model. An entity is encouraged, but not required, to measure the fair value of investment property on the basis of a valuation by an **independent valuer** who holds a recognised and relevant professional qualification and has recent experience in the location and category of the investment property being valued. **Fair Value should**

reflect the Rental income from current leases and other assumptions that market participants would use when pricing investment property under current market conditions.

(b) Inability to measure fair value reliably

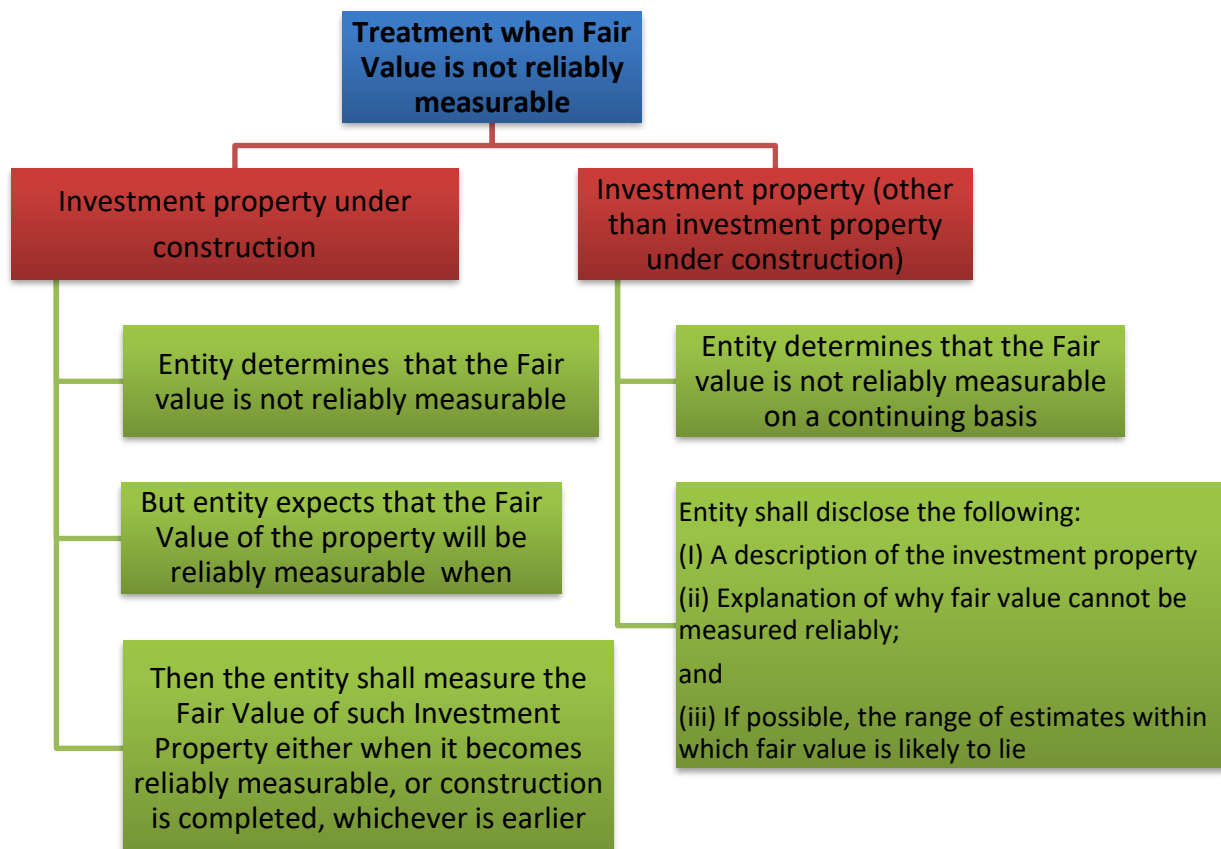
There is a rebuttable presumption that an entity can reliably measure the fair value of an investment property on a continuing basis.

If an entity determines that the fair value of an investment property (other than an investment property under construction) is not reliably measurable on a continuing basis, the entity should make the disclosures as prescribed under Ind AS 40.

(c) Investment property in the course of construction

If an entity determines that the fair value of an investment property under construction is not reliably measurable but expects the fair value of the property to be reliably measurable when construction is complete, it should measure the fair value of that investment property either when its fair value becomes reliably measurable or construction is completed (whichever is earlier).

Once construction of that property is complete, it is presumed that fair value can be measured reliably. If this is not the case, the entity should make the disclosures as required by Ind AS 40.



7. TRANSFERS FROM AND TO INVESTMENT PROPERTY

The transfers are possible, but only **when there's a change in use or asset's purpose**, for example:

1. You start renting out the property that you previously used as your headquarters (transfer to investment property from owner-occupied property under INDAS 16)
2. You stop renting out the building and start using it for yourself.
3. You held a land for undefined purpose and recently, you decided to construct an apartment house to sell apartments when they are built (transfer from investment property to inventories).
4. Commencement of owner-occupation, or of development with a view to owner-occupation, for a transfer from investment property to owner-occupied property;
5. Commencement of development with a view to sale, for a transfer from investment property to inventories;
6. End of owner-occupation, for a transfer from owner-occupied property to investment property;
7. Inception of an operating lease to another party, for a transfer from inventories to investment property.

So what's the accounting treatment in this case.

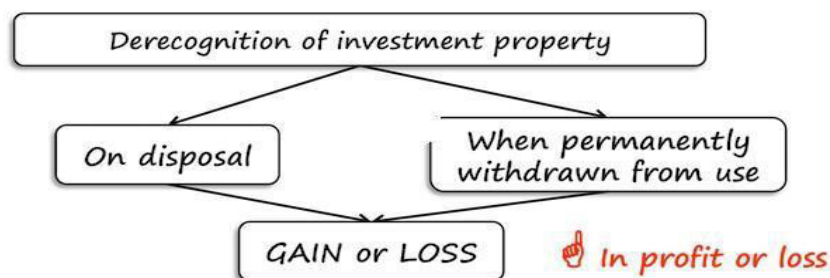
Transfers between investment property, owner-occupied property and inventories **do not change the carrying amount of the property transferred** and they do not change the cost of that property for measurement or disclosure purposes

Note:

- Such change in classification is **not a change in Accounting Policy**. Hence no retrospective effect.
- PPE reclassified to Investment Property:- Earlier PPE was revalued and after some years it is reclassified to Investment Property. In such case it is reclassified to the same carrying amount after revaluation effect. But no further revaluation shall be done.
- Balance of Revaluation Surplus shall be continued till the disposal of Property.

8. DERECOGNITION OF INVESTMENT PROPERTY

The De-recognition rules (when you can remove your investment property from your books) in INDAS 40 **are similar to the rules in IND AS 16**.



$$= \text{Net Disposal Proceeds} - \text{Carrying Amount}$$

Example 5:

Sun Ltd, an aeronautics company is having a building which is given on an operating lease. The book value of such building in the books is ₹ 2,00,000.

Case - A

Pluto Ltd. offers to buy the building at ₹ 4,00,000.

Bank	Dr	4,00,000	
	To Investment Property		2,00,000
	To Gain on disposal		2,00,000

Case- B

Pluto Ltd. Offers to take the building on finance lease for 10 years at a lease rental of ₹ 80,000 p.a. The present value of minimum lease payments is ₹ 3,20,000.

Lease Receivable	Dr	3,20,000	
	To Investment Property		2,00,000
	To Gain on Disposal		1,20,000

9. DISCLOSURES

An entity should disclose:

- ❖ Its **accounting policy** for measurement of investment property.
- ❖ the criteria it uses to distinguish investment property from owner-occupied property and from property held for sale in the ordinary course of business.
- ❖ The **Fair Value** of Investment Property. In the exceptional cases when an entity cannot measure the fair value of the investment property reliably, it should disclose:
 - a description of the investment property;
 - an explanation of why fair value cannot be measured reliably; and
 - if possible, the range of estimates within which fair value is highly likely to lie.
- ❖ the amounts recognised in profit or loss for:
 - rental income from investment property;
 - direct operating expenses (including repairs and maintenance) arising from investment property that generated rental income during the period; and
 - direct operating expenses (including repairs and maintenance) arising from investment property that did not generate rental income during the period.
- ❖ In addition to the general disclosures required above, an entity is required to disclose:
 - the depreciation methods used;
 - the useful lives or the depreciation rates used;
 - the gross carrying amount and the accumulated depreciation (aggregated with accumulated impairment losses) at the beginning and end of the period;

IND AS 116

LEASES

**"The higher you go, the more challenges you face.
Every new Levels Attract new devils"**

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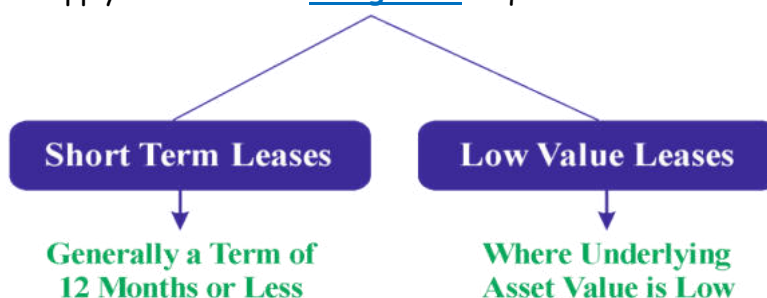
Note: Ind AS 116 is applicable to Lessee's as well as Lessor's Financial Statements

1.SCOPE OF INDAS 116:

Ind AS 116 shall be applied to **all leases except** for:

Sr. No.	Particulars	Reason
1	Leases to explore for or use minerals, oil, natural gas and similar non-regenerative resources	Within the scope of Ind AS 106 'Exploration for and Evaluation of Mineral Resources'
2	Leases of biological assets held by a lessee	Within the scope of Ind AS 41 'Agriculture'
3	Service concession arrangements Eg. BOT Contracts	Within the scope of Appendix D of Ind AS 115 'Revenue from Contracts with Customers'
4	Licences of intellectual property granted by a lessor	Within the scope of Ind AS 115 'Revenue from Contracts with Customers'
5	Rights held by a lessee under licensing agreements for such items as motion picture films, video recordings, plays, manuscripts, patents and copyrights	Within the scope of Ind AS 38 'Intangible Assets'

A **lessee** can elect not to apply Ind AS 116's **recognition** requirements to:



If a lessee **elects to apply** the above recognition exemption, the lessee shall recognise **the lease payments** associated with those leases **as an expense** on **either a straight-line basis over the lease term or another systematic basis**, if that basis is more representative of the pattern of the lessee's benefit. Hence ROU Asset and Lease Liability not recorded.

(A) Short Term Leases

Meaning - A short-term lease is a lease that, at the commencement date, has a lease term of 12 months or less and does not include an option to purchase the underlying asset.

Conditions -

- This **Exemption shall be applied to the entire class of Underlying Assets** on Which Lessee has Right to Use.
- A short-term lease **does not include an option to purchase** the underlying asset.

Renewal Option - If the option of renewal of term (beyond 12 Months) is available at commencement date -

Such option is Reasonable Certain	Option is not Reasonable Certain
Not a Short Term Lease	Short Term Leases

Author's Note:

Question: If renewal option was not available at commencement of lease or at commencement it was not certain that lessee will avail the option, but after some period, lessee availed the renewal then what? Short Term Lease continues or not?

Answer: If renewal is for 12 months or more then No Short-Term lease for the further period. If renewal is for less than 12 months then lessee has to analyse based on nature i.e. it can be Short-Term if no more renewal is planned in future. It can-not be Short Term if renewal is continues in nature.

(B) Leases of Low Value Assets (Low Value Leases):

1. Individual Asset having **Low Value** can be exempted from Recognition criteria of Ind AS 116.
2. However, IndAS 116 does not explicitly define the leases of low-value assets.
3. The exemption for leases of low-value items intends to capture leases that are high in volume but low in value – e.g. leases of small IT equipment (laptops, mobile phones, simple printers), leases of office furniture etc. Ind AS 116 is silent on any threshold to determine the value for classifying any asset as low value assets.
4. **The exemption can be made on a lease-by-lease basis.**
5. Individual Asset having Low Value can be Exempted from IndAS 116 only when following two conditions are satisfied-
 - (i) Such Asset can provide Benefit to Lessee **on its own** (i.e. it is capable of giving benefit individually) or together with other resources which are readily available.
 - (ii) Such Asset is **not highly dependent or highly interrelated with other Assets.**

Important Notes:

1. When a New Asset is typically not of a Low Value then this exemption will not be applied, example Lease of Cars would not qualify because new car would typically not be of Low Value.
2. **Sub-letting of Leased Asset** - If a lessee sub-leases an asset, or expects to sub-lease an asset, the **head lease does not qualify as a lease of a low-value asset**, i.e., an intermediate lessor who subleases, or expects to sublease an asset, cannot account for the head lease as a lease of a low-value asset.

However, Sublease is allowed for "Short Term Lease" Exemption.

PART 2 - IMPORTANT DEFINITIONS

(1) What is Lease?

A Lease is

- A contract, or part of a contract
- That provides the **right to control** the use of an **identified asset**
- For a **period of time**
- In **exchange for consideration (lease rent)**.

(2) Dates under Leases -

Inception of the Lease	Commencement of the Lease
<p>Date of Lease agreement or Date of Commitment by Parties whichever is earlier.</p> <p>As at this date, the lessee shall assess if the contract is or contains lease.</p>	<p>Date on which Asset is Available for Lessee</p> <p>As at this date-</p> <p>Lessee initially recognises a lease liability and related Right of Use Asset</p> <p>Lessor (for finance leases) initially recognises its net investment in the lease on the commencement date.</p> <p>In simple terms, Journal Entries are recorded from the Commencement date.</p>

(3) RIGHT TO CONTROL

To assess whether lessee has the right to control the use of an identified asset, an entity (lessee) shall assess, whether it has:

- (a) The right to obtain **substantially all of the economic benefits** from use of the identified asset; **and**
- (b) The **right to direct the use** of the identified asset.

How to determine whether customer has Right to obtain substantially all of the Economic Benefits?	How to determine Right to Direct the Use of the Identified Asset?
<p>Right to obtain substantially all the Economic Benefits means customer can exclusively use the asset throughout that period.</p> <p>A customer can obtain economic benefits either directly or indirectly for e.g., by using, holding or subleasing the asset.</p>	<p>A customer has the right to direct the use of an identified asset whenever it has the right to direct how and for what purpose the asset is used throughout the period of use (i.e., it can change how and for what purpose the asset is used throughout the period of use).</p> <p>The focus should be on whether the customer has the decision-making rights that will most affect the economic benefits that will be derived from the use of the asset.</p>

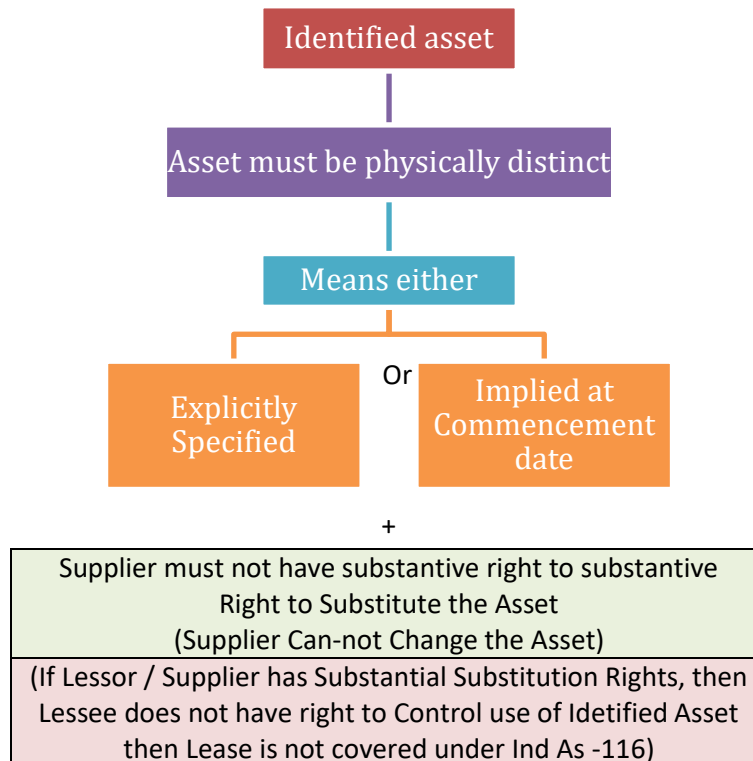
Author's Note:

However, Lessor may impose some of its **protective rights** (i.e. to protect its Assets). Such as maximum amount of use or not to sub-lease etc. We should ignore the Protective rights imposed by Lessor while determining whether Lessee has Right to Direct the Use or Not.

(4) IDENTIFIED ASSET

An Asset is identified only when it satisfies following conditions:

- 1) Asset must be physically distinct.
- 2) Supplier (Lessor) does not have Substantive substitution rights on Asset.



Identified Asset **must be** physically distinct, **be it entirely or in some portion**.

For Example - A building is generally treated as physically distinct but one floor may also be considered as physically distinct if the same can be used independently.

Substantive Substitution Rights with Supplier

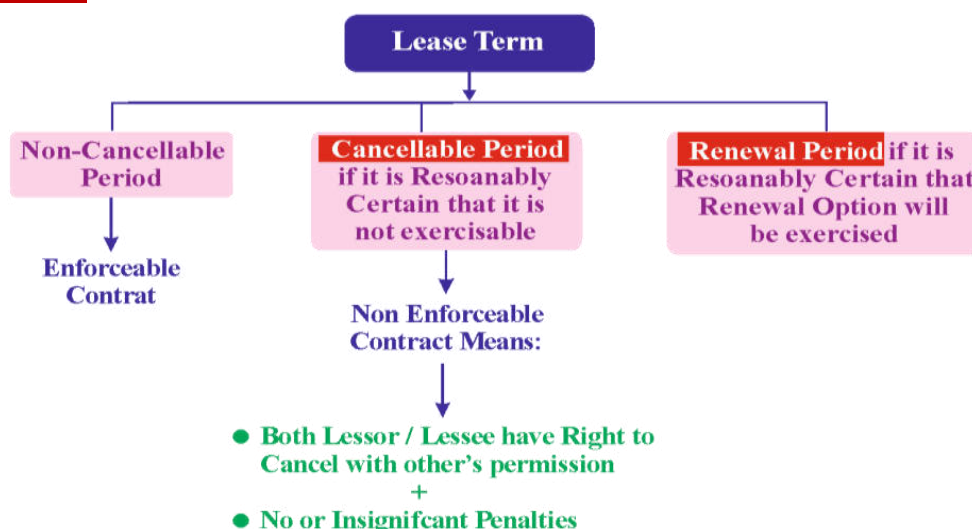
Even if an asset is specified, a customer does not have the right to use an identified asset if, at inception of the contract, a supplier has the substantive right to substitute the asset throughout the period of use.

A supplier's right to substitute an asset is **SUBSTANTIVE** when **BOTH** of the following conditions are met:

(a) Supplier has the **Practical ability** to substitute alternate asset **throughout the period of use**. (This means substituting the asset for reasons other than operational inefficiency or any contractual obligation.)

(b) The Supplier would **Benefit Economically** from substituting the asset. (For Ex: One high cost machinery with another similar low cost machine so that supplier can earn more from the high value machine by leasing it or selling it to third party).

(5) LEASE TERM:



Lease Term includes any **non-consecutive periods of time** (for eg. 3 months in every year I will use the Vehicle to run my business).

(6) CANCELLABLE LEASES:

If for the particular period, the terms and conditions of the contract are not enforceable then such period is called cancellable lease.

The contract is **not enforceable** if:

- (i) **both** the lessor and lessee each have **the right to terminate** the lease without permission from the other party; **AND**
- (ii) with no more than an **insignificant penalty**

Suppose the term of a contract is 10 years and the non-cancellable / lock-in period is 6 years. The lease term shall be as follows:

If the termination option is with 'Lessor'	If the termination option is with 'Lessee'	If the termination option is with 'Both' (i.e., any party can terminate)
<p>The lease term shall be 10 years. Because even after 6th year, the lessee would be contractually bound until 10th Year i.e. lessee cannot refuse to make the payment till the expiry of the contract and also, has the right to use the asset until 10th year, unless lessor terminates the contract.</p>	<p>Alternative - 1 The lease term shall be 10 years assuming reasonable certainty. Because after the expiry of 6th year, though the lessee is not contractually bound till 10th year, i.e., the lessee can refuse to make payment anytime without lessor's permission but, it is assumed that the lessee is reasonably certain that it will not exercise this option to terminate. Hence, though there is no enforceable obligation from lessee's point of view beyond 6th year but, basis the said assumption, the lease term shall be 10 years.</p> <p>Alternative - 2 If it is reasonably certain that lessee will avail Termination option then Lease Term will be only 6 Years</p>	<p>The lease term shall be 6 years. Because after 6th year, either party can terminate the contract without the consent of the other party and hence, the contract is not enforceable after 6th year ONLY in case there is insignificant penalty for termination.</p> <p>However, alternative answer may exist.</p>

PART 3 – RECOGNITION AND MEASUREMENT OF LEASE CONTRACT IN THE BOOKS OF LESSEE

Lessee shall measure and recognise the followings in the books:

- (a) RIGHT - OF - USE ASSET
- (b) LEASE LIABILITY

1. INITIAL RECOGNITION AND MEASUREMENT

LEASE LIABILITY	RIGHT-OF-USE ASSET								
<p>Recognise at PV of remaining lease payments to be made over the lease term discounted using the Implicit Rate of Interest (i.e. IRR)</p> <p>If Implicit rate of interest can-not be readily determined, then take Lessee's Incremental Borrowing Rate.</p> <p>Lease Payments covers Present Values of-</p> <ul style="list-style-type: none"> • Fixed Payments less Lease Incentives • In-substance Fixed Payments • Variable Lease Payments depends on Index or Rate • Guaranteed Residual Value • Purchase option Price • Penalties for Terminating the Lease <p>Lease Payments Excludes -</p> <ul style="list-style-type: none"> • Payment made for and allocated to Non-lease Component (if accounted for separately) • Variable Lease Payments not dependent on Index or Rate 	<p>A lessee initially measures the ROU Asset at COST.</p> <p>Cost of ROU:</p> <table style="width: 100%; border-collapse: collapse;"> <tr> <td style="width: 70%;">Initial Lease Liability</td> <td style="text-align: right;">XXX</td> </tr> <tr> <td>Down payment</td> <td style="text-align: right;">XXX</td> </tr> <tr> <td>Any initial direct costs</td> <td style="text-align: right;">XXX</td> </tr> <tr> <td>PV dismantling cost</td> <td style="text-align: right;">XXX</td> </tr> </table> <p>Note:</p> <p>Lessee may be required to make payments for construction or designing of an underlying asset so that lessee can use it after lease arrangement, these are accounted under Ind AS 16 and are not a part of lease payments.</p>	Initial Lease Liability	XXX	Down payment	XXX	Any initial direct costs	XXX	PV dismantling cost	XXX
Initial Lease Liability	XXX								
Down payment	XXX								
Any initial direct costs	XXX								
PV dismantling cost	XXX								

Journal entry in the books of lessee at Commencement

ROU Asset	Dr.	Sum total of all below items
To Lease liability	Cr.	PV of outstanding lease payments by lessee using interest rate implicit in lease
To Bank	Cr.	Down Payment
To Bank / Creditor	Cr.	Initial direct costs incurred by lessee
To Provision for dismantling / removing the underlying asset	Cr.	Estimate of costs to be recognised only when lessee incurs an obligation for these costs (Ind AS 37)

Let's define each and every term in Lease Payments deeply-

Fixed Lease Payments	An amount agreed between lessee and Lessor
In Substance Fixed Payments (i.e. Variable but unavoidable)	<p>Payments which may contain variability but that in substance are unavoidable. These payments are variable as per the terms given in the agreement, but there is no genuine variability in those payments.</p> <p>Example - A Lessee enters into a 10 year lease of commercial space, for which lease payment will be Rs. 1000/- Per month unless sales are more than</p>

	Rs. 20000. If sales will be higher than 20000/- the lease payment will be Rs. 1,00,000 pm, it is normal for a lessee to make a sale of at-least Rs. 5,00,000 pm.
Lease Incentives receivable from Lessor	Payments made by a lessor to a lessee associated with a lease, or the reimbursement or assumption by a lessor of costs of a lessee. (such as transportation expenses)
Variable Lease Payments	Only those payments will be covered which are depending on Index or a Rate . Eg. Payments linked to consumer price index Payments linked to a Benchmark Interest Rate (such as Libor, PLR)
Purchase option price	If the lessee is reasonably certain to exercise a purchase option, the exercise price is included as a lease payment
Penalties for terminating a lease	If it is reasonably certain that the lessee will not terminate a lease, the lease term is determined assuming that the termination option would not be exercised, and any termination penalty is excluded from the lease payments. Otherwise , the lease termination penalty is included as a lease payment.
Guaranteed Residual Value (GRV)	It is the guarantee given on the residual value of the asset. At the end of lease term, the value of the leased asset must be of this amount. If the residual value of the asset is less than the guaranteed value; the lessee needs to pay the balance amount (GRV less Actual Residual Value)
Discounting Rate	1st Priority - Interest Rate Implicit in the Lease (i.e. IRR) of the Lessor 2nd Priority - Lessee's Incremental Borrowing Rate.
Interest Rate Implicit in the Lease (i.e. IRR) (Consider always from Lessor's point of view) (Refer Practical Example 2)	It is the rate at which- $PV \text{ of } (LP + UGRV) = FV \text{ at Inception} + IDC$
Lessee's Incremental Borrowing Rate	It is the rate at which Lessee can Borrow additional funds over a similar terms , security for the same amount of underlying asset.

2. SUBSEQUENT MEASUREMENT (at Balance Sheet)

RIGHT-OF-USE ASSET:

a) At every BS date measure ROU Asset using either **COST Model** or **REVALUATION Model** (Ind AS 16).

b) Depreciation-

- Apply **Ind AS 16** to depreciate ROU Asset
- Period of Depreciation is either:
 - **Commencement Date to the end of Useful life** (if ownership will be transferred to lessee at the end of lease term or lessee has option to purchase the asset at the end of the term if reasonable certain). Or
 - **Commencement Date till Remaining useful life of the asset or Lease Term whichever is lower** if ownership is not getting transferred or no option to buy.

LEASE LIABILITY:

- Lease liability at balance sheet date shall be **equal to PV of remaining lease payment** at discount rate.
- Charge Interest Expenses (Finance Charges) on the lease liability over the lease term **to unwind the discount**.
- Re-measuring the carrying amount to reflect any reassessment or lease modifications. (such as **due to Changes in the future lease payments**).
- Interest expense is calculated as under:

Year (1)	Opening Bal. of Lease Liability (2)	Interest @ Discount Rate (3 = 2 x Rate)	Actual Payment (Lease Payment) (4)	Closing Bal. of Lease Liability (5 = 2 + 3 - 4)

(Refer Practical Example 1 on Lessee's Accounting)

What are the expenses which Lessee shall transfer to its Profit and Loss Statement?

- ❖ **Depreciation** of the ROU Asset
- ❖ **Interest** expense on the Lease Liability
- ❖ **Variable lease payments** that are not included in the lease liability (for e.g., variable lease payments that do not depend on an index or rate)
- ❖ **Impairment** of the ROU Asset (INDAS 36)
- ❖ **Change in Lease Liability** after adjusting ROU (if ROU reduced to Zero)

Leases denominated in a Foreign Currency (Refer Practical Example 3)

- Lessee shall **remeasure** the foreign currency-denominated lease liability using the **exchange rate at each reporting date**, like they do for other monetary liabilities.
- Any changes to the lease liability due to exchange rate changes are recognised in **profit or loss**.
- Because the **ROU Asset is a non-monetary asset measured at historical cost**, it is not affected by changes in the exchange rate.

3. RE-MEASUREMENT OF LEASE LIABILITY

Ind AS 116 requires lessees to **REMEASURE LEASE LIABILITIES** upon a change in lease payments on account of **ANY** of the following:

Unavoidable changes (Market related changes)	Changes made by lessor (Non-Market related changes)
<ul style="list-style-type: none"> ● Change in Expected GRV ● Change in future lease payments due to change in an Index or a Rate ● The Variability of Payments is resolved so that they become in-substance Fixed Payments 	<ul style="list-style-type: none"> ● Change in the Lease Term ● Change in assessment of an option to purchase the asset
Discounting Rate - Same original Discounting Rate shall be considered while calculating revised Lease Liability.	Discounting Rate - Revised Discounting Rate shall be considered while calculating revised Lease Liability.

Journal Entry:

1. Increase in Lease Liability:

ROU Asset A/c Dr.
To Lease Liability A/c

2. Decrease in Lease Liability:

Lease Liability A/c Dr
To ROU Asset A/c

Note: If Carrying amount of **ROU Asset is Zero or reduced to Zero** and further reduction due to re-measurement shall be transferred to **Profit and Loss A/c**.

(Refer Practical Example 4)

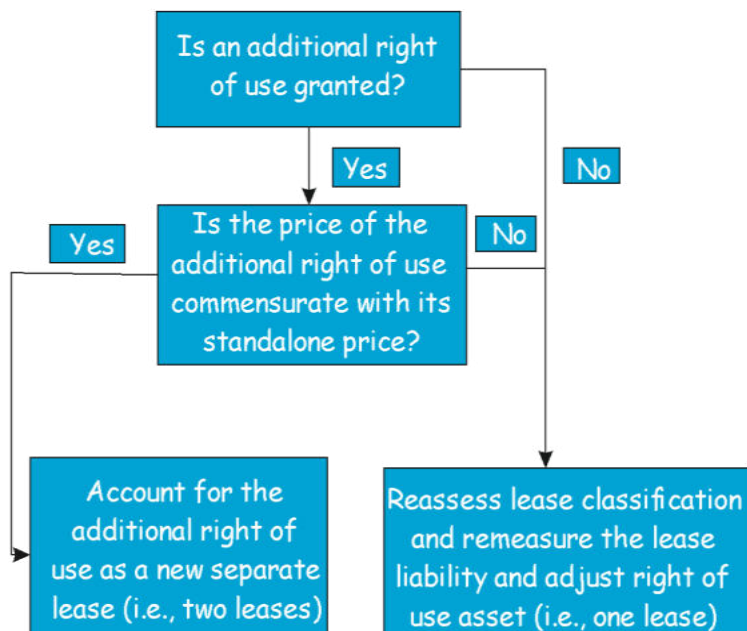
PART 4 – IMPORTANT POINTS

<p>LEASE OF MULTIPLE ASSETS: Eg. Two or more Buildings, Building with equipment's etc.)</p> <p>Each Asset shall be treated as "Separate Lease Component" (i.e., separate Contract) only when two conditions fulfilled.</p>	<p><u>Conditions</u></p> <p>(a) Lessee can take benefit from each Asset on its own or together with other resources that are readily available to the lessee.</p> <p style="text-align: center;">AND</p> <p>(b) The underlying asset is not highly dependent on, or highly interrelated with other assets.</p> <p>(Example - Parking Space taken separately with Flat Purchased)</p> <p>If any one or both the conditions are not met then, the right to use multiple assets is considered a Single Lease Component.</p>
<p>CONTRACT COMBINATION</p> <p>Two or More contracts with Same party entered into or near the same time be considered a "Single Contract" if any one of these conditions are met -</p>	<p><u>Conditions:</u></p> <p>The contracts are negotiated as a package.</p> <p style="text-align: center;">OR</p> <p>The amount of the consideration to be paid in one contract depends on the price or performance of the other contract.</p> <p style="text-align: center;">OR</p> <p>All or major assets are leased for a common objective. It means assets are dependent or inter-related with each other.</p> <p>Let us take an example: Separate contracts entered into between lessee and lessor to lease factory Building, Machineries, and Vehicles. The common overall objective is to run a factory for a commercial production purpose. In such case individual contract to lease a land & Building or Machineries or Vehicles would not help to understand the single overall objective. Further since the objective is common hence price and performance of these assets are interrelated.</p>
<p>HOW TO SEPARATE LEASE COMPONENTS FROM NON-LEASE COMPONENTS.</p> <p>Non-lease component means supply of other Goods or services</p>	<p>Only items that contribute to securing the output of the asset are lease components.</p> <p>Example 1</p> <p>A supplier may lease a truck and also operate the leased asset on behalf of a customer (i.e., provide a driver). This service is not related to securing the use of the truck. Means truck can be given on lease without driver's service.</p>

	<p>Example 2</p> <p>Payments for maintenance activities, including common area maintenance (for e.g., cleaning the common areas of a building, removing snow from a car park for employees and customers) and other goods or services transferred to the lessee (for e.g., providing utilities or rubbish removal) are considered as non-lease components because they provide the lessee with a service.</p>
<p>NOT A SEPARATE COMPONENT OF CONTRACT</p> <p>(Author's Note: Do not treat them as separate Non-Lease Component, they should be part of Lease Payments only)</p>	<p>Any payment made by lessee to lessor that relate to the Lease Asset and for those activities that do not transfer separate Goods or Services to the lessee.</p> <p>(For e.g., payments made for real estate taxes that would be owed by the lessor regardless of whether it leased the building and regardless of who the lessee is)</p>
<p>OPTIONAL EXEMPTION of using <u>Practical Expedient</u> to not to separate non-lease component.</p> <p>Using Practical expedient means using Short Cut.</p>	<p>Lessee has the choice to account for each separate lease component and non-lease components as a SINGLE LEASE COMPONENT. No need to bifurcate.</p> <p>However, the practical expedient is not permissible for lessor.</p>
<p>ALLOCATION OF TOTAL CONSIDERATION TO LEASE AND NON-LEASE COMPONENTS</p> <p>(if lessee doesn't opt for practical expedient)</p>	<p>In the Ratio of observable Stand-alone Prices of Lease and Non-lease Component.</p> <p>Stand-alone Prices means the Prices at which a customer would purchase a component of a contract separately when available.</p>
<p>How to account Non-lease Component?</p>	<p>As per the Other Applicable Standards</p>

LEASE MODIFICATIONS

- A 'lease modification' is a **change** in the scope of a lease, or the consideration for a lease, **that was not part of the original terms and conditions of the lease**.
- For e.g., adding or terminating the right to use one or more underlying assets, or extending or shortening the contractual lease term.
- Under Lease Modification, the important question is "**Do we need to make separate lease accounting or we should adjust existing carrying amount of ROU & Lease Liability**"?



Difference Cases of Lease Modification are as under:

<p>Case 1: Increase in Lease Term (Refer Practical Ex 5)</p>	<p>Step 1: Calculation Carrying Amount of Lease Liability as on Modification date</p> <p>Step 2: Calculate Revised PV of Lease Payments as per Revised Discount Rate for increase term</p> <p>Step 3: Difference of Carrying Amount (Step 1) and Revised Amt. (Step 2) is added or deducted through ROU Asset</p>
<p>Case 2: Change in Consideration without change in Lease Term (Refer Practical Ex 6)</p>	<p>Same Steps as above (same as case 1)</p>
<p>Case 3: Decrease in Lease Term (Refer Practical Ex 7)</p>	<p>Step 1: Decrease the Carrying Amt. of ROU Asset Proportionately with decrease in lease term as under:</p> <p>Revised ROU Asset as per Decreased Term = $\frac{\text{Current Carrying Amt} \times \text{Remaining Revised Lease Term}}{\text{Original Remaining Lease Term}}$</p> <p>Step 2: Decrease the carrying amount of Lease Liability as per revised lease term with Original Discount Rate</p> <p>Step 3: Difference of Step 1 and 2 is charged to Profit and Loss A/c as under:</p> <p style="text-align: center;">Lease Liability A/c Dr. To ROU Asset A/c</p>

	To Gain A/c
	<p>Step 4: Remeasure the lease liability again as per revised discount rate and remaining lease term and adjust through ROU Asset.</p>
<p>Case 4: Decrease in Scope of ROU Asset (Refer Practical Ex 8)</p>	<p>Step 1: Decrease the Carrying Amt. of ROU Asset Proportionately as under:</p> <p>Revised ROU Asset = $\frac{\text{Current Carrying Amt} \times \text{Revised Rights (Scope)}}{\text{Original Rights (Scope)}}$</p> <p>Step 2: Decrease the carrying amount of Lease Liability as under:</p> <p>Decreased Lease Liability = $\frac{\text{Current Carrying Amt} \times \text{Revised Rights (Scope)}}{\text{Original Rights (Scope)}}$</p> <p>Step 3: Difference of Step 1 and 2 is charged to Profit and Loss A/c as under:</p> <p style="text-align: center;">Lease Liability A/c Dr. To ROU Asset A/c To Gain A/c</p> <p>Step 4: Remeasure the lease liability again as per revised discount rate and remaining lease term and adjust through ROU Asset.</p>
<p>Case 5: Increase in Scope of ROU Asset without stand-alone price (Refer Practical Ex 9)</p>	<p>Step 1: Calculate the Lease Liability and ROU value of additional Scope as per Revised Discount Rate</p> <p style="text-align: center;">ROU Asset A/c Dr. To Lease Liability A/c</p> <p>Step 2: Existing ROU & Lease Liability shall be revised based on Revised Discount Rate.</p>

PRESENTATION IN FINANCIAL STATEMENTS

Balance Sheet	Statement of profit or loss	Statement of cash flows
<p>ROU Assets: They are presented either:</p> <ul style="list-style-type: none"> - Separately from other assets (e.g., owned assets) <p style="text-align: center;">OR</p> <ul style="list-style-type: none"> - Together with other assets as if they were owned, with disclosures of the balance sheet line items that include ROU Assets and their amounts <p>ROU Assets that meet the definition of investment property are presented as investment property</p>	<p>Depreciation and Interest:</p> <p>Depreciation on Right of use asset and interest expense on lease liabilities are presented separately (i.e., they CANNOT be combined).</p> <p>This is because interest expense on the lease liability is a component of finance costs.</p>	<p>Principal portion of the lease liability:</p> <ul style="list-style-type: none"> - These cash payments are presented within financing activities <p>Interest portion of the lease liability:</p> <ul style="list-style-type: none"> - These cash payments are presented within financing activities <p>Short-term leases and leases of low-value assets:</p> <ul style="list-style-type: none"> - Lease payments pertaining to them (i.e., not recognised on the balance sheet as per Ind AS 116) are presented within operating activities.
<p>Lease Liabilities:</p> <p>They are presented Separately from other liabilities under the head Financial Liability.</p>		<p>Variable lease payments not included in the lease liability:</p> <ul style="list-style-type: none"> - These are also presented within operating activities

PART 5 – RECOGNITION AND MEASUREMENT OF LEASE CONTRACT IN THE BOOKS OF LESSOR

A '**lessor**' is defined as an entity that provides the right to use an **underlying asset** for a period of time in exchange for consideration.

Classification of Lease for Lessor:

1. **An Operating Lease** is a lease other than a finance lease.
2. **A Finance Lease** is a lease that **transfers substantially all the risks and rewards** incidental to ownership of an asset. Legal title may or may not eventually be transferred.

At inception, lessors shall classify the lease contract as FINANCE LEASE or OPERATING LEASE.

1. FINANCE LEASE

Situations and Indicators of Finance Lease

INDAS 116 outlines examples of **situations** that would normally lead to a lease being classified as a **finance lease**:

1. **Ownership:** The **lessor transfers ownership** of the asset to the lessee by the end of the lease term. (Hire Purchase)
2. **Purchase Option:** The lessee **has the option to purchase the asset at a price** that is expected to be **sufficiently lower** than the fair value at the date of the option exercisability. It is reasonably certain, at the inception of the lease, that the option will be exercised
3. **Lease Term:** The **lease term is for the major part (at least 75%) of the economic life** of the asset even if the title is not transferred.
4. **PV of MLP:** At the inception of the lease the **present value of the minimum lease payments** amounts to at least substantially **(at least 90%)** all of the **fair value** of the leased asset.
5. **Specialised Asset:** The leased assets are of such a specialized nature that **only the lessee can use them without major modifications. (i.e. customized asset for lessee's use)**

KEY CONCEPTS FOR UNDERSTANDING LESSORS ACCOUNTING

'Gross investment in the lease' (GIL) = Initial Down Payment + Annual Lease Payments + GRV + UGRV	
'Net investment in the lease' (NIL)	(PV of GIL) PV of (DP + Lease Payments + UGRV) - Initial Direct Cost
'Unguaranteed residual value' (Total Estimated Residual Value less GRV)	Total Estimated Residual Value (-) GRV

ACCOUNTING FOR FINANCE LEASE

Non-dealer Lessor	Dealer or Manufacturer Lessor
<p>Initial Recognition</p> <p>Lease Receivable A/c Dr. (Net Invst. in Lease) Bank A/c Dr. (Down Payment) To Asset (PPE) A/c (Carrying Amt.) Difference in above entry is transfer to P&L a/c</p> <p>Year End:</p> <p>Lease Receivable A/c Dr. To Finance Income (P&L) A/c</p> <p>Bank A/c Dr. To Lease Receivable A/c (Collection of Lease Rent)</p>	<p>Initial Recognition:</p> <p>Dealer Lessor shall record Sale at commencement of Lease:</p> <p>Lease Receivable A/c Dr. (Net Invst. in Lease) COGS A/c Dr. (Balancing Fig.) To Sale A/c (Lower of FV or PV of MLP) To Inventory A/c (Carrying Amt.)</p> <p style="text-align: center;">Sale (-) COGS = Profit on Outright Sale</p> <p>Year End:</p> <p>Same as Non-dealer Lessor's Accounting</p>

Calculation of Unearned Finance Income:

Disclose Unearned Finance Income every year:

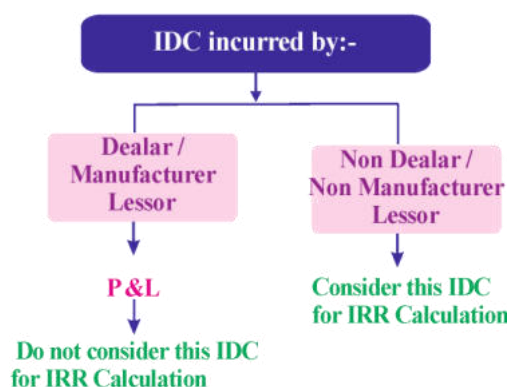
$$\text{Gross Investment in Lease (-) Net Investment in Lease}$$

Subsequent Measurement at Balance Sheet Date:

At every BS date, **Lease Receivable** shall be recognised at Current Net Investment in Lease (i.e. PV of Remaining Lease Payments + Re-estimated UGRV).

UGRV shall be reviewed at-least once in a year and if there is **any reduction** in the estimated UGRV the reduced amount shall be taken into account, this will result in reduction of Finance Income of the lessor.

(**Note:-** Remeasurement of lease receivable account will result into gain or loss transfer to Statement of Profit/Loss)



(Also Refer Practical Example 10 on Lessor's Accounting)

2. OPERATING LEASE

Particulars	Treatment
Initial Measurement	Not Required
Recognition of Lease Income	Bank A/c Dr. Deferred Rent A/c Dr. To Lease Rent Income A/c

	Recognise Income on SLM basis unless another systematic basis is more representative.
Depreciation on Asset	Depreciation A/c Dr. To Asset A/c
Initial Direct Cost incurred by Lessor	Add any initial direct costs incurred to the carrying amount of the underlying asset
Variable lease payments	Variable lease payments that do not depend on an Index or a Rate are excluded in the above treatment and are instead recognised as income when they arise. (i.e. Actual Basis)

Lease of Land and Building:

- Classify the lease of Land as **Operating Lease** since **land normally has an indefinite economic life.**
- If lease of Building is classified as Finance Lease, **the Lease Payments (including any lump-sum upfront payments) are allocated between the land and the buildings elements in proportion to the relative fair values.**

3. LEASE MODIFICATIONS

A 'lease modification' is a **change in the scope of a lease, or the consideration for a lease**, that was **not part of the original terms** and conditions of the lease (for e.g., adding or terminating the right to use one or more underlying assets, or extending or shortening the contractual lease term).

Finance Lease Modification		Operating Lease Modification
Separate Lease	Not a Separate Lease	
If both criteria are met , a lessor would account it as separate New Lease: a) Additional Rights to use are Granted & b) At Standalone Price	<u>Case 1: - Conversion from Finance Lease into Operating Lease</u> <ul style="list-style-type: none"> No Retrospective Changes Transfer CA of Lease Receivable to Asset A/c Asset A/c Dr. To Lease Receivable A/c <u>Case 2: Other Modification</u> (Change in Lease Term or Lease Payments) Remeasure Lease Receivable A/c with new Terms at New Discount rate & transfer the difference in P&L A/c	A lessor shall account for a modification to an operating lease as a new lease from the date of the modification , considering any prepaid or accrued lease payments relating to the original lease as part of the lease payments for the new lease.

PART 6 - SUB LEASES

A 'Sub-lease' is defined as a transaction for which an underlying asset is **re-leased** by a lessee (**intermediate lessor**) to a third party, and the lease ('head lease') between the head lessor and lessee remains in effect.

Original Lease is Called - **Head Lease**

Original Lessee who has given the asset on sub-lease is called - **Intermediate Lessor**

Example - There are two lease agreements

1. Mr. Vishal has given an Asset on Lease to Mr. Jai (**this is Head Lease**)

Mr. Vishal is Lessor and Mr. Jai is Lessee

2. Mr. Jai sub-leased the same asset to Mr. Ravi (**Sub-Lease**)

Mr. Jai is intermediate lessor and Mr. Ravi is Lessee

Here we need to understand the Accounting in the books of Mr. Jai (i.e. Original Lessee or Intermediate Lessor).

Accounting of Sub-lease in the books of Intermediate Lessor depends on the nature of Head Lease-

1. **When the head lease is a short-term lease** and Intermediate Lessor has opted for exemption, then the **sublease is classified as an operating lease**, this is because the Intermediate lessor has not recognised any ROU Asset and Lease Liability in its books under Head Lease. Therefore, intermediate can never show the sub-lease as Finance Lease
2. **When the head lease has been recognised by intermediate Lessor in its books as ROU Asset and Lease Liability** then treat the sub-lease as follows:

If the sublease is classified as a 'Finance Lease'	If the sublease is classified as an 'Operating Lease'
<ul style="list-style-type: none"> • The original lessee shall de-recognises the ROU Asset and continues to account for the original lease liability in accordance with the lessee accounting model. • The original lessee shall recognises Lease Receivable A/c at Net investment in sublease (NIL) and evaluates it for impairment. 	<ul style="list-style-type: none"> • The original lessee continues to account for the lease liability and ROU asset. • Recognise Sub-lease Rent on SLM basis.

Presentation in the Financial Statements

- Intermediate lessors are **not permitted to offset lease liabilities and lease assets** that arise from a head lease and a sublease, respectively.
- Similarly, intermediate lessors are **not permitted to offset depreciation and interest expenses & lease income** relating to a head lease and a sublease of the same underlying asset, respectively.

PART 7 – SALE & LEASE BACK

A **sale and leaseback transaction** involves the sale of an asset and the leasing the same asset back. In this situation, a seller becomes a lessee and a buyer becomes a lessor.

SALES AND LEASE BACK involves two transactions -

1. Sale of Asset by Seller Lessee to Buyer Lessor.
2. Lease Transaction (Already Understood earlier)

Sale Transactions (Very Important to Understand):

- First of all, determine is there an actual sale purchase of Asset.
- As per Ind AS 115, Sale and Purchase can be recognised only **when control is transferred** i.e. when substantial risk and rewards are transferred.
- Hence, there would be two case scenarios as under:

If Control is Transferred (Operating Lease Back)	If Control is NOT transferred (Finance Lease Back)
If the control of an underlying asset is passed to the buyer-lessor, the transaction is accounted for as a ' sale or purchase ' of the asset and a ' lease '.	If the control of an underlying asset is NOT passed to the buyer-lessor, both the seller-lessee and the buyer-lessor account for the transaction as a ' financing transaction '. Therefore IndAS 109 will be applied instead of IndAS 116.

(a) Accounting of Sale and Lease Back when Control is transferred:

Books of Buyer (Lessor)	
The buyer-lessor accounts for the purchase of the asset in accordance with other Ind ASs based on the nature of the asset (for e.g., Ind AS 16 for property, plant and equipment).	
Books of Seller (Lessee)	
Step 1	Calculate the Ratio: $\frac{\text{PV of Lease Payment (LP)}}{\text{Fair Value (FV) of Asset}}$
Step 2	Calculate the Recognise the Lease Liability: PV of Lease Payment at Appropriate Discount Rate
Step 3	Recognise the ROU Assets at the following amount: ROU Asset = $\frac{\text{CA} \times \text{Pv of LP}}{\text{FV of Asset}}$ + Down Payment under case 3 below
Step 4	Recognise the Gain/Loss on Transferred Part of the Asset Sold. Total Gain = Fair Value - Carrying Amount of Asset Gain (loss) is divided into two parts: a. Gain on transferred portion of Asset b. Gain on retained portion of Asset The seller-lessee shall recognise only the on transferred part by deducting the gain on retained part from Total Gain.

	Gain on Retained Part = $\frac{\text{Total Gain} \times \text{PV of LP}}{\text{Fair Value of Asset}}$		
Journal Entry in the books of seller	Cash/Bank A/c Dr. ROU Asset A/c Dr. To PPE A/c (Carrying Amt.) To Gain on transfer of Right A/c To Lease Liability A/c (PV of LP) To Loan A/c (Refer Case 2 below)		
	CASE 1 Sale Value = Fair Value	CASE 2 Sale Value is More than Fair Value	CASE 3 Sale Value is less than Fair Value
		Sale Value - Fair Value = Loan Taken	Fair Value - Sale Value = Down Payment
Present Value of Lease Payments	Total PV of all Future Payments	Total PV (-) Loan Amount	PV of all Future Payments
Any Loan Element?	No	Yes (SV - FV)	No
Total Gain/Loss	FV - CA	FV - CA	FV - CA
Any Adjustment in ROU?	No	No	FV less Sale Value is treated as Down Payment & added to ROU
Practical Examples	Practical Example 12	Practical Example 13	Practical Example 14

(b) Accounting of Sale and Lease Back when Control is not transferred:

Treat the entire transaction as Finance Arrangement by Seller Lessee from buyer Lessor and apply Ind AS 109 accounting as under: **(Refer Practical Example 11)**

Seller-lessee	Buyer-lessor
<ul style="list-style-type: none"> Do not de-recognise the Asset sold. Recognise Financial Liability (Loan) equal to sale proceeds. Recognise annual finance charges on above financial liability based on appropriate discount rate. The discount rate (IRR) should be the rate at which the Present value of future outflows should be equal to current inflow from sale proceeds. 	<ul style="list-style-type: none"> Do not recognise the Asset Purchased from Seller Lessee. Recognise the Financial Asset (Loan/Advance Given) at the amount equal to transfer proceeds. Recognise annual finance income on above financial asset based on appropriate discount rate.

PART 8 – TRANSITION APPROACH

An entity shall apply Ind AS 116 for annual reporting periods beginning on or after **01 April 2019**.

For the purposes of the requirements of this 'Transition' section, the **date of initial application is the beginning of the annual reporting period** in which an entity first applies Ind AS 116.

For Example - If entity applies IndAS wef FY 19-20, the Transition date means date of initial application and it will be 01.04.2019.

There is a practical expedient provided which permits lessees and lessors to make an election of not reassessing whether existing contracts contain a lease as defined under Ind AS 116.

Transition Options for Lessees - Under Previous GAAP, Lessee may have applied lease contract either as Operating Lease or Finance Lease and now both of these approaches are not available under Ind AS 116. Instead Ind AS 116 requires the lessee to recognise ROU Asset and Lease Liability at PV of Lease Payments.

Now for transition to Ind AS 116, Lessees have two options:-

1. **Apply Full Retrospective Approach**
2. **Apply Modified Retrospective Approach**

Let's discuss the Transition treatment in the books of Lessees:-

Full Retrospective Approach

Retrospectively to each prior reporting period presented, applying IndAS 8, i.e., an entity applies Ind AS 116 as if it had been applied since the inception of all lease contracts that are presented in the financial statements.

If Ind AS 116 is applied at 01 April 2019, this means that, in the 31st March 2020 financial statements, the comparative period to 31 March 2019 must be restated (assuming that this is the only comparative period presented).

A restated opening balance sheet at 01 April 2018 will also need to be disclosed as required by Ind AS 1.

Hence, the Balance Sheets for 3 different dates will be presented:

As at 31st March 2020, 31st March 2019 & 1st April 2018.

In simple words,

- Apply Ind AS 116 to all Lease contracts appearing on Transition Date i.e. 01.04.2018 **in such a way that Ind AS 116 would have been applied from the very inception of the lease.**
- Under the full retrospective approach, the lease liability and the ROU asset are measured on the commencement date using the incremental borrowing rate **at lease commencement date.**
- Transfer the **difference** if any arising on application of transition provision to **Retained Earnings as on 01.04.2018.**

Modified Retrospective Approach

Leases Previously Classified as Operating Leases under IND AS 17 or Previous GAAP	Leases Previously Classified as Finance Leases under IND AS 17 or Previous GAAP
<ul style="list-style-type: none"> • Do not restate the comparative figures. • Recognise the cumulative effect of the Ind AS 116 as on Initial Application date i.e. 01.04.2019 or any other later application date. • Recognise Lease Liability at PV of Remaining Lease Payments, discounted using the lessee's incremental borrowing rate at the date of initial application. • Recognise ROU Asset on a lease by lease basis at either - <ul style="list-style-type: none"> (a) Alternative 1 - Its carrying amount as if IndAS 116 had always been applied since the commencement date, but using a discount rate based on the lessee's incremental borrowing rate at the date of initial application OR (b) Alternative 2 - An amount equal to the lease liability which is recognised at Initial application date. • Under Alternative 1, the difference between the Lease Liability Amount and ROU Asset Amount shall be transferred to Opening retained earnings. 	<ul style="list-style-type: none"> • The carrying amount of the ROU asset and the lease liability at the date of initial application shall be the carrying amount of the lease asset and lease liability immediately before that date measured applying Ind AS 17. • For such leases, a lessee shall account for the ROU asset and the lease liability applying Ind AS 116 from the date of initial application i.e. 01.04.2019 or any later date from which IndAS 116 is applied. • Thus, a lessee will not change its initial carrying amounts for assets and liabilities under finance leases existing at the date of initial application of IndAS 116.

KEY DIFFERENCES BETWEEN IND AS 116 AND AS 19

The significant differences between Ind AS 116 and AS 19 are given below:

Sr. No.	Particulars	Ind AS 116	AS 19
1	Lease definition	Under Ind AS 116, the definition of lease is similar to that in AS 19. But, in Ind AS 116, there is substantial change in the guidance of how to apply this definition. The changes primarily relate to the concept of 'control' used in identifying whether a contract contains a lease or not. Ind AS 116 provides detailed guidance on whether an arrangement contains a lease or whether there are non-lease / service components within the arrangement.	Under Ind AS 116, the definition of lease is similar to that in AS 19. However, guidance part given therein is different.
2	Modifications	Ind AS 116 brings in comprehensive prescription on accounting of modifications in lease contracts. It permits leases, as a practical expedient, not to assess whether the rent concessions that occur as a direct consequence of COVID 19 pandemic and meet specified conditions are lease modifications and instead, to account for those rent concessions as if they were not lease modifications.	No such comprehensive coverage is there
3	Scope	Ind AS 116 has no such scope exclusion	AS 19 excludes leases of land from its scope
4	Definition	Ind AS 116 makes a distinction between 'inception of lease' and 'commencement of lease'	No such distinction has been made in AS 19
5	Classification	Ind AS 116 eliminates the requirement of classification of leases as either operating leases or finance leases for a lessee and instead, introduces a single lessee accounting model which requires lessee to recognise assets and liabilities for all leases unless it applies the recognition exemption (for leases of low value assets or short- term	AS 19 requires a lessee to classify leases as either finance leases or operating leases

		leases)	
6	Sale & Leaseback transactions	In Ind AS 116, the approach for computation of gain/loss for a completed sale is different. The amount of gain/loss should reflect the amount that relates to the right transferred to the buyer-lessor.	As per AS 19, if a sale and leaseback transaction results in a finance lease, excess, if any, of the sale proceeds over the carrying amount shall be deferred and amortised by the seller-lessee over the lease term in proportion to depreciation of the leased asset.
		Ind AS 116 requires a seller-lessee and a buyer-lessor to use the definition of a sale as per Ind AS 115, Revenue from Contracts with Customers to determine whether a sale has occurred in a sale and leaseback transaction. If the transfer of the underlying asset satisfies the requirements of Ind AS 115 to be accounted for as a sale, the transaction will be accounted for as a sale and a lease by both the lessee and the lessor. If not, then the seller-lessee shall recognise a finance liability and the buyer-lessor will recognise a financial asset to be accounted for as per the requirements of Ind AS 109, Financial Instruments.	AS 19 does not contain such specific requirement
7	Treatment of initial direct costs Finance lease - lessor accounting Non-manufacturer/ Non-dealer Manufacturer/	Interest rate implicit in the lease is defined in such a way that the initial direct costs included automatically in the finance lease receivable. Same as per AS 19 seller	Either recognised as expense immediately or allocated against the finance income over the lease term. Recognised as expense

	Dealer Operating lease- Lessor accounting	Added to the carrying amount of the leased asset and recognised as expense over the lease term on the same basis as lease income.	immediately. Either deferred and allocated to income over the lease term in proportion to the recognition of rent income, or recognized as expense in the period in which incurred
8	Initial direct costs	Ind AS 116 contains clearer definition of 'initial direct costs, such as commissions and legal fees, are often incurred by lessors in negotiating and arranging a lease. Ind AS 116 define initial direct costs as 'Incremental costs of obtaining a lease that would not have been incurred if the lease had not been obtained, except for such costs incurred by a manufacturer or dealer lessor in connection with a finance lease.' Further, definition of the term 'interest rate implicit in the lease' has been modified in Ind AS 116.	Different guidance given
9	Presentation	As a consequence of introduction of single lease model for lessees, there are many changes in the presentation in the three components of financial statements viz. Balance sheet, Statement of Profit and Loss, Statement of Cash flows.	Different guidance given
10	Disclosure	There are a number of changes in the disclosure relating to qualitative aspects of leasing transactions. For e.g., Entities are required to disclose the nature and risks arising from leasing transactions. Also, in case of lessor, there are changes in the disclosure of maturity analysis of leases payments receivable.	Different guidance given

Student Notes:-



Student Notes:-

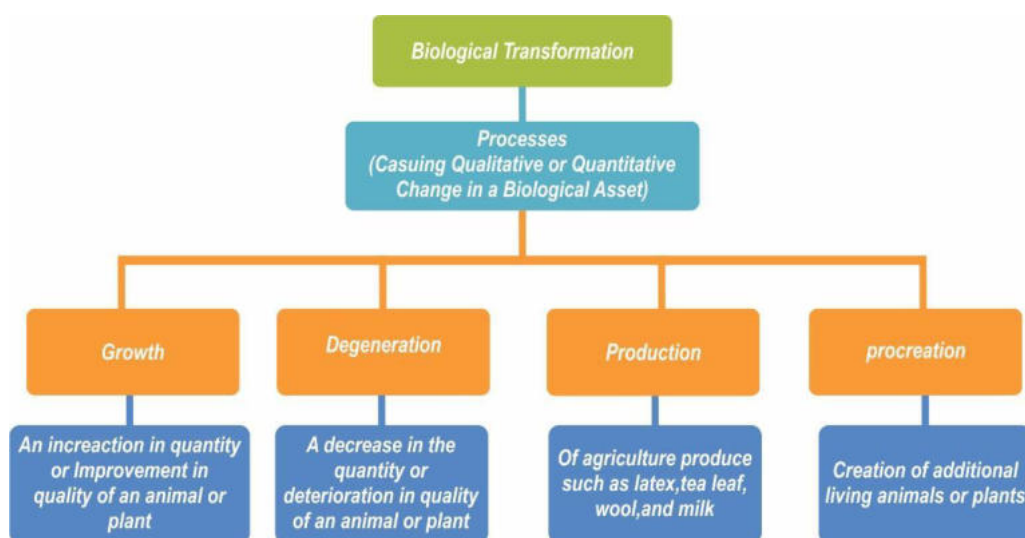


IND AS 41 AGRICULTURE

“Definiteness of Purpose is the Starting Point of all achievement”

1. DEFINITIONS

- (a) **Biological Asset** is defined as a living animal or plant.
- (b) **Agricultural Produce** is the harvested product (can say “Raw Material without further processing) of the entity's biological assets.
- (c) **Biological Transformation** comprises the processes of growth, degeneration, production, and procreation **that cause qualitative or quantitative changes** in biological asset.
- (d) **Agriculture Activity** means Management of biological transformation of biological assets for Sale or Conversion into agriculture produce or additional biological assets.



(e) **HARVEST** is the **detachment** of produce from a biological asset or the cessation of a biological asset's life processes.

(f) **BEARER PLANT** may be defined as a living plant that:

- i. is used in the production or supply of **agricultural produce**;
- ii. is expected to bear produce for **more than one period**; and
- iii. has a remote likelihood of being sold as agricultural produce, except for incidental scrap sales.

For example, tea bushes, grape vines, oil palms and rubber trees, usually meet the definition of a bearer plant and are outside the scope of Ind AS 41 and covered under Ind AS 16.

These are Agriculture Activity	These are Not Agriculture Activity
<ul style="list-style-type: none"> ● Pharma companies grow their own plants in order to produce and sale drugs. ● If a company maintains Cows and Produces Milk then this is an agricultural activity ● Fish Farming ● Harvesting Grapes ● A managed breeding programme carried out to produce animals for sale 	<ul style="list-style-type: none"> ● ZOO: (safari, recreational park, riding hall, etc.) ● Security Dogs and Animals ● Fishing in River, Ocean etc ● Growing Grape vines (its is a bearer plant) ● Producing wine - Inventory (Ind AS 2) ● Natural breeding that takes place in animals used in recreational activities is not a managed activity

2. APPLICABILITY & NON - APPLICABILITY

(1) Ind AS 41 applies to the following:

- a. Biological Assets relating to Agriculture activity
- b. Agricultural Produce at the point of harvest relating to agriculture activity
- c. Government Grants relating to agriculture activity

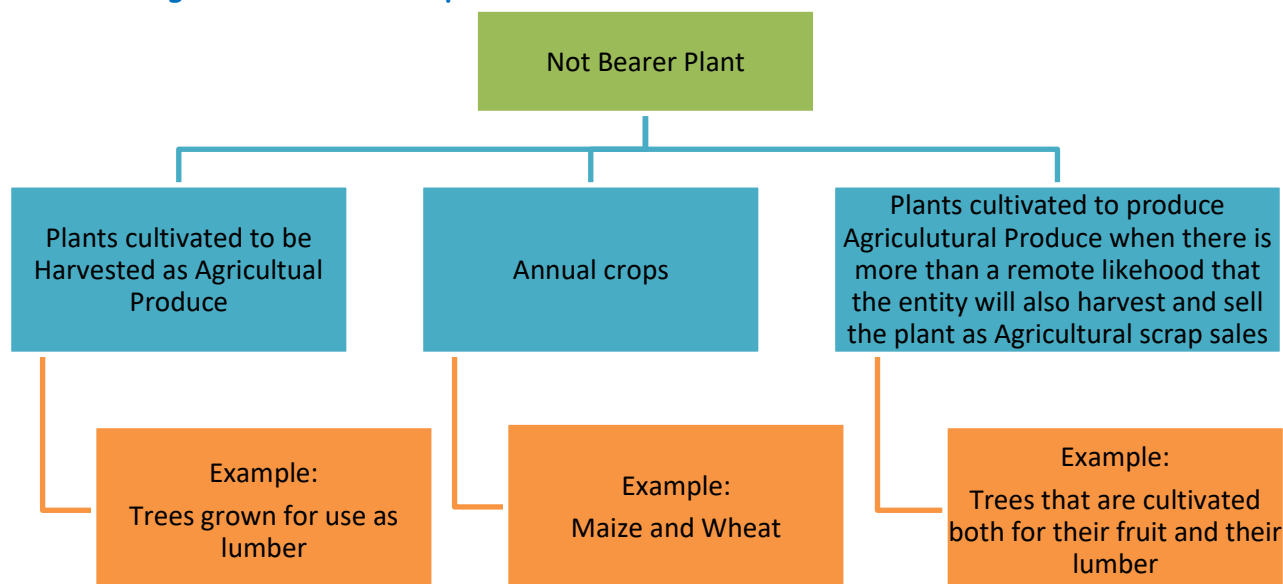
Author's Note:

At the point of harvest means Only for the First Time after Harvesting.

(2) Ind AS 41 does not applies to the following:

- (a) Land related to agricultural activity: for example, the land on which the biological assets grow, regenerate and/or degenerate (Ind AS 16 may be applied);
- (b) Bearer plants related to agricultural activity. Such bearer plants covered within the scope of Ind AS 16. However, this Standard applies to the produce on those bearer plants.
- (c) Government grants related to bearer plants (Ind AS 20 will be applied).
- (d) Intangible assets associated with the agricultural activity, for example licenses and rights are covered under Ind AS 38.
- (e) Right of Use Assets arising from a lease of Land related to Agriculture Activity (IND AS 116 LEASES)

The following are NOT bearer plants:



AUTHOR'S NOTE:

This Standard is applied to agricultural produce, which is the **harvested product** of the entity's biological assets, **only at the point of harvest**. Thereafter, Ind AS 2 or another applicable Standard is applied.

The table below provides examples of biological assets, agricultural produce, and products that are the result of processing after harvest:

Biological assets	Agricultural produce	Products that are the result of processing after harvest
Sheep	Wool	Yarn, carpet
Trees in a timber	Felled Trees	Logs, lumber
Dairy Cattle	Milk	Cheese
Pigs	Carcass	Sausages, cured hams
Cotton plants	Harvested cotton	Thread, clothing
Sugarcane	Harvested cane	Sugar
Tobacco plants	Picked leaves	Cured tobacco
Tea bushes	Picked leaves	Tea
Grape vines	Picked grapes	Wine
Fruit trees	Picked fruit	Processed fruit
Rubber trees	Harvested latex	Rubber products

3. RECOGNITION OF ASSETS

Entities are required to recognise a **Biological Asset or Agricultural Produce at the Point of Harvest when, and only when, ALL** of the following conditions are met:

- (a) The entity **CONTROLS** the asset as a result of past events;
(Control over biological assets or agricultural produce may be evidenced by **legal ownership or rights to control**, for example legal ownership of cattle and the branding or otherwise marking of the cattle on acquisition, birth, or weaning.)
- (b) It is probable that **FUTURE ECONOMIC BENEFITS** associated with the asset will flow to the entity;
(Future economic benefits are expected to flow to the enterprise from its ownership or control of the asset) and
- (c) The **FAIR VALUE OR COST** of the asset can be **measured reliably**.

4. MEASUREMENT & ACCOUNTING

1. Biological Assets

Initial Recognition	At Fair Value less Cost to Sell (FVLCTS)	
How to Calculate FVLCTS	Sales Price of Biological Asset (-) Transportation Cost to transport the asset born by seller (-) Cost to sell (Transaction cost like brokerage/auctioneer's fees born by seller)	
Journal Entry at Initial Recognition	Biological Assets A/c Dr. (FVLCTS) Fair Value Loss A/c Dr. (balancing fig. P&L a/c) To Bank A/c (Payment to buy Asset) To Fair Value Gain A/c (balancing fig. P&L a/c)	
	<u>New Born Baby Animal (Eg. Calf) at FVLCTS on Date of Birth:</u> Biological Asset A/c Dr. To Gain on New Born A/c	
Payment to buy Asset	Purchase Price of Biological Asset (it could be different from market price) (+) Transport Cost born by buyer to transport the asset to entity's farm (+) Transaction Cost (brokerage)	
Subsequent Measurement at B/s date	At Revised Fair Value less Cost to Sell. Any change due to remeasurement is Fair Value Gain or Loss and transfer to Profit and Loss A/c.	
Conversion of Biological Assets into Agriculture Produce	Eg. Slaughtering of Animal to get carcass <u>On Conversion:</u> Agriculture Produce A/c (Inventory) Dr. (FVLCTS) Loss A/c Dr. (balancing fig.) To Bank A/c (Cost of conversion) To Biological Asset A/c (Carrying Amt.) To Gain A/c (balancing fig.)	
	<u>On Sale of Inventory:</u> COGS A/c Dr. (Carrying Amt.) To Agriculture Produce (Inventory) A/c	
	Bank A/c Dr. (Sale Proceeds) To Revenue from Sale A/c	
Derecognition of Biological Assets due to Sale or Death	Bank A/c Dr. (Net Amt. received on sale) Loss on Sale/Death Dr. (balancing fig.) To Biological Asset A/c (Carrying Amt.) To Gain on Sale of Biological Asset A/c (bal. fig.)	
Expenses on Biological Assets	Expenses incurred to maintain biological assets for their growth such as breeding cost, food cost, fertilizers etc. are transfer to Profit and Loss A/c	

2. Agriculture Produce at Point of Harvest

Initial Recognition	At Fair Value less Cost to Sell (FVLCTS)	
Journal Entry at	Agriculture Produce A/c Dr. (FVLCTS)	

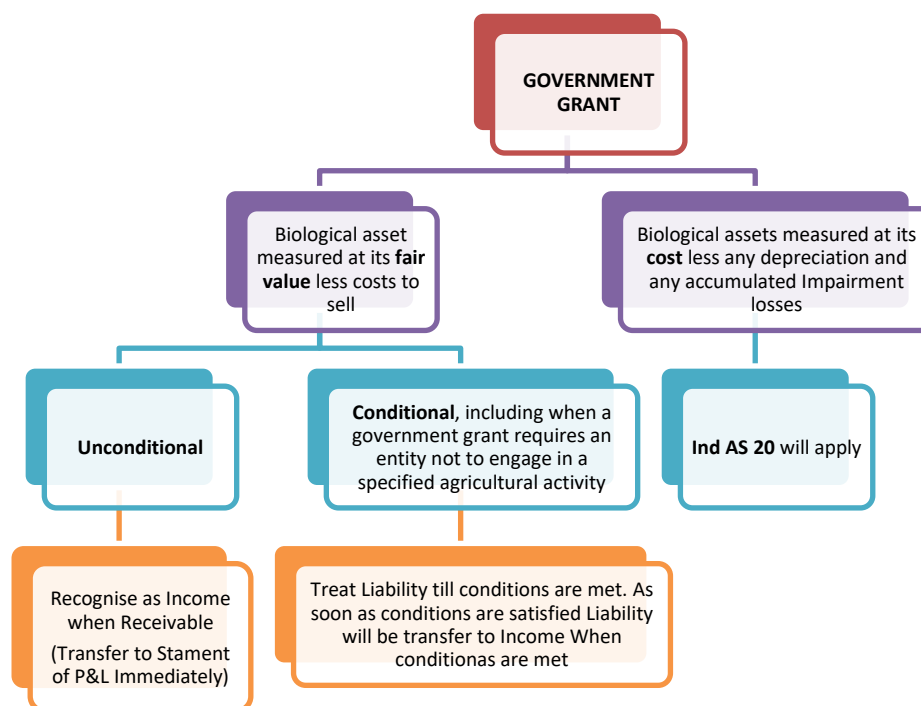
Initial Recognition	To Fair Value Gain A/c
Subsequent Measurement at B/s date	Agriculture Produce will be treated as Inventory and Ind AS 2 shall be applicable for subsequent measurement. Cost of such inventory for the purpose of Ind AS 2 shall be previous measurement (i.e. FVLCTS) under Ind AS 41

3. Other Important Points

- 1) The fair value less cost to sell of a biological asset can change **due to both physical changes and price changes** in the market.
- 2) It is true that the general rule in Ind AS 41 Agriculture is to measure all biological assets at **fair value less costs to sell**. However, there are **few exceptions**:
 - a) The biological asset is **NOT a part of agricultural activity such as** guard dogs, fish caught in the ocean, Zoo etc.
 - b) The biological asset is **a bearer plant**.
 - c) **The fair value is not reliably measurable**

When the fair value cannot be measurable, you can measure the asset at its **cost less accumulated depreciation**.

5. GOVERNMENT GRANTS



- When Govt. Grant is received for Biological Asset which is measured at Fair Value less costs to sell then **do not ever think of deducting the grant amount from carrying amount** of biological assets.
- Apply Ind AS 20 on Grants relating to "Biological assets which are not related to agricultural activity" or "Biological assets relating to agricultural activity but measured at cost".

11

IND AS 23 BORROWING COSTS

1. MEANING of BORROWING COSTs

Borrowing Cost is the:

- (a) Interest and
- (b) Other cost

that is incurred by an enterprise in connection with borrowing of funds.

The following exclusive points should be considered for the purpose of borrowing cost:

- Interest Exp. calculated **using the effective interest method** as described in IND AS - 109 Financial Instruments.
- Amount of **Interest (finance charges)** should also be included as a part of borrowing cost which is paid or payable on **lease liability** recognized in accordance with IND AS 116).
- **Exchange Difference** arising from Foreign Currency Borrowings to the extent of difference in Interest cost (IND AS - 21).

Author's Note:

1. Dividend on **redeemable preference share** capital is borrowing cost.
2. **Equity** Dividend or Dividend on **irredeemable preference** share capital is **not borrowing cost**.
3. Cost of issue of equity capital is not borrowing cost.

(Refer Practical Example 1 for Effective Rate of Interest)

2. FOREIGN EXCHANGE FLUCTUATION

(a) Foreign Exchange Loss on Foreign Currency borrowing:

Borrowing costs shall be lower of:

- (i) Actual Exchange Loss; or
- (ii) Saving in Interest due to foreign currency loan (difference of interest cost on local currency loan and foreign currency loan)

Step 1	Calculate Actual Interest Cost on foreign currency loan (apply closing exchange rate to convert into functional currency)
Step 2	Calculate Saving in Interest Cost due to foreign currency loan as under: Interest on Loan if taken in India XXX (-) Actual Interest on Loan on FC Loan XXX
Step 3	Calculate Actual Exchange Loss due to increase in Foreign Exchange Rate
Step 4	Lower of Step 2 or Step 3 will be Borrowing cost

(b) Foreign Exchange Gain on Foreign Currency borrowing:

- (i) **General rule:** transfer to profit and loss directly, it is not adjustment to borrowing cost.
- (ii) **Exchange gain in subsequent years after previous exchange loss:** The **Gain to the extent of the loss previously recognized** as an adjustment should also be recognised as an adjustment to interest i.e. deducted from borrowing cost.

(Refer Practical Example 2 & 3)

3. MEANING OF QUALIFYING ASSETS

Qualifying Asset means:

- An ASSET
- that takes **Substantial period of time**
- to get ready for intended **use or sale**.

Note 1: Normally a period of **12 months is considered to be the substantial period of time**. However it is not defined, it can be considered as per the judgement of the entity. If question is silent we can assume that asset is taking substantial period.

Note 2: **Inventories** that are manufactured or produced in **large quantities on a repetitive basis** and that **takes substantial period of time** to get ready to sale **may not be qualifying asset**.

4. TREATMENT OF BORROWING COSTS

As per IND AS - 23, amount of borrowing cost which is directly attributable to:

- **Acquisition; (A)**
- **Construction; (C) or**
- **Production (P)**

of any Qualifying Asset is Capitalized.

If any borrowing cost is **not having any connection with Q.A.** than such amount should be transfer to **Profit and Loss account**.



5. TYPES OF BORROWINGS & BORROWING COSTS

There can be two types of borrowings which are as follows:-

- A. **Specific Borrowing:** Loan is taken for specific qualifying asset
- B. **General Borrowing:** Loan is not for any specific qualifying asset. It can be used for any purpose or for multiple assets.

Specific Borrowing Cost	General Borrowing Cost
Entire borrowing cost shall be capitalised from the date of 1 st expenditure on qualifying asset. (i.e. start capitalization of entire borrowing cost from the date of 1 st expenditure irrespective of expenses on different dates)	Capitalisation shall be done expenditure wise (i.e. from the date of each expenditure on qualifying asset). To capitalize the borrowing cost we have to calculate weighted average of the borrowing rate (WABR) as under: $\frac{\text{Total Borrowing Cost incurred during the year} \times 100}{\text{Total Borrowings O/s during the Year}}$ $\text{Expenditure on QA} \times \text{WABR} (\%) \times \text{Time Weight}$
If expenditure on qualifying asset is incurred out of specific as well as general borrowed funds then we shall first use specific borrowings if such borrowing is available on the date of expenditure.	
(Refer Practical Examples 4 to 10)	

Author's Note:

In computing the capitalisation rate for generally borrowed funds, the entity should **exclude** borrowing costs on borrowings which are specifically used for the purpose of obtaining a qualifying asset until that specific asset is ready for its intended use or sale.

Once such specific asset is ready for its intended use or sale, borrowing costs related to borrowings of such asset shall be considered as **part of general borrowing costs** of the entity and be used for computation of capitalisation rate on general borrowings.

EXPENDITURE TO WHICH CAPITALISATION RATE IS APPLIED:

Expenditure Already incurred on QA (including Borrowing cost capitalized till last year)	XXX
Add: Expenditure incurred in CY (in Cash or payable)	XXX
Less: Progress Payments or Grants received during the CY	(XXX)
Total Expenditure on which WABR shall be applied	XXX

IMPORTANT POINTS:

- (a) Once borrowing cost is capitalized there may be some possibility that recoverable amount of asset is lower than the carrying amount of asset hence such asset can be tested for impairment.
- (b) As per IND AS 23, if any enterprise has **earned temporary income** by **investment of unused borrowed funds** then amount of temporary income **should be adjusted against total borrowing**

cost and only thereafter principals of recognition should be applied.

6. CAPITALIZATION of BORROWING COSTS:

Commencement of Capitalisation:	<p>Start capitalizing Borrowing cost from the later of following dates:</p> <ol style="list-style-type: none"> Date of start of expenditure on A/C/P of Qualifying Asset Date of start of incurring interest Date when necessary activities started (Such as technical or administrative work prior to commencement of physical construction)
Suspension of Capitalisation	<p>Capitalization of Borrowing Costs shall be suspended during the extended periods in which Active Development is interrupted.</p> <p>Note: Borrowing costs which are related to the suspension period should be transferred to Profit and loss.</p> <p>However, if necessary activities are interrupted due to unavoidable reason (or) temporary delays is necessary then no need to suspend the capitalization of Borrowing cost. (eg. High water level during construction of bridge)</p>
Cessation of Capitalisation	<ul style="list-style-type: none"> Capitalization should cease when substantially all the activities necessary to prepare the qualifying asset for its intended use or sale are complete. Cessation to take place in part if construction of qualifying asset is completed in parts and a part is capable of being used separately.

Example on Commencement of Capitalization

X Ltd is commencing a new construction project, which is to be financed by borrowing. The key dates are as follows:

- 15 May 20X1: Loan interest relating to the project starts to be incurred
- 2 June 20X1 : Technical site planning commences
- 19 June 20X1 : Expenditure on the project started to be incurred
- 18 July 20X1 : Construction work commences Identify commencement date.

SOLUTION:

In the above case, the three conditions to be tested for commencement date would be: Borrowing cost has been incurred on: 15 May 20X1

Expenditure has been incurred for the asset on: 19 June 20X1

Activities necessary to prepare asset for its intended use or sale: 2 June 20X1 Commencement date would be the date when the above three conditions would be satisfied in all i.e., 19 June 20X1.

Example of Suspension of Capitalisation

Construction suspended between October 20X1 to January 20X2 during which period certain heavy construction equipments under use was shifted to another site.

In this case, capitalization of borrowing costs needs to be suspended since active development is interrupted.

Example on Cessation of Capitalisation:

H Limited, a real estate company, gives immovable property on rent. It has completed on May 31, 20X1, a commercial complex consisting of various offices that could be rented out. It expects that the commercial complex will be completely rented out by June 30, 20X1. However, due to adverse market conditions, only 10% of the commercial complex could be rented out by its reporting date of March 31, 20X2. H Limited wants to capitalise the eligible borrowing costs incurred up to March 31, 20X2.

H Limited should capitalise borrowing costs only up to May 31, 20X1. The borrowing cost incurred thereafter cannot be capitalised as the asset was ready for its intended use on May 31, 20X1. The fact that only a small portion could be rented out by March 31, 20X2, is immaterial.

Example on Cessation of Capitalisation on some part of Asset:

An entertainment park consisting of several rides and facilities, each of which can be used individually, is an example of a qualifying asset for which each part is capable of being usable while construction continues on other parts. On the other side in a case of an industrial undertaking such as a steel mill, all parts have to be completed before any earlier completed part can be put to use.

7. OTHER RELEVANT CONCEPTS

A. Capitalising borrowing cost in Group Financial Statements

- There may be a situation when the **borrowings are taken by one company and qualifying asset is developed by another company within a group.**
- Borrowing cost in the consolidated financial statements shall be capitalized only when borrowed funds are actually applied on such qualifying asset. (means check the end use of borrowed funds)
- However, **the entity carrying out the development should not capitalise any interest** in its stand-alone financial statements as **it has no borrowings.**
- If, however, the entity has **intra-group borrowings** (loan taken by subsidiary from holding) then interest on such borrowings **may be capitalised** in its stand-alone financial statements if funds are applied to qualifying asset.

B. Cessation of Capitalisation for Maturing Inventories

For maturing inventories, it is sometimes difficult to determine when the '**period of production ends**, i.e. when inventories are being held for sale as opposed to being held to mature. Consider the following example:

Example:

Whisky is 'mature' after three years, but goes on improving with age for many more years. Provided that it is consistent with the entity's business model to hold such items so that they mature further, it would seem acceptable to continue to add borrowing costs to the value of such maturing inventories for as long as it can be demonstrated that the particular item of inventory continues to increase in value solely on account of increasing age, rather than because of market fluctuations or inflation. If this cannot be demonstrated, then the inventories should be regarded as held for sale and no further borrowing costs should be capitalised.

C. Notional Borrowing Cost:

- A notional borrowing cost **cannot be capitalized.**
- Where an entity has **no borrowings and use its own cash resources** to finance the construction of property, plant and equipment, **the entity can not assume that interest** that could have been earned on that cash represents forgone benefit and could be capitalized.

12

IND AS 36

IMPAIRMENT OF ASSETS

IMPAIRMENT means Reduction in the value of Assets due to external or internal indicators such as change in technology, physical damage etc.

1. APPLICABILITY AND NON - APPLICABILITY:

A. Ind AS 36 is applicable to:

1. PPE (Ind AS 16)
2. Intangible Assets (Ind AS 38)
3. Investment Property (Ind AS 40)
4. Goodwill Acquired in Business Combinations (Ind AS 103)
5. Investments in Subsidiaries/JV/Associates if measured as Cost (Ind AS 27)

B. Ind AS 36 is Not Applicable to:

1. Inventories (as covered in Ind AS 2)
2. Contract assets and assets arising from costs to obtain or fulfill a contract (Ind AS 115)
3. Deferred tax assets (Ind AS 12)
4. Assets arising from employees benefits (Ind AS 19) (eg. Plan Assets/Investments at Fair Value)
5. Biological Assets measured at fair value less cost to sell (Ind AS 41)
(It means Biological Assets measured at Cost are subject to Impairment under this standard only i.e. under Ind AS 36)
6. Non-current assets (or disposal groups) classified as held for sale (as covered in Ind AS 105)
7. Financial Assets (within the scope of Ind AS 109 & 32) (eg. Shares, Debtors, Loans and Advances etc)

2. INDICATIONS OF IMPAIRMENT

A. External indicators for Impairment of Asset: (List is not exhaustive or conclusive)

- a) Asset's market value has declined significantly more than would be expected as a result of the passage of time or normal use.;
- b) Significant changes with an adverse effect on the entity have taken place due to change in technology, market, economy or legal environment.
- c) Market interest rates have increased during the period, and those increases are likely to affect the discount rate; and
- d) Book Value of Net Assets is more than Market Value Net Assets.

B. Internal source of information: (List is not exhaustive or conclusive)

- a) Obsolescence or Physical damage of an asset;



- b) **Asset becoming idle**, plans to dispose of an asset before the previously expected date, and reassessing the useful life of an asset as finite rather than indefinite;
- c) Plans to **discontinue or restructure the operation** to which an asset belongs,
- d) Economic **performance** of an asset is, or will be, **worse** than expected.

Indications of Impairment in case of Investment in Subsidiary; Joint Venture or Associate

- (i) The carrying amount of the investment in the separate financial statements exceeds the carrying amounts in the consolidated financial statements of the investee's net assets, including associated goodwill;

For Example: Investment Value in SFS of Holding Co. is 14.50 Lacs; Value of Net Assets including Goodwill of Sub. in CFS is 15 Lacs out of which 90% belongs to holding's share i.e. 13.50 lacs.

OR

- (ii) The dividend declared by subsidiary exceeds the total comprehensive income of the subsidiary, jointly controlled entity or associate in the period the dividend is declared.

3. IDENTIFYING AN ASSET THAT MAY BE IMPAIRED

Asset is impaired only when Carrying Amount is more than Recoverable Amount.

$$CA - RA = \text{IMPAIRMENT LOSS}$$

Mandatory Impairment Testing Annually of these Assets:	<ul style="list-style-type: none"> Intangible Assets with indefinite useful life Intangible Assets not yet available for Use. Goodwill acquired in a Business Combination
Impairment Testing only when any indication arise:	<ul style="list-style-type: none"> PPE Investment Property

4. MEASUREMENT OF RECOVERABLE AMOUNT

Recoverable Amount	Higher of Fair Value less cost to sell and Value in use.
Fair Value	Fair Value shall be calculated as per Ind AS 113
Cost to Sell	legal costs, stamp duty and similar transaction taxes , costs of removing the asset, and direct incremental costs to bring an asset into condition for its sale. But Employees termination benefits are not cost to sell.
Value in use (VIU)	Present value of the future cash flows expected to be derived from use of an asset including disposal at the end of useful life.
Discounting Rate for VIU	<ul style="list-style-type: none"> Pre-tax discount rate should be used. Discount rate can be either weighted avg. cost of capital or entity's

	incremental borrowing rate.
Estimating Future Cash Flows for VIU	<ul style="list-style-type: none"> • Reasonable and supportable assumptions should be considered • Projections should cover a maximum of 5 years unless longer period can be justified. • Future Cash Flows should not include: <ul style="list-style-type: none"> ➤ Cash inflows from receivables ➤ Cash outflows from payables ➤ Cash flows of future restructuring (including Business acquisitions to which entity is not yet committed) ➤ Cash flows expected from improving or enhancing the asset's performance ➤ Income tax receipts/payments
Foreign Currency Future Cash Flows (Refer Practical Example 1)	<p>Step 1: FC Cash flows × Discount Rate relating to country of foreign currency</p> <p>Step 2: Translate Discounted cash flows using exchange rate on the date of measurement of Value in Use.</p>
<p>Note: If FVLCTS is not determinable, then value in use is considered as Recoverable Amount If VIU is not determinable, then Recoverable amount of such asset can-not be determined. In Such case Impairment of CGU shall be done.</p>	

Example: (on Expected Cash Flows)

Calculate expected cash flows in each of the following cases:

- (a) the estimated amount falls somewhere between ₹ 50 and ₹ 250, but no amount in the range is more likely than any other amount.
- (b) the estimated amount falls somewhere between ₹ 50 and ₹ 250, and the most likely amount is ₹ 100. However, the probabilities attached to each amount are unknown.
- (c) the estimated amount will be ₹ 50 (10 per cent probability), ₹ 250 (30 per cent probability), or ₹ 100 (60 per cent probability).

SOLUTION

- (a) the estimated expected cash flow is ₹ 150 $[(50 + 250)/2]$.
- (b) the estimated expected cash flow is ₹ 133.33 $[(50 + 100 + 250)/3]$.
- (c) the estimated expected cash flow is ₹ 140 $[(50 \times 0.10) + (250 \times 0.30) + (100 \times 0.60)]$.

(Also Refer Practical Example 2)

5. IMPAIRMENT OF INDIVIDUAL ASSET

Steps to be followed for calculation and treatment of Impairment loss:

Step 1: Calculate Carrying Amount of Asset as on Balance Sheet (After charging depreciation)

Step 2: Calculate Recoverable Amount of Asset

Step 3: If Carrying Amount is higher than Recoverable Amount then difference is Impairment Loss

Step 4: Treatment of Impairment loss as under:

- If Asset belongs to Cost Model - Charge the Impairment loss to P&L A/c
- If Asset belongs to Revaluation Model - Charge the impairment loss to revaluation surplus (OCI) if available and remaining loss to P&L A/c

Step 5: Calculate Revised Carrying Amount of Asset after Impairment for the purpose of further depreciation in future. (CA before impairment - Impairment loss)

Journal Entry for Impairment Loss:

Impairment Loss A/c Dr.	Revaluation Surplus A/c (OCI) Dr.	(1 st Priority)
To Asset A/c	Profit and Loss A/c Dr.	(Balancing Fig.)
	To Impairment Loss A/c	

(Refer Practical Example 3)

Important Note:

1. If **impairment loss is more than carrying amount** of asset, then **liability should be recognised** after writing off the carrying amount.
2. Since **impairment loss is not deductible** under income tax, **Deferred Tax affect** should be calculated after impairment, since carrying amount of asset would be different from Tax Base of Asset. (Tax base means value of asset as per tax records) (Refer Practical Example 4)

6. IMPAIRMENT LOSS OF A CASH-GENERATING UNIT (CGU) INCLUDING GOODWILL & CORPORATE ASSET

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

- ☞ Always try to impair Individual Asset first for which indication of impairment exist and estimate the recoverable amount of that individual asset.
- ☞ If it is not possible to estimate the recoverable amount of the individual asset, then recoverable amount of the cash-generating unit to which the asset belongs should be determined and apply impairment testing of CGU.
- ☞ CGU may include current assets, goodwill, corporate assets and liabilities also.



- ☞ Only those Assets and Liabilities should be considered in carrying amount of CGU which are taken into account for determining Recoverable Amount (i.e. basis should be same)
- ☞ Examples of liabilities that can become part of CGU - Provision for decommissioning liabilities, specific loans taken for CGU Assets.

Example:

A company manufactures a flavored drink from Machine A and the drink can be sold only in bottles for which machine B is to be used. Here both machines can-not generate cash flows individually hence they shall be clubbed together to form a CGU.

More Examples - Magazine Titles, Buses running in a different routes

Carrying Amount of CGU:	Carrying Amount of PPEs of CGU (+) Carrying Amount of Intangible Assets of CGU (+) Carrying Amount of Current Assets of CGU (+) Carrying Amount of Goodwill allocated to CGU (+) Carrying Amount of Corporate Assets allocated to CGU
Corporate Assets:	Assets other than goodwill that helps CGU under review and other CGUs to generate Independent Cash Flows. (For Ex. Head office buildings)
How to Impair Goodwill and Corporate Assets	Goodwill and Corporate Assets doesn't generate independent cash flows hence they can-not be tested for impairment individually. Goodwill shall be allocated to different CGUs of business that are expected to benefit from the synergies of the business acquisition. Corporate Assets are allocated to different CGUs on a Reasonable basis
How to allocate Goodwill and Corporate Assets?	Goodwill shall be allocated either in the ratio given in the question (or) in the ratio of Fair Values of CGUs at the time of business acquisition. Corporate Assets shall be allocated either in the ratio given in the question (or) in the ratio of following amounts of each CGU: Carrying Amt. x Useful life (if useful life is not given then only carrying amount of CGUs can be used to find out ratio)
Un-allocable Goodwill and Corporate Assets	Apply Bottom up approach for Goodwill and Corporate Assets which are Allocable to CGUs. Apply Top-down approach for Goodwill and Corporate Assets which

	are not allocable to CGUs.
Important Note	Impairment Loss is never allocated to Current Assets or any other assets on which Ind AS 36 is not applicable

Steps to Solve the Complete Question:

Approach	Particulars	CGU 1	CGU 2	CGU 3	Total
Bottom Up	Carrying Amt of CGUs	XXX	XXX	XXX	XXXX
	(+) Allocate Goodwill	XXX	XXX	XXX	XXXX
	(+) Allocate Copr. Assets	XXX	XXX	XXX	XXXX
	Total Carrying Amount of CGUs	XXX	XXX	XXX	XXXX
	Less:				
	Total Recoverable Amt. of CGUs	XXX	XXX	XXX	XXXX
Bottom up continued	Impairment Loss of CGUs	XXX	XXX	XXX	XXX
	(-) Allocable Goodwill	XX	XX	XX	XX
	(-) then Impairment Loss allocate to that Asset which can be tested for impairment individually	XXX	XXX	XXX	XXX
	(-) Remaining Imp. Loss is allocated to all other Assets including Corporate Assets in the given ratio	XXX	XXX	XXX	XXX
Top- down	Revised Carrying Amt. of CGUs	XXX	XXX	XXX	XXX
	(+) Un-allocable Goodwill or Corporate Assets	-	-	-	XXX
	Total Carrying Amount of Entity as a whole				XXX
	(-) Recoverable Amt. of Entity as a whole				XXX
Top- down	Additional Impairment Loss for Un-allocable Goodwill and Corporate Assets only (Do not impair CGUs since they are already tested for impairment)				XXX

7. NON-CONTROLLING INTEREST – IMPACT OF UN-RECOGNISED GOODWILL

- 1) NCI means other shareholders of subsidiary co. **not having control** over subsidiary's business.
- 2) NCI is calculated by Two different Methods: -

Fair Value Method (Market Value Method)	Proportion of Net Assets Method
$\text{NCI} = \text{No. of Shares held by NCI} \times \text{Market Price per share of Subsidiary}$	$\text{NCI} = \text{Fair Value of Total Net Assets} \times \text{NCI \%}$

(Refer Practical Example 5)

- 3) When NCI is calculated by Fair Value method then Full Goodwill arise and such full goodwill is included in Carrying Amt. of CGU as well as Recoverable Amount of CGU.
- 4) However, when NCI is calculated as per Proportionate of Net Asset Method then Partial Goodwill arise which is attributable to Holding Company only, this means Goodwill attributable to NCI is not recognised and not included in carrying amount of CGU.
- 5) Recoverable amount of CGU always includes Full Goodwill. Therefore, entity shall gross up the goodwill to include NCI's portion of goodwill into the carrying amount of CGU

Apply following Steps:

Particulars	Amount
Carrying Amount of CGU	XXX
Add:	
Goodwill attributable to Holding Co. (Calculated as per Proportionate Method)	XXX
Add:	
Un-recognised Goodwill (Attributable to NCI)	XXX
<u>Goodwill attributable to Parent</u> x NCI's Share	
Parent's Share	
Total Carrying Amount of CGU	XXX
Less:	
Total Recoverable Amount of CGU as given in the Question	XXX
Impairment Loss of CGU	XXX
Allocation of Impairment Loss to Goodwill First:	
➤ Impairment Loss to Parent's Goodwill (Holding's Share)	XXX
➤ Impairment Loss to NCI's Goodwill (NCI's Share)	XXX
No need to record impairment loss of NCI's Goodwill since this goodwill was unrecognized.	
Remaining Impairment Loss attributable to other Assets shall be apportioned to Holding and NCI	XXX

(Refer Practical Example 6)



8. REVERSAL OF IMPAIRMENT LOSS

Indicators of reversal of Impairment Loss:

External -

- Asset's value has **increased significantly** during the period;
- Significant changes with an **favorable effect** on the entity have taken place due to change in **technology, market, economy or legal environment**.
- Market **interest rates** have **decreased** during the period, and those increases are likely to affect the discount rate; and

Internal -

- Asset's performance has been significantly improved. It may be **because of Cost incurred** to improve or enhance the performance or **Cost incurred to restructured the operation** during the period.
- **Economic performance** of the asset is, or will be, **better than expected**.

Goodwill:

An impairment loss recognised for goodwill shall not be reversed in a subsequent period.

Assets other than Goodwill:

If there is an Indication that shows Impairment Loss recognised earlier may no longer exists or may have decreased, then entity shall revers the impairment loss and accordingly recoverable amount is to be determined.

How to Calculate the Reversal of Impairment Loss:

Step 1: Current Carrying Amount of Asset - assume 1000/-

Step 2: Current Recoverable Amount of Asset - assume 1200/-

Step 3: Calculate Current Carrying Amount of Asset if Asset were never impaired
(assume 1150/-)

Step 4: Revised Carrying amount after reversal should be lower of Step 2 & Step 3
(Means 1150/-)

Step 5: Reversal of Impairment Loss = Step 4 - Step 1 (means 1150 - 1000 = 150)

Step 6: Current Carrying Amount (Step 1) + Reversal of I/L (Step 5) = Revised Carrying Amt.
Depreciation shall be charged on Revised Carrying Amount

(Refer Practical Example 7)

Accounting treatment of Reversal of Impairment Loss:

Asset A/c Dr.

To Impairment Loss Reversal A/c

Impairment Loss Reversal A/c Dr.

To Revaluation Surplus A/c (if available & Asset is under Revaluation model)

To Profit and Loss A/c (Balancing Fig.)

Reversal of Impairment Loss of CGU:

A reversal of an impairment loss for a cash-generating unit shall be allocated to the assets of the unit, **except for goodwill, in proportion of carrying amounts of those assets**.

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IND AS 105 - NON-CURRENT ASSETS HELD FOR SALE AND DISCONTINUED OPERATIONS

**"Limitations live only in our Minds
But if we use our imaginations, Our Possibilities become Limitless"**

1. WHY IND AS105?

When a company **stops continuing its business or plans to sell an asset** then the **users** of financial statements mainly investors **should be informed** about these events.

Therefore, IND AS 105 is drafted to set the requirements to be followed when above events takes place.

2. NON-APPLICABILITY OF IND AS105?

It is very important to note that the requirements of this standard applies to **ALL Non - Current Assets**, however measurement provisions shall not be applicable to:

- DTA (IND AS 12)
- Assets arising from employee benefits (IND AS 19) (eg. Plant Assets)
- Financial Assets (IND AS 109) (eg. Investment in Shares/Long term securities etc)
- Biological Assets which are measured at Fair value less cost to sell (IND AS 41)
- Contractual rights under insurance contracts (IND AS 104)
- Inventory (IND AS 2)

3. WHEN TO CLASSIFY AN ASSET AS HELD FOR SALE?

- ✓ An Entity should classify a **non-current asset or disposal group as held for sale** if:
 - Carrying amount will be **recovered principally through a sale**;
 - rather than continuing **use**.
- ✓ These Assets or disposal group are to be **presented separately** from other assets in the Balance Sheet. For disposal group Assets and liabilities shall not be offset.

Disposal group is a new concept introduced by IND AS 105 and it represents a group of assets and liabilities to be disposed of together as a group in a single transaction.

For example, when a company runs a few divisions and decides to sell one division, then all assets (including PPE, inventories, deferred tax, etc.) and all liabilities of that division would represent a disposal group.

When will an Asset be recovered through a sale rather than Continuing use?

Two Conditions must be fulfilled:

- (1) Asset/disposal group must be available for immediate sale (i.e. Ready to Sale)
- (2) Sale must be highly probable (i.e. High chances of sale in future)

Asset must be available for Immediate Sale	Sale must be highly Probable (5 Conditions)
<p>In Following cases Asset will not be considered for immediate sale:</p> <ol style="list-style-type: none"> a. The asset continues to be vital for the entity's operation; or b. Asset is required to be renovated before sale to enhance its value. 	<ol style="list-style-type: none"> 1. Management must be committed to a plan to sell the asset (eg. Resolution is passed); 2. An active program to find a buyer must have been initiated; 3. The asset must be actively marketed for sale at a price reasonable to its current fair value; 4. The sale is expected to be completed within 1 year from the date of classification; 5. Significant changes to or withdrawal from the plan to sell the Assets are unlikely.

Other Important Points:

1. **Loss of Control in Subsidiary:** An entity which has **committed to a sale plan** which involves loss of control of a subsidiary **shall classify all the assets and liabilities of that subsidiary as held for sale** when the criteria set out above are met.
2. **Exception to the period of One year** - An entity can still classify an asset (or disposal group) as held for sale, even if the timeframe of one year to conclude the sale transaction has lapsed. For this:
 - a. The delay must have been caused by the events or circumstances which are **beyond the control of the entity**; and
 - b. There must be sufficient evidences that the entity is **still committed** to its selling plan.
3. **Abandoned Asset:** Non-current assets (or disposal group) that need to be **abandoned** will **not qualify to classify as held for sale** because their carrying amount will be principally recovered through continuing use in the entity's operation rather through the sale.
There must be an "Intention to Sale". If asset is being abandoned from use but no intention to sale then we can-not classify an asset as held for sale"
(Asset Abandoned means stopped using the asset for some time)
4. **Asset acquired exclusively with a view to subsequent disposal:** When an entity acquires a non-current asset (or disposal group) **exclusively with a view to its subsequent disposal**, the non-current asset (or disposal group) **is classified as held for sale at the acquisition date**.
5. **Criteria met after reporting period:** If the criteria of held for sale are met after the reporting period but before the date of approval of the financial statements, a non-current asset **should not be classified as held for sale**. It is a **Non-adjusting Event**, only appropriate disclosure is required.

Important ICAI Module Examples:

1. A property being used as a headquarters by the entity needs to be vacated before it can be sold. The time required to vacate the building is usual and customary for sale of such assets. Hence the criteria for classification as held for sale would be met.
In above example, if property can be vacated only after a replacement is available then this may indicate that the property is not available for immediate sale, but only after the replacement becomes available.
2. An entity plans to renovate some of its property to increase its value prior to selling it to a third party. The entity is already searching for a buyer at current market values. But due to the plans to renovate the property prior to sale, the property may not be meeting condition of available for immediate sale.
3. An entity is committed to its selling plan of a manufacturing facility in its present condition and so classifies it as held for sale. After a firm purchase commitment, the buyer's inspection identifies environmental damages not previously known to exist. The entity is required by the buyer to make good the damage, which will extend the time frame of one year to complete the sale within one year. However, the entity has initiated actions to make good the damage and satisfactory rectification is highly probable. In this situation exception to one year requirement will met.
4. Entity ceases to use a manufacturing plant because demand has declined. However, the plant is maintained in a workable condition and it is expected to be brought back into use in future when demand picks up.
It is to be treated as abandoned asset rather as held for sale because its carrying amount will be principally recovered through continuous use, therefore the entity will not stop charging depreciation or will not treat it as held for sale. Because its carrying amount will be recovered principally through continuing use to the end of its economic life.
5. At the end of the reporting period, ABC Company's board of directors has approved a plan to sell a non-current asset. The eventual disposal requires approval by a majority of company's shareholders through a formal vote which will take place after the reporting period. At the end of the reporting period, a majority of the company's shareholders have provided the company with signed irrevocable agreements stating that they will vote in favour of the disposal. The 'highly probable' test is met because the shareholders have irrevocably committed to approving the transaction and, therefore, the vote by the shareholders is merely a formality.
6. An entity has acquired a building exclusively with a view of its subsequent disposal. The management is highly confident that the property can be sold in one year. The property requires refurbishing it to enhance its value which is highly probable to be completed in less than a period of three months. The building will be classified as held for sale on the date of acquisition itself even though it is not immediately available for sale.

5. HOW TO ACCOUNT FOR ASSETS HELD FOR SALE?

- (1) On the date of classification of Asset as held for Sale present the Asset as under:
Lower of -
- Carrying Amount of Asset / Disposal Group; or
 - Fair Value less costs to sell (FVLCTS)
- Note: Any reduction from carrying amount to FVLCTS is treated as impairment loss**
- (2) Depreciation and amortization shall be immediately stopped from the date of classification as held for sale.
- (3) **Treatment of Loss** - After you classify an asset as held for sale, you would recognize any impairment loss in profit or loss only.

Fair Value Loss (P&L) A/c Dr.

To Non-current Asset A/c

Individual Assets	Disposal Group
<p>On Initial measurement - Impairment loss is to be recognised in P&L a/c</p> <p>Subsequently thereafter, if fair value less cost to sell <u>increases</u> - Gain should be recognised <u>only to the extent of earlier cumulative impairments</u>.</p>	<p>On Initial measurement - Impairment loss shall be allocated to disposal group in the following order:</p> <ul style="list-style-type: none"> (a) First, Carrying Amt. of Goodwill (b) Then to other assets of disposal group pro rata on the basis of carrying amount of each assets in the group. (c) Do not allocate the loss to such assets of disposal grp which are not covered under Ind AS 105 such as inventory. <p>Subsequently when fair value less costs to sell <u>increases</u> - Gain (reversal of impairment loss) to the extent of goodwill is not to be recognised. Gain on other assets is to be recognised in P&L a/c</p>

- (4) **Updated Carrying amount immediately before Classification as HFS:**
- **Individual Asset:** Immediately before we classify any asset as held for sale, we should measure the assets under applicable IND AS. For example, we should measure an item of property, plant and equipment under IND AS 16.
 - **Disposal Group:** On subsequent re-measurement of a disposal group, the carrying amounts of any assets and liabilities that are **not** within the scope of the measurement requirements of this IND AS (eg. Inventory or Financial Instruments) but are included in a disposal group classified as held for sale, **should be re-measured in accordance with applicable Ind AS** (eg. IND AS 2 or IND AS 32) before the fair value less costs to sell of the disposal group is re-measured.
- Also, the impairment loss of disposal group shall not be allocated to those assets which are

part of disposal group but not covered within the scope of Ind AS 105

Format to Solve Questions of Disposal Group:

Step 1:

Calculate Total Impairment Loss of Disposal Group:

Total Carrying Amount at the Time of Classification as HFS	XXX
(-) Total FVLCTS	XXX
Impairment Loss	XXX

Step 2: Allocation of Impairment Loss as under:

	Goodwill	Non-Current Asset 1	Non-Current Asset 2
Carrying Amt. as at BS date	XX	XX	XX
(-) Apply Other Ind AS to disposal grp before classification as HFS & recognise the Loss	XX	XX	XX
Carrying Amt. at the time of Classification as HFS	XX	XX	XX
Allocate Impairment Loss of Step 1 to Goodwill First and then to remaining Non-Current Assets	XX Upto CA of Goodwill	XX (Total Imp Loss - Loss allocated to goodwill) shall be apportioned in the ratio of carrying amt of non-current assets)	
Revised Carrying Amt.	-	XX	XX

Practical Example 1: (Individual Non-Current Asset)

A Ltd purchased a property for ₹ 15,00,000 on 1 April 20X1. The useful life of the property is 10 years. On 31st March 20X4, A Ltd classify the property as held for sale. The impairment testing provides the estimated recoverable amount of ₹ 9,50,000. The fair value less cost to sell on 31 March 20X3 was ₹ 9,00,000.

On 30th June 20X4, FVLCTS is 8,40,000.

On 30th September 20X4, FVLCTS is 10,00,000

Solve here:

Practical Example 2:

- ✓ A Ltd acquired a property for ₹ 2,00,000. After few years the cumulative depreciation on the property is of ₹ 80,000 has been recognised and subsequently the property is classified as held for sale under Ind AS 105.
- ✓ At the time of classification as held for sale it will be measured at lower of its carrying amount which is ₹ 1,20,000 (2,00,000 - 80,000) and fair value less costs to sell as estimated at ₹ 1,00,000.
- ✓ Accordingly, there is a write-down on initial classification of property as held for sale and accordingly the property is carried at ₹ 1,00,000. A loss of ₹ 20,000 is recognised in profit or loss.
- ✓ On next reporting date, the property's fair value less costs to sell is estimated at ₹ 85,000. Accordingly, a loss of ₹ 15,000 is recognised in profit or loss and the property is carried at ₹ 85,000.
- ✓ Subsequently, the property is sold for ₹ 90,000. A gain of ₹ 5,000 is recognized in P&L.

Note: When the sale is expected to occur beyond one year, the entity should measure the costs to sell at their present value.

6. CHANGE IN A 'PLAN TO SALE'

- ☞ Earlier Classified as Held for Sale
 - ☞ Now it ceases to classify the asset or disposal group as held for sale
- ☞ Re-measure the Non-current asset at Lower of -
 - (a) Carrying Amount of Asset if there was not classification as HFS earlier.
 - Original Carrying Amount before classification as held for Sale
 - Less - Accumulated Depreciation/Amortisation on such CA
 - Less - Accumulated Revaluation
 - OR
 - (b) Recoverable Amount at the date of subsequent decision not to sell

Any difference due to reclassification from held for sale to other category will be treated as gain or loss and transfer to profit and loss account.

Practical Example 3: (Reversal of Impairment Losses)

A freehold property was originally acquired for ₹ 40,00,000. Some years later, after cumulative depreciation of ₹ 11,00,000 has been recognised, an impairment loss of ₹ 3,50,000 is recognised, taking

the carrying amount to ₹ 25,50,000, which represents the estimated value in use of the property. Shortly thereafter, as a consequence of a proposed move to new premises, the freehold property is classified as held for sale.

At the time of classification as held for sale:

- carrying amount is ₹ 25,50,000; and
- fair value less costs to sell is assessed at ₹ 25,00,000.

Accordingly, the initial write-down on classification as held for sale is ₹ 50,000 and the property is carried at ₹ 25,00,000. Following classification as held for sale, no further depreciation is recognised. At the next reporting date, the property market has improved and fair value less costs to sell is reassessed at ₹ 26,50,000. The gain of ₹ 1,50,000 is less than the cumulative impairment losses recognised to date (₹ 3,50,000 + ₹ 50,000 = ₹ 4,00,000). Accordingly, it is credited in profit or loss and the property is carried at ₹ 26,50,000.

Six months after that, the property market has continued to improve, and fair value less costs to sell is now assessed at ₹ 30,00,000. This further gain of ₹ 3,50,000 is, however, in excess of the cumulative impairment losses recognised to date (₹ 3,50,000 + ₹ 50,000 - ₹ 1,50,000 = ₹ 2,50,000). Accordingly, a restricted gain of ₹ 2,50,000 is credited in profit or loss and the property is carried at ₹ 29,00,000. Subsequently, the property is sold for ₹ 30,00,000, at which time a gain of ₹ 1,00,000 is recognised. An entity should recognise a gain for any subsequent increase in fair value less costs to sell of an asset, but not in excess of the cumulative impairment loss that has been recognised either in accordance with this IND AS or previously in accordance with IND AS 36 Impairment of Assets.

7. DISCONTINUED OPERATIONS

- 1) A Discontinued Operation is a component of an entity that either has been disposed of or is classified as held for sale and:
 - (a) represents a separate major line of business (means different segment) or geographical area (such as Branch) of operations; OR
 - (b) is part of a single co-ordinated plan to dispose of a separate major line of business or geographical area of operations; OR
 - (c) is a subsidiary acquired exclusively with a view to resale.
- 2) Once it is identified that there is a discontinued operation, we should present it separately from other continuing operations in our financial statements
(refer Schedule III - Statement of Profit and Loss)
- 3) Specific Disclosure Requirements:
 - a. Statement of Profit & Loss:
 - The Pre Tax, Tax Amount and Post Tax profit or loss of discontinued operations, and
 - The post-tax gain or loss recognized on the measurement to fair value less costs to sell or

on the disposal of assets or disposal groups.

The analysis (details) of a above amounts shall be reported in the notes or in the statement of Profit and Loss.

b. Balance Sheet: Present Assets and Liabilities of discontinued operation separately from continuing operation including disclosures.

Example:

In February 20X2, PQR Limited decides to abandon all of its coal mines, which constitute a major line of business. All work stops at the coal mines during the year ended 31 March 20X2. In the financial statements for the year ended 31 March 20X1, results and cash flows of the coal mines are treated as continuing operations. In the financial statements for the year ended 31 March 20X2, the results and cash flows of the coal mines are treated as discontinued operations and PQR Limited is required to make the disclosures as per Ind AS 105.

Example:

Company XYZ has 5 different operating segments, one of which solely produces consumer goods. All of the consumer goods production facilities are situated in Central Europe. XYZ also has other operations in Central Europe for other operating segments. In April 20X1, XYZ disposed of its consumer goods segment which meets the definition of a component of a business and represents a separate major line of business and would therefore be considered as a discontinued operation.

Example:

XYZ Company has one business segment, and it operates in the UK, the US and Australia. Each of these operations represents a component of XYZ and a major geographical area of operations. Management has decided to sell the US operation, which met the criteria to be classified as held for sale during the year. The US operation should be disclosed in the XYZ's financial statements as a discontinued operation, despite the fact that there has been no change to the number of business segments.

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IND AS 12

INCOME TAXES

"Doubt kills more dreams than failure ever will"

1. IMPORTANT DEFINITIONS

1. **Accounting Income:** is the net profit or loss before tax as shown in statement of profit and loss. (Profit before tax)
2. **Taxable Income (tax loss):** is the amount of the income (loss) for a period, calculated as per tax laws.
3. **Tax Base:** Value of any Asset or Liability that would appear as per Tax Records (i.e. in Income Tax Balance Sheet if we prepare it separately)
If any Asset is not Tax deductible and any Liability is not Taxable (i.e. Permanent difference) then Tax base = Carrying Amount.
4. **Current Tax:** is the amount of income tax to be payable (recoverable) in respect of the taxable income (tax loss) for a period. (Tax on Taxable Income)
5. **Tax Expense (tax saving) = Current Tax +/- Deferred Tax**
6. **Deferred Tax** is the tax on Temporary differences.
7. **Temporary Differences:** is a difference between the carrying amount of an Asset or Liability (as per books) and its Tax Base (as per Tax Records).
8. **Taxable Temporary Differences:** are temporary differences that will result in taxable amounts in determining taxable profits of future periods. (Tax payable in future due to expected increase in Taxable income) It results DTL.
9. **Deductible Temporary Differences:** are temporary differences that will result in amounts that are deductible in determining taxable profits of future periods. (Tax saving in future due to expected decrease in future Taxable income) It results in DTA.

Example of Tax Base:

when we have recorded an interest receivable (Rs. 100/-) on accrual basis but this interest revenue is taxed on a cash basis, assume cash will be received in the next year, then the tax base of interest receivable is 0 in CY and Carrying Amt of Interest Receivable (asset) is 100/-. Why?

Because in CY we don't record interest in Tax Balance Sheet (No Entry). But in Next Year, when we actually receive the cash and remove the interest receivable from our books, we have to include full amount of cash received into our tax return. At the same time, we cannot deduct anything from this amount for tax purposes.

2. CURRENT TAXES & Their Measurement

i.e. CURRENT TAX ASSET & CURRENT TAX LIABILITY

(a) Current tax Liability: (also known as Provision for Tax)

- Current Year Tax Payable
- (+) Prior Period Tax Payable
- (-) Tax already Paid (TDS/Advance Tax)

(b) Current tax Assets:

- Taxes Already Paid (TDS/Advance Tax)
- (-) Current Year Tax Payable
- (-) Prior Period Tax Payable

Note: Current Tax Asset also include any refund for which entity is eligible on carried backward of tax loss of CY against PY Taxable Income. (Refer example below)

Example 1

An entity has paid a tax in the previous year on a profit of Rs. 5,00,000 and suffered a loss in the current year of Rs. 6,00,000. Such loss of Rs. 6,00,000 can be adjusted against the Profit to the extent of Rs. 5,00,000 and the entity will create Tax Asset to that extent. It is called carry backward of losses.

(c) Tax Rate: Current tax liabilities (assets) shall be measured using the tax rates of same year that have been enacted.

(d) An enterprise should offset assets and liabilities representing tax if the enterprise:

- (a)** has a **legal enforceable right**; (i.e. both tax asset and tax liability are levied by same tax authority) and
- (b) intends** to settle the asset and the liability on a net basis.

Note:

In consolidated financial statements, a current tax asset of one entity (say Holding Co.) in a group can-not be offset against a current tax liability of another entity (say Subsidiary Co.) of the same group since the entities concerned doesn't have any legally enforceable right to make or receive a single net payment.

(e) Journal Entry of Current Tax Expense:

- (i) Current Tax Expense (P&L) A/c Dr.
To Current Tax Liability A/c
- (ii) Advance Tax or TDS A/c Dr.
To Bank / Debtor A/c

3. DEFERRED TAX LIABILITY

Recognize Deferred Tax Liability on **all Taxable Temporary Differences**, **except** on initial recognition of Goodwill, if such goodwill is not tax deductible.

Note: In tax jurisdiction, where goodwill is tax deductible, deferred tax liability should be recognised for the taxable temporary difference

(Refer Practical Example 1)

Items of Taxable Temporary differences where DTL is created

Taxable Temporary Differences	DTL recognition though
Depreciation in books is less than Depreciation under Tax records in the current year.	Profit and Loss A/c
100% expenditure is deductible in CY on scientific research but in books it is depreciable in more than 1 year.	Profit and Loss A/c
Investment in Shares/Debentures (Financial Assets) is carried at Fair Value in Books of accounts however Tax Base is a acquisition cost. Tax Base is Lower than Carrying Amount of Investments	Profit and Loss A/c (or) OCI
Accrued expenses with a carrying amount of Rs. 100. The related expense will be deducted for tax purposes on a cash basis in future. Tax base of the accrued expenses is nil.	Profit and Loss A/c
Upward revaluation of PPE (Gain) as per Ind AS 16 in books, however in tax records no such revaluation is charged to tax. (it will be chargeable to tax only when such Asset will be sold in future and capital gain would be charged or asset will generate taxable income in future against which depreciation will not be available in tax records) (Refer Practical Example 2)	OCI (Revaluation Surplus)
Assets recorded under business combinations at fair value which is more than carrying amount of Assets (tax base of Assets) in acquiree's books. (Refer Practical Example 3, 4)	Goodwill

Example 2: (DTL due to Depreciation)

Machine Costing Rs. 100 lakhs.

Useful life = 10 years, depreciation = 10%. Tax depreciation = 20%.

At year 1 end: Book value of Machine = Rs. 90 lakhs

Tax Base of Machine = Rs. 80 lakhs therefore its Taxable Temporary difference of Rs. 10 lakhs. If Tax Rate is 30%, DTL will be 30% of 10 lakhs i.e. 3 lakhs

Journal Entry:

Recognition of DTL	Deferred Tax Expense A/c (P&L or OCI) To Deferred Tax Liability A/c
Reversal of DTL	Deferred Tax Liability A/c Dr. To Deferred Tax Expense A/c (P&L or OCI)

5. DEFERRED TAX ASSET

A deferred tax asset shall be recognized for **all deductible temporary differences to the extent that it is probable that taxable profit will be available** against which the deductible temporary difference can be utilized.

Items of Deductible Temporary Differences where DTA is created

Deductible Temporary Differences	DTA recognition though
Depreciation in books is more than Depreciation under Tax records in the current year.	Profit and Loss A/c
Research Phase expenditure is fully charged to P&L in books, however it is deductible in 5 years as per Tax Law	Profit and Loss A/c
Provision for bad and doubtful debts created in books against debtors, it is disallowed under Income Tax, will be allowed in future in case of actual bad debts. Carrying Amount of debtors will be lower than Tax base.	Profit and Loss A/c
Interest revenue received in advance, with a carrying amount of Rs 100. The related interest revenue was already taxed on a cash basis. The tax base of the interest received in advance is nil. Revenue will be recognised as income in the next year	Profit and Loss A/c
Assets recorded under business combinations at fair value which is less than carrying amount of Assets (tax base of Assets) in acquiree's books	Reduction of Goodwill or Recognition of CR
Downward revaluation of PPE (loss) as per Ind AS 16 in books, however in tax records no such revaluation is deductible to tax.	OCI (Revaluation Surplus)

Example 3 (Research Exp. Fully charged to P&L but 1/5 deduction pa allowed)

Carrying amount is nil (because entire amount is treated as an expense to determine accounting profit) and tax base is the amount which will be deductible in future. Difference is deductible temporary difference that results in a **DTA through P&L**.

DTA on Un-used Tax Losses and Tax Credits

- Existence of Unused tax losses and tax credits is a strong evidence that **future taxable profits may not be available**.
- When an entity has a history of recent losses, the entity recognise a deferred tax asset arising from unused tax losses only when below conditions are fulfilled.
 - (i) whether it is probable that the entity will have taxable profits before the unused tax losses.
 - (ii) whether the entity has sufficient taxable temporary differences relating to the same taxation authority and the same taxable entity, which will result in taxable amounts against which the unused tax losses or unused tax credits can be utilised before they expire;
 - (iii) whether the unused tax losses result from identifiable causes which are unlikely to recur;

(Example - Covid 19)

- (iv) whether tax planning opportunities are available to the entity that will create taxable profit in the period in which the unused tax losses or unused tax credits can be utilised.

Journal Entry:

Recognition of DTA	Deferred Tax Asset A/c To Deferred Tax Income A/c (P&L or OCI)
Reversal of DTA	Deferred Tax Income A/c Dr. (P&L or OCI) To Deferred Tax Asset A/c

6. MISC PROVISIONS ON DTA & DTL

- (a) **Tax Rate:** Deferred tax (Asset/liabilities) shall be measured using the tax rates that are expected to apply to that period in which such DTA/DTL would be reversible/settled.

These expected rates need to be based on tax rates or tax laws that have been enacted or substantively enacted by the end of the reporting period.

- (b) **Multiple Tax Rates:** In such cases, an entity measures deferred tax liabilities and deferred tax assets using those tax rates and the tax base that are consistent with the expected manner of recovery or settlement.

In consolidated financial statements, DTA/DTL on temporary differences on items of subsidiary co. shall be created using Tax Rate applicable to Subsidiary co. **(Refer Practical Example 5)**

Example 4:

An asset has a carrying amount of Rs. 100 and a tax base of Rs. 60. A tax rate of 20% would apply if the asset was sold and a tax rate of 30% would apply to other income.

- (i) The entity recognises a deferred tax liability of Rs. 8 (Rs. 40 at 20%) if it expects to sell the asset without further use or
- (ii) a deferred tax liability of Rs. 12 (Rs. 40 at 30%) if it expects to retain the asset and recover its carrying amount through use.

- (c) **An enterprise should offset assets and liabilities representing tax if the enterprise:**

- (i) has a **legal enforceable right**; (i.e. both tax asset and tax liability are levied by same tax authority) and
- (ii) **intends** to settle the asset and the liability on a net basis.

- (d) **Permanent Differences:** No deferred tax Asset/Liability shall be recognized if any Asset is not tax deductible and any Liability is not taxable. In this situation Tax Base will be assumed to be equal to the Carrying Amount. Examples: Personal expenses of director debited in P&L but permanently disallowed, Penalty paid debited in P&L but permanently disallowed etc.

- (e) **MAT Credit:** MAT Credit as per Income Tax (Sec 115 JB) recognised in books is treated as DTA.
- (f) **DT on Compound Financial Instruments:** Carrying amount of loan liability will be lower than tax base, DTL shall be created through Equity. (Refer Practical Example 9)
- (g) **Re-Assessment of Un-recognised Deferred Tax Assets:** At the end of each reporting period, an entity reassesses un-recognised deferred tax assets. The entity recognises a previously un-recognised deferred tax asset to the extent that it has become probable that future taxable profit will allow the deferred tax asset to be recovered.

7. RECONCILIATION

1. A numerical Reconciliation between Tax Expense and the product of accounting profit multiplied by applicable tax rate.
2. A numerical Reconciliation between average effective tax rate (tax expense divided by accounting profit) and the applicable tax rate.
3. Reconciliation is required in following cases:
 - (i) When there is any permanent differences.
 - (ii) When some portion of Taxable Profit is charged as per special Tax Rate.
4. Entity operating in several tax jurisdictions, reconcile the total Current Tax (aggregate of all tax jurisdictions) with total Tax on aggregate Accounting Income as under:

Tax on Total Aggregate Accounting Income (considering Domestic Tax Rate)	XXX
Less/Add: Effect of Change in Tax Rates in several Tax Jurisdictions	xxx
Less/Add: Effect of Permanent differences in several Tax Jurisdictions	xxx
Total Aggregate Current Tax	XXX

(Refer Practical Example 6, 7 and 8)

8. SPECIAL SITUATIONS

CASE 1 - CREATING DEFERRED TAX ON CAPITAL GAIN IN CASE OF INDEXATION

- (a) Whenever an entity recognises an asset, it expects that it will recover the carrying value of that asset. For example, if an entity recognises an item of land at Rs 1,00,000, it expects that it will be able to recover at least Rs 1,00,000 if that land is sold at sometime in future.
- (b) The income tax provisions, assuming, provides that if this piece of land is sold after one year, there will be an indexation benefit @ 10% per year. Thus, if the land is sold after one year, the cost of the land will for the purpose of taxation will be assumed at ₹ 1,10,000 (Rs 1,00,000 + 10%). If it is sold after two years, the cost of the land for the purpose of taxation will be assumed at

Rs 1,21,000 (Rs 1,10,000 + 10%).

- (c) The tax rate in all years continues to be flat 30%.
- (d) Thus, the recovery of the carrying value of land after two years will result into a tax saving of Rs 6,300 i.e. 30% of 21000 (121000-100000).
- (e) Thus, if after two and half year, land is sold for Rs 1,50,000, the entity will pay a tax of Rs 8,700 at 30% of Rs 29,000 (Rs 1,50,000 - Rs 1,21,000). If there would have been no indexation benefits, the tax liability would have been Rs 15,000 at 30% of Rs 50,000 (Rs 1,50,000 - Rs 1,00,000). Saving in tax is of Rs 6,300 (15,000-8,700).
- (f) The entity should recognise a deferred tax asset of Rs 6,300 in this case.
- (g) This principle has to be applied to each item of asset.

Note: There are controversial view in case of Indexation of land for a temporary difference because if the land is not going to be sold in a near future particularly in business then in such case it is not advisable to calculate temporary difference.

CASE 2 - ACQUIRER'S DEFERRED TAXES ON BUSINESS COMBINATIONS

- (i) Due to business combination, **Acquirer's own Recognised DTA or Un-recognised DTA** is required to be **re-assessed**, since probability of realizing such DTA could change.
- (ii) For example, the acquirer may be able to utilise the benefit of its unused tax losses against the future taxable profit of the acquiree. Alternatively, as a result of the business combination it might no longer be probable that future taxable profit will allow the deferred tax asset to be recovered.
- (iii) In such cases, such DTA should be de-recognised (if recognised earlier) or recognised (if not recognised earlier) **but it should not form part of business combination accounting and should not affect goodwill arising due to business combination.**

CASE 3 - CT & DT ARISING FROM SHARE BASED PAYMENT TRANSACTIONS

Share Based payment transaction is recognised in **books on accrual basis** however **under tax law, deduction will be available only when share option is actually exercised** by employee.

Carrying Amount of Asset	Tax Base of Asset	Deferred Tax Impact
<p style="text-align: center;">Nil</p> <p>Entire amount is expensed of in the same year.</p>	<p>Employee Expense dis-allowed will become Asset in Tax Records.</p>	<p>DTA will be recognised in the year of Disallowance.</p> <p>DTA will be reversed in the year when option will be exercised.</p>

(Refer Practical Example 10)

CASE 4 - DISTRIBUTION OF DIVIDENDS

- In some jurisdictions, income taxes are payable at a higher or lower rate if part or all of the net profit or retained earnings is paid out as a dividend to shareholders of the entity.
- In some other jurisdictions, income taxes may be refundable or payable if part or all of the net profit or retained earnings is paid out as a dividend to shareholders of the entity.
- In these circumstances, current and deferred tax assets and liabilities are measured at the tax rate applicable to undistributed profits.

Example 5:

The following example deals with the measurement of current and deferred tax assets and liabilities for an entity in a jurisdiction where income taxes are payable at a higher rate on undistributed profits (50%) with an amount being refundable when profits are distributed. The tax rate on distributed profits is 35%. At the end of the reporting period, December 31, 20X1, the entity does not recognise a liability for dividends proposed or declared after the reporting period. As a result, no dividends are recognised in the year 20X1. Taxable income for 20X1 is Rs1,00,000. The net taxable temporary difference for the year 20X1 is Rs. 40,000.

The entity recognises a current tax liability and a current income tax expense of Rs50,000. No asset is recognised for the amount potentially recoverable as a result of future dividends. The entity also recognises a deferred tax liability and deferred tax expense of Rs20,000 (Rs40,000 at 50%) representing the income taxes that the entity will pay when it recovers or settles the carrying amounts of its assets and liabilities based on the tax rate applicable to undistributed profits.

Subsequently, on March 15, 20X2 the entity recognises dividends of Rs10,000 from previous operating profits as a liability.

On March 15, 20X2, the entity recognises the recovery of income taxes of Rs1,500 (15% of the dividends recognised as a liability) as a current tax asset and as a reduction of current income tax expense for 20X2.

CASE 5 - LEASE TRANSACTION IN THE BOOKS OF LESSEE

Particulars	Carrying Amount	Tax Base	Deferred Tax
ROU ASSET	Recognised as per Ind AS 116	Tax Base is Nil (No Recognised is allowed under Income Tax)	DTL shall be recognised
Lease Liability	Recognised as per Ind AS 116	Tax Base is Nil (No Recognised is allowed under Income Tax)	DTA shall be recognised
			New DTA/DTL shall be created

CASE 6 - TAX HOLIDAY PERIODS

Deferred tax calculation in case of tax holidays under Section 80-IA/80- IB/10A/10B of Income tax Act

Deferred tax in respect of temporary difference which **reverses** during the tax holiday period is not

recognised to the extent of the entity's gross total income exempt during the tax holiday period.

Example 6:

Y Ltd. is a full tax free enterprise for the first ten years of its existence and is in the second year of its operation. Depreciation temporary difference resulting in a tax liability in year 1 and 2 is Rs.200 lakhs and Rs. 400 lakhs respectively. From the third year it is expected that the temporary difference would reverse each year by Rs.10 lakhs. Assuming tax rate of 40%, find out the deferred tax liability at the end of the second year and any charge to the Profit and Loss account.

SOLUTION:

PARTICULARS	YEAR 1	YEAR 2
Temporary Difference	200	400
Reversal in Tax Holiday Period	80	0
Reversal after Tax Holiday Period	120	400
DTL charged to P&L	48	160

Total DTL as at the end of year 2 in BS will be $48 + 160 = 208$

CASE 7 - INVESTMENTS IN SUBSIDIARIES, BRANCHES, ASSOCIATES AND INTERESTS IN JOINT VENTURE ARRANGEMENTS:

Financial Statement of Investor (Holding Co. or Investor in Associate/JV)

Carrying Amount of Investment in Subsidiary, Associate or Joint Venture may be different from its Tax Base due to remeasurement of investments and recognition of profits in the books.

Such remeasurements are not allowed and profits are not chargeable to tax unless it is realised in cash in the form of sale or receipt of dividend. Following are important Deferred tax impacts.

Investment in Subsidiary	No Deferred Tax shall be recognised if parent has determined that those profits will not be distributed in the foreseeable future. Parent may controls the dividend policy of subsidiary hence the difference in Investment Value is of permanent in nature.
Investment in Associate	An investor in an associate does not control that entity and is usually not in a position to determine its dividend policy. Therefore, Investor shall recognise a deferred tax liability arising from temporary difference associated with its investment in the associate.
Investment in Joint Venture	Depends on Nature of Control. DTL shall be recognised only when Investor is not in a position to control the entity.

CASE 8 - LEVELS OF TAXABLE INCOME

When different tax rates apply to different levels of taxable income, deferred tax assets and liabilities are measured using the average rates that are expected to apply to the taxable profit.

Example 7: (Different levels of taxable income)

Income & Tax Slab	Tax Rates
0 - 2,50,000	Nil
2,50,000 - 5,00,000	5%
5,00,000 - 10,00,000	20%
10,00,000 above	30%
Cess	4%

- Mr. Jai has taxable income of Rs.18,00,000. Hence Tax liability based on above Tax Slab is Rs. 3,66,600.
- Weighted average tax rate = $3,66,600/18,00,000 \times 100 = 20.37\%$
- Therefore, for Calculation of Deferred taxes, weighted avg. tax rate should be considered i.e. 20.37%

Summary of Temporary Differences and Deferred Taxes:

	For Assets	For Liabilities
If carrying amount > tax base	Taxable Temporary Difference Deferred Tax Liability (e.g. WDV as per books > WDV as per Income Tax)	Deductible Temporary Difference Deferred Tax Asset (e.g. Provision for Bonus as per books > Provision for Bonus as per IT)
If carrying amount < tax base	Deductible Temporary Difference Deferred Tax Asset (e.g. WDV as per books < WDV as per Income Tax)	Taxable Temporary Difference Deferred Tax Liability (e.g. Loan carrying amount as per books < Loan carrying amounts as per tax)
If carrying amount = tax base	No temporary difference	No temporary difference

9. DIFFERENCE BETWEEN INDAS 12 AND AS 22

Sr.No	PARTICULARS	INDAS 12	AS 22
1	Approach for creating Deferred Tax.	Ind AS 12 is based on balance sheet approach.	AS 22 is based on income statement approach. It requires recognition of tax consequences of differences between taxable income and accounting income.
2	Limited Exceptions for Recognition of Deferred Tax Asset	As per Ind AS 12, subject to limited exceptions, deferred tax asset is recognised for all deductible temporary differences to the extent that it is probable that taxable profit will be available against which the deductible temporary difference can be utilised.	As per AS 22, deferred tax assets are 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. Where deferred tax asset is recognised against unabsorbed depreciation or carry forward of losses under tax laws , it is recognised only to the extent that there is virtual certainty supported by convincing evidence that sufficient future taxable income will be available against which such deferred tax assets can be realised.
3	Recognition of current and deferred tax.	As per INDAS 12 current and deferred tax are recognized as income or as expense through Profit and Loss a/c; OCI; Goodwill or Other Equity .	AS 22 does not specifically deal with this aspect. Hence Current and Deferred Tax shall always be recognized as income or as expense through Profit and Loss Statement .
4	Investments in subsidiaries, associates and joint ventures	As per Ind AS 12, deferred tax liability is recognised for all taxable temporary differences associated with investments in subsidiaries, associates and joint ventures, if certain conditions are satisfied.	AS 22 does not deal with this aspect.

5.	DTA/DTL arising out of Revaluation of assets	Ind AS 12 requires that deferred tax asset/liability arising from revaluation of non-depreciable assets shall be measured on the basis of tax consequences from the sale of asset rather than through use.	AS 22 does not deal with this aspect.
6.	In case of a company paying tax under section 115JB.(MAT)	Ind AS 12 does not specifically deal with this aspect	AS 22 specifically provides guidance regarding tax rates to be applied in measuring deferred tax assets/liabilities in a situation where a company pays tax under section 115 JB.

Student Notes:-



Student Notes:-



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IND AS 19

EMPLOYEE BENEFITS

"Make each day your Masterpiece"

1. EMPLOYEE BENEFITS

1) Meaning:

- Any consideration payable by employer to its employees against **services rendered** by them for the employer.
- Such consideration is payable due to "**contractual agreement**" between employer and employee or sometimes due to informal practices as a result of "**constructive obligation**".
- Ind AS 19 covers all types of employee benefits **excluding share-based payments** to employees.

Constructive Obligation:

An Obligation to pay that arises out of entity's actions rather than a contract. It may typically occur from past conduct (i.e. **Past Practices/Commitments**).

2) Types of Employee Benefits:

SHORT-TERM EMPLOYEE BENEFITS, which are expected to be settled within **Twelve Months after the end of reporting period**, such as wages, salaries etc.

POST-EMPLOYMENT BENEFITS, which are payable **after the completion of employment** such as gratuity, pension, other retirement benefits, post-employment life insurance and post-employment medical care etc.

OTHER LONG-TERM EMPLOYEE BENEFITS, which are payable beyond 12 months from the end of reporting period. E.g. Long Term Bonus plans

TERMINATION BENEFITS, which are payable to employees due to termination of their services before retirement. E.g. Retrenchment Compensation.

2. SHORT-TERM EMPLOYEE BENEFITS (NO ACTUARIAL ASSUMPTION & NO DISCOUNTING)

1) General Accounting Treatment:

Employee Benefit Expenses (Salary/Bonus) A/c Dr.

To Employee Benefits Payable A/c (Provision)

Employee Benefits Payable (Provision) A/c Dr.
To Bank A/c

2) Bonus in form of Profit Sharing:

It is also considered as an employee benefit expense if payable on satisfaction of required conditions.

It is payable as a **defined percentage of profit** earned by the employer.

3) Leaves Compensation (Paid Leaves or Compensating Absence):

Employer compensates to employees for their extra services provided by them during the leave period. Compensation can be provided in the form of either Cash or Extra leaves in the next period.

Accumulating Paid Leaves		Non-Accumulating Paid Leaves
Unused leaves can be carried forward to the next year		Unused leaves can-not be carried forward to the next year
Vesting Leaves (Payable in cash)	Non-vesting leaves (payable in the form of excess leaves in next year)	No Accounting
Here employee is eligible for cash payment against unused leaves. Hence 100% cash expense for unused leaves are recognised.	Here employee is eligible for extra leaves in the form of carried forward of unused leaves. Here it is not necessary that employee may utilize 100% excess leaves allowed, hence employee expense is recognised based on estimated leaves to be utilized.	
Expenses = Total Unused Leaves X Avg. Salary Per Day	Expenses = No. of Employees expected to utilize the unused leaves X No. of unused leaves expected to be utilized by each employee X Avg. Salary Per Day	
Avg. Salary Per Day = Total Annual Salary ÷ No. of Working Days		

Example 1:

Annual Salary - 12,00,000; Total Working Days - 300; Leaves allowed in a year - 12 days; Leaves actually taken by employee - 9 days. Unused leaves will be settled in form of cash.

DIFFERENCE BETWEEN DCP AND DBP

Basis of Difference	Defined Contribution Plans (DCP)	Defined Benefit Plans (DBP)
Meaning	Entity pays fixed contributions into a separate entity (a fund) and will have no legal or constructive obligation to pay further contributions.	Post-employment benefit plans other than defined contribution plans (i.e. No Fixed Contribution)
Actuarial & Investment Risk (Benefits will be more/less than expected)	Risk in substance on the Employee	Risk in substance on the entity.
Examples	Provident Fund Contribution by employer	Gratuity
Actuarial Assumptions	Not Required	Required
Discounting	Not Required unless it is payable beyond 12 months.	Always Required
Accounting	Same as short term employee benefits	Apply "Projected Unit Credit" Method

2) Accounting For Defined Benefit Plans: (Under Post Employment Benefit and Long Term Employment Benefits)

Scope of Accounting:

- Calculation of Defined Benefit Obligation (DBO) A/c and related Expenses
- Calculation of Plan Assets A/c and related Incomes
- Calculation of Actuarial Gains/Losses on DBO and Plan Assets
- Presentation of DBO and Plan Asset in Balance Sheet
- Presentation of Expenses (Incomes) in Profit and Loss Statement and OCI.

RECOGNITION OF DEFINED BENEFIT OBLIGATIONS (LIABILITY)

<p>Important Steps to calculate annual Defined Benefit Obligation</p>	<p>Step 1: Calculate Expected Benefits to be paid to employees Expected Final Salary x Benefit (%) x No. of Years of Service</p> <p>Step 2: Allocate the Benefits to each year of Service (Attributed Benefits) Step 1 ÷ No. of Years of Service</p> <p>Step 3: Calculate Current Service Cost (CSC) using discounting rate. PV of Attributed Benefits (PV working in upward mode)</p>
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	<p>Current Service Cost (CSC) A/c Dr. (P&L) To DBO Payable A/c</p> <p>Step 4: Calculate Interest Cost on Opening Balance of DBO Payable using same discount rate.</p> <p>Interest Cost A/c Dr. (P&L) To DBO Payable A/c</p>
Actuarial Gains or Loss in DBO liability	<p>Due to change in financial and demographic assumptions of actuary or due to change in final expected salary, no. of years of services, DBO liability shall be remeasured with new assumptions.</p> <p>Increase in DBO Liability = Actuarial Loss (OCI) Actuarial Loss (OCI) A/c Dr. To DBO Payable A/c</p> <p>Decrease in DBO Liability = Actuarial Gain (OCI) DBO Payable A/c Dr. To Actuarial Gain (OCI) A/c Dr.</p>
Past Service Cost (PSC)	<p>If there is a modification in Defined Benefits announced by employer which results in increase of benefits for employee (i.e. additional benefits) then DBO Liability shall be increased accordingly.</p> <p>Past Service Cost (P&L) A/c Dr. To DBO Payable A/c</p>
Curtailment and Settlement	<p>Curtailment means cancellation of Defined Benefits of employees. Settlement means providing compensation to employees against cancellation of benefits. Curtailment shall reduce the liability as under:</p> <p>DBO Payable A/c Dr. To Bank A/c Dr. To Gain on Settlement A/c (P&L)</p>
Payment of Benefits to Employee	<p>Whenever the employee retires, he/she will be eligible for benefits.</p> <p>DBO Payable A/c Dr. To Bank A/c Dr.</p>

RECOGNITION OF PLAN ASSETS (INVESTMENT for DBO)

Meaning	Investment made by Employer for meeting DBO liability. It is always recognised at Fair Value.
Contribution to Plan Assets	Contribution to Plan Asset means making Investment as per actuarial assumption under:

(+) Past Service Cost	XXX	(-) Payment of Benefits	XXX
(-) Curtailment of Benefits	XXX	(+/-) Actuarial Gain/(loss)	XXX
(-) Payment of Benefits	XXX	Closing Balance of Plan Asset	XXX
(+/-) Actuarial Loss/(Gain)	XXX		
Closing Balance of DBO	XXX		

Presentation in Financial Statements

BALANCE SHEET	STATEMENT OF PROFIT AND LOSS & OCI
Closing Balance of DBO	<u>Items of P&L:</u>
(-) Closing Bal. of Plan Asset	<u>Employee Benefit Expenses</u>
Net Defined Liability/(Asset)	<ul style="list-style-type: none"> • Current Service Cost under Employee Benefit Exp. • Past Service Cost • Gain on Curtailment
If there is Net Defined Asset, it is shown at lower of:	<u>Finance Cost</u>
(a) Actual Amount calculated as above; or	<ul style="list-style-type: none"> • Net Interest Cost under Employee Benefit Exp.
(b) Asset Ceiling (Realisation from Exit of Plan)	(Net Interest Cost means Interest Cost on DBO less Expected Return on Plan Asset)
If plan asset is shown at Asset ceiling, then difference is transferred to OCI (NRPL)	<u>Items of OCI:</u>
	<u>Not Reclassified to P&L</u>
	Actuarial Gain/Loss on DBO
	Actuarial Gain/Loss on Plan Asset
	Loss on Plan Asset due to Asset Ceiling
	Net Remeasurement Gain/Loss

Other Important Points:

1. The discount rate shall be determined by reference to **market yields** at the end of reporting period on **Government Bonds**.
However, foreign subsidiaries, associates, joint ventures and branches shall take discount rates by reference to **high quality corporate bonds**.
2. **Current/Non-Current Distinction:**
This Standard does not specify whether an entity should distinguish current and non-current portions of assets and liabilities arising from post-employment benefits.
3. **Offset:**
An **asset relating to one plan can-not be offset against a liability relating to another plan** unless the entity:
 - (a) has a **legally enforceable right** to use a surplus in one plan to settle obligations under the other plan; and

- (b) There is an **intention** either to settle the obligations on a net basis, or to realise the surplus in one plan and settle its obligation under the other plan simultaneously.

4. TERMINATION BENEFITS

An entity is required to recognise a liability and expense for termination benefits in the year of announcement of Termination Plan.

Amount paid for Termination of Employment	Termination Benefit Exp A/c Dr. (P&L) To Termination Benefits Payable A/c
Amount paid to receive services in future	It's a Normal Salary benefit

Example on Termination Benefits:

As a result of a recent acquisition, an entity plans to close a factory in ten months and, at that time, terminate the employment of all of the remaining employees at the factory. Because the entity needs the expertise of the employees at the factory to complete some contracts, it announces a plan of termination as follows:

Each employee who stays and renders service until the closure of the factory will receive on the termination date a cash payment of Rs 30,000. Employees leaving before closure of the factory will receive Rs 10,000.

There are 120 employees at the factory. At the time of announcing the plan, the entity expects 20 of them to leave before closure. Therefore, the total expected cash outflows under the plan are Rs. 3,200,000 (ie $20 \times \text{Rs}10,000 + 100 \times \text{Rs} 30,000$). As required by paragraph 160, the entity accounts for benefits provided in exchange for termination of employment as termination benefits and accounts for benefits provided in exchange for services as short-term employee benefits.

Termination benefits

The benefit provided in exchange for termination of employment is Rs. 10,000. This is the amount that an entity would have to pay for terminating the employment regardless of whether the employees stay and render service until closure of the factory, or they leave before closure. Even though the employees can leave before closure, the termination of all employees' employment is a result of the entity's decision to close the factory and terminate their employment (i.e. all employees will leave employment when the factory closes). Therefore, the entity recognises a liability of Rs. 1,200,000 (i.e. $120 \times \text{Rs}. 10,000$) for the termination benefits provided in accordance with the employee benefit plan at the earlier of when the plan of termination is announced and when the entity recognises the restructuring costs associated with the closure of the factory.

Benefits provided in exchange for service

The incremental benefits that employees will receive if they provide services for the full ten-month period are in exchange for services provided over that period. The entity accounts for them as short-term employee benefits because the entity expects to settle them before twelve months after the end of the annual reporting period. In this example, discounting is not required, so an expense of Rs. 200,000 (i.e. $\text{Rs}. 2,000,000 \div 10$) is recognised in each month during the service period of ten months, with a corresponding increase in the carrying amount of the liability.

4. TYPES AND TREATMENT OF GOVERNMENT GRANTS

Sr. No.	Type of Grant	Treatment
1.	<p>Grants related to Income (Revenue Nature)</p> <p>When the Expenditure is yet to be incurred then grant amount should be recognised as liability until related expenditure is incurred. When such expenditure is incurred, the above liability shall be reversed.</p>	<p>(a) (first method) presented as a credit in the statement of profit and loss, either separately or under a general heading such as 'Other income';</p> <p style="margin-left: 40px;">1) Bank a/c Dr To Def. Govt. Grant A/c</p> <p style="margin-left: 40px;">2) Def. Govt. Grant A/c Dr To P&L A/c</p> <p style="text-align: center;">(OR)</p> <p>(b) (Second method) deducted in reporting the related expense.</p> <p style="margin-left: 40px;">1) Bank a/c Dr To Def. Govt. Grant A/c</p> <p style="margin-left: 40px;">2) Def. Govt. Grant A/c Dr To Expense A/c</p>
2.	<p>Grant for Expenses or Losses already incurred;</p> <p style="text-align: center;">or</p> <p>Grant for immediate financial Support (Bailout Package)</p>	<p><u>If Un-conditional Grant:</u> Recognise directly to Profit and Loss a/c in the period when receivable</p> <p style="margin-left: 40px;">1) Govt. Grant Receivable A/c Dr To P&L A/c</p> <p style="margin-left: 40px;">2) Bank A/c Dr To Govt. Grant Receivable A/c</p> <p><u>If Conditional Grant:</u> Deferred and Amortise over the period of fulfillment of conditions</p>
3.	<p>Non-Monetary Grant (In Kind)</p> <p>Example: Land received free of cost or at concessional price</p>	<p>(a) If acquired at Concessional Price then Recognise the Grant at Actual Price Paid (acquired cost) or Fair Value.</p> <p>(b) If acquired at free of cost, then there is an option to Recognise at either Fair Value or Nominal Value.</p> <p>Nominal Value may be Rs. 1/-</p>

4.	<p>Grants related to Non-depreciable Assets Eg. Land/stock/cash</p>	<p>Conditional Grant: If it requires fulfillment of certain obligations then recognise in P&L a/c over the period of fulfillment of obligation.</p> <p>1) Bank A/c Dr To Def. Govt. Grant A/c</p> <p>2) Def. Govt. Grant A/c Dr. To P&L A/c (Amortised on systematic basis)</p> <p>Unconditional Grant: If it doesn't require any fulfillment of obligations in the future period then recognise the grant immediately in P&L a/c.</p> <p>Govt. Grant A/c Dr To P&L A/c</p>
5.	<p>Grants related to depreciable assets Eg. machine/building/vehicle</p>	<p>Option 1 - Deferred Income Treat it as Deferred Income:</p> <p>1) Bank A/c Dr To Def. Govt. Grant A/c</p> <p>DGG a/c shall be recognised in P&L a/c on a systematic basis over the useful life of the asset.</p> <p>2) Def. Govt. Grant A/c Dr. To P&L A/c (Amortised on systematic basis)</p> <p>Option 2 - Deduction from Cost Should be presented by deducting the grant amount from Carrying Amount and depreciation shall be charged on net carrying amount after deduction.</p> <p>1) Bank A/c Dr. To Govt. Grant A/c</p> <p>2) Govt. Grant A/c Dr To PPE A/c</p>

6.	Loans at less than market rate of interest	<p>Recognised and measured as per INDAS 109.</p> <p>Grant = Amount Received - Initial Carrying Amt as per INDAS 109</p> <p>Bank A/c Dr. To Loan A/c (at Fair Value) To Deferred Grant A/c (Bal. Fig.)</p>
7.	Forgivable Loans	<p>If conditions already complied then immediately transfer to P&L a/c.</p> <p>Loan A/c Dr To P&L A/c</p> <p>If conditions are required to be complied on continuous basis then over the period of compliance of conditions.</p> <p>Deferred Grant A/c Dr To P&L A/c</p>

Note:

Amount contributed by government as promoters' contribution is not treated as Govt. Grant. It is an Equity contribution and should be directly transfer to Other Equity.

5. REPAYMENT (REFUND) OF GOVERNMENT GRANTS

If Grant was recognised directly in P&L as income	If Grant was recognised as Deferred Income	If Grant was recognised as reduction from Cost of Asset
Refund of grant is debited to Profit and loss a/c	Refund of grant will be debited to Deferred Grant A/c to the extent of balance available. Any remaining amount of refund will be debited to Profit and loss a/c	Refund of grant will be debited to the same Asset A/c
P&L A/c Dr. To Grant Payable/Bank A/c	Deferred Grant A/c Dr. P&L A/c Dr. To Grant Payable/Bank A/c	Asset A/c Dr. To Grant Payable/Bank A/c Calculate Revised Depreciation on Asset for Further Years.

A government grant that becomes repayable should be accounted for as a **change in accounting estimate** and be treated in accordance with Ind AS 8, "Accounting Policies and Changes in Accounting Estimates and Errors".

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IND AS 21 – THE EFFECTS OF CHANGES IN FOREIGN EXCHANGE RATES

“You Learn More from Failure than Success”

1. WHAT IS COVERED IN IND AS 21

- Accounting for Foreign Currency Transactions.
- Translation of Financial Statements of Foreign Operations (FO) such as Foreign Subsidiary, Associates, JV & Branch into Presentation Currency
- Intra Group Transactions between Parent and FO
- Translation of Financial Statements of Entity into a Presentation Currency.

2. KEY DEFINITIONS

Foreign Currency	Any Currency other than Functional Currency of entity. (it can be more than one)
Functional Currency (Refer Practical Example 1 to 4)	Entity <u>maintains its books</u> in Functional Currency. It is a currency of the Primary Economic Environment in which entity operates. Primary economic environment will normally be the one in which entity <u>primarily generates and expends cash</u> i.e. it operates. Indicators to identify Functional Currency: (a) <u>Primary Indicators:</u> <ul style="list-style-type: none"> • Currency that mainly influence the Sales Price of Goods/Services (OR) • Currency that mainly influence the Cost of Providing Goods/Services (b) <u>Secondary Indicators:</u> <ul style="list-style-type: none"> • Currency in which Funds from financing activities are raised. (e.g. loan taken or equity raised) (OR) • Currency in which receipts of Operating Activities are Retained.

	<p>Note:</p> <ul style="list-style-type: none"> • An entity does not have a free choice of functional currency. • Focus should be more on "pricing determination in which currency", not on "denomination of transaction in which currency".
Presentation Currency	It is a currency in which Financial Statements are presented. Financial statements can be presented in more than one Currencies. E.g. A company is listed in Indian Stock Exchange as well as foreign country's Stock exchange, has to present its financial statements in Rupees as well as Currency of that country.
Monetary Items	Assets and Liabilities which are recoverable or payable in Fixed or determinable amount of Cash. E.g. Cash, Bank Balance, Debtors, Creditors, Loans etc.
Non-Monetary Items	Assets and Liabilities other than Monetary Items such as PPE, Investments, Inventory, Share Capital, Goodwill etc.
Foreign Operation (FO)	Any Subsidiary, Associate, JV or Branch whose operating activities are carried in any other country.

3. TREATMENT OF FOREIGN CURRENCY TRANSACTIONS

Any Transaction undertaken in Foreign Currency such as Purchase/Sale of Goods and Services, PPE, Borrowing or Investing:

INITIAL RECOGNITION: Recognise transaction at the **SPOT RATE** i.e. the Exchange rate prevailing on transaction date.

SUBSEQUENT MEASUREMENT: (At Balance Sheet Date or Settlement Date)

Subsequent Measurement on Balance Sheet shall be done only of Assets and Liabilities which are incurred in foreign currency:

Items	How to Measure
<p>Foreign Currency Monetary Items (FCMI)</p> <p>(Refer Practical Example 5)</p>	<ul style="list-style-type: none"> • Translate in Exchange Rate at the Reporting Date (i.e. Closing Rate) • Transfer the Exchange Difference to Profit and Loss A/c <p style="text-align: center;">Foreign Debtors A/c Dr. To Ex. Gain A/c (If debtors Increases)</p>
<p>Non-Monetary items measured at historical cost (e.g. PPE at Cost Model)</p>	<p>These items are not restated or translated; instead they remain at the Exchange Rate at the date of transaction. (i.e. Historical Rate)</p>

<p>Non-Monetary items measured at other than cost. (e.g. PPE at Revaluation Model, Inventory measured at NRV, Investments measure at FVTPL or FVTOCI)</p>	<ul style="list-style-type: none"> • Translate in Exchange Rate available on the date of determination of Fair Value/NRV/Market Value. • Transfer the Exchange Difference (Gain/Loss) to P&L if such non-monetary item is measured through P&L such as Inventory measured at NRV or Investments measured at FVTPL • Transfer the Exchange Difference (Gain/Loss) to OCI if such non-monetary item is measured through OCI such as PPE at revaluation model <p>(Refer Practical Example 6)</p>
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4. FINANCIAL STATEMENTS OF FOREIGN OPERATION

(Foreign Subsidiary, Associate, JV and Branch)

1. Currency of Foreign Operation:

Currency of Foreign Operation will be same as currency of Reporting Entity i.e. Holding Co. if all the conditions are satisfied:

- (a) Activities of foreign operations are carried out as an extension of that reporting entity (i.e. as per reporting entity's direction)
- (b) Transaction of foreign operation with reporting entity are in a High Proportion/volume.
- (c) Cash flows of foreign operations directly affect the cash flows of the reporting entity and are readily available for remittance to it.
- (d) Cash flows of foreign operation are not sufficient to pay its debts and other obligations.

If any of the above conditions are not satisfied, the foreign operation is treated as independent and Functional Currency of foreign operation will be different from that of reporting entity's functional currency and to be determined as per the primary and secondary indicators.

2. Translation of Financial Statement of Foreign Operation:

When foreign operation prepares its financial statements in its own functional currency different from that of reporting entity's currency then such financial statements are translated into presentation currency of reporting entity for the purpose of consolidation as per following rule:

All Assets and Liabilities	Conversion at Closing Exchange Rate of BS date
Revenue Items (Incomes and Expenses)	Conversion at Average Exchange Rate
Share Capital and Other Equity Items	Either converted amount will be given in the question or can be converted into actual spot rate. If spot rate is not given then opening rate may be taken.
Inventory and Assets subject to Impairment	Lower of: (a) Cost (converted at actual spot rate) or

	(b) NRV or Recoverable Amt. (converted at Ex. Rate of date of determination of NRV or Recoverable Amt.)
Goodwill	<p>Step 1: Calculate Goodwill in Foreign Currency value</p> <p>Step 2: Convert Goodwill into Presentation currency at Closing Exchange Rate of BS Date</p>
Treatment of Exchange Difference	<p>Exchange Difference is transferred to Foreign Currency Translation Difference A/c (FCTR) through OCI.</p> <p>Parent's Share of FCTR is presented separately under Other Equity in Consolidated Financial Statements</p> <p>NCI's Share of FCTR (if any) is added to the value of Total NCI in Consolidated Financial Statements</p>
Disposal of Foreign Operation e.g. Sale of subsidiary	<p><u>Case 1: Loss of Control</u> Parent's share of FCTR is reclassified to Profit and Loss A/c</p> <p><u>Case 2: Disposal without Loss of Control</u> Proportionate share of Parent's FCTR is transferred to NCI</p>

3. Intra Group Transactions between Parent and Foreign Operation:

Intra Group Transactions are divided into two categories:

- (a) Net Investment in Foreign Operation i.e. Long-Term Loan Transactions for which settlement is neither planned nor likely to occur in the foreseeable future.
- (b) All other Transactions such as Sale/purchase of goods/services or Short-term loans etc.

- All intragroup transactions are **eliminated** while preparing Consolidated Financial Statements (CFS).
- **Exchange gains/losses arising from All other transactions** (other than Net investment in Foreign Operation) are **shown in Consolidated Profit and loss**, because group has real exposure to foreign currency since one of the entities (Holding or Subsidiary) will need to obtain or sell the foreign currency to settle the obligation of foreign currency or realised the proceeds received in foreign currency.
- Exchange gains/losses (arising from Long-term loans for which settlement is neither planned nor likely to occur in the foreseeable future) are treated as under:

In Separate Financial Statement of FO	In CFS of Group
Shown in Profit and Loss A/c since loan is a monetary item.	Exchange difference shall be recognized initially in Other Comprehensive Income (OCI) and reclassified from equity to Profit and Loss A/c on disposal of the Net Investment.

Example: (Disposal without Loss of Control)

A parent has 100% interest in a subsidiary for a number of years. The subsidiary has been classified as a foreign operation and Rs. 5 million relating to the translation differences of subsidiary has been

recognised in other comprehensive income and accumulated in a separate component of equity. The parent disposes of 30% of its interest but retains control. What would be the treatment on the date of disposal?

Answer:

Rs. 1.5 million ($5 \times 30\%$) of cumulative translation exchange differences are transferred within equity from foreign currency translation reserve to non-controlling interest. No amounts are reclassified to profit or loss.

Example: (Disposal with Loss of Control)

A parent has 80% interest in a subsidiary for number of years. The subsidiary has been classified as a foreign operation and Rs. 5 million have been recognized in other comprehensive income. 80% have been accumulated in a separate component of equity and balance 20% attributed to non-controlling interest. The parent disposes 40% of its interest resulting in loss of control. What would be treatment on date of disposal?

Answer:

Rs. 4 million ($5 \times 80\%$) of cumulative translation exchange differences are transferred from equity to profit and loss. Rs. 1 million already reflected as part of non-controlling interest are derecognized and included in the calculation of the profit or loss on disposal.

Example: (Net Investment in Foreign Operation)

An Entity A has a foreign subsidiary B whose functional currency is Dollar (B). The Functional Currency of the entity A is Rupee. On 1st Jan, 20X6 when the exchange rate was \$1 = Rs. 80. Entity A has given loan to subsidiary B of Rs. 80,00,000. On 31st December, 20X6 the loan has not been repaid and is regarded as a part of net investment in the foreign subsidiary, as settlement of the loan is neither planned nor likely to occur in the foreseeable future. The exchange rate on 31st Dec, 2016 is \$1 = Rs. 77 and the average rate for the year was \$1 = Rs. 78. How this loan would be treated in the entity A's and group financial statement?

SOLUTION:

- There is no exchange difference in the entity A's financial statements, as the loan has been made in Rupees.
- In the foreign subsidiary's financial statements, the loan is translated into its own functional currency (dollar) at the rate of \$1 = Rs. 80 i.e. \$ 1,00,000 as of 1st Jan, 20X6.
- At the year-end 31st Dec, 20X6, the closing rate will be used to translate this loan. This will result in the loan being restated at \$ 103896 ($80,00,000 \div 77$), giving an exchange loss of \$3896, which will be shown in the subsidiary's (B) Profit and Loss account.
- In the group financial statements, this exchange loss will be translated at the average rate, as it is in the subsidiary's Profit and Loss account item, giving loss of Rs.3,03,888 ($\$ 3896 \times 77$). This will be recognised in the other equity through OCI. Because the loan is not planned to be settled in the foreseeable future.

Note: Even Perpetual Debt Instrument with fixed rate of interest are also an example of "Net Investment in Foreign Operation".

6. TRANSLATION OF FINANCIAL STATEMENTS FROM FUNCTIONAL TO PRESENTATION CURRENCY

All Assets and Liabilities	Conversion at Closing Exchange Rate of BS date
Revenue Items (Incomes and Expenses)	Conversion at Average Exchange Rate
Share Capital and Other Equity Items	Either converted amount will be given in the question or can be converted into actual spot rate. If spot rate is not given then opening rate may be taken.
Inventory and Assets subject to Impairment	Lower of: (a) Cost (converted at actual spot rate) or (b) NRV or Recoverable Amt. (converted at Ex. Rate of date of determination of NRV or Recoverable Amt.)
Treatment of Exchange Difference	Exchange Difference is transferred to Foreign Currency Translation Difference A/c (FCTR) through OCI.

7. CHANGE IN FUNCTIONAL CURRENCY

- Functional Currency can be changed only *if there is a change to the underlying transactions, events and conditions* (ie. Change in Primary economic environment in which entity operates)
- Translation procedures:
 - All items (Assets, Liabilities, Equity, and Expenses & Incomes) are translated into the new functional currency using the exchange rate at the date of change.
 - Exchange Gain/Loss will not arise.
- Change in functional currency may be accompanied by a change in presentation currency. The choice of presentation currency represents an *accounting policy*, and any change should be applied *retrospectively* in accordance with Ind AS 8.

8. SPECIAL CASES

1. Dividend received by Parent Co. from Foreign Subsidiary Co.:

When dividend is declared by Subsidiary	Holding co. shall record such dividend on accrual basis by translating into SPOT Rate.
When dividend is actually paid on another date	Dividend received shall be converted into exchange rate on the date of receipt. Difference shall be transfer to Profit and Loss A/c

2. Foreign Currency Borrowings:

Particulars	Foreign Currency Working	Exchange Rates	Conversion into Functional Currency
Opening Balance	\$	Opening Ex. Rate	₹
(+) Interest (%)	\$	Avg. Rate	₹
(-) Repayment	\$	Actual Rate	₹
Closing Balance	\$ (Bal. Fig.)	Closing Ex. Rate	₹
Exchange Difference (Balancing Figure)			₹

3. Advance collected from Customer:

Whenever we collect advances from customer where revenue is not yet recognized & to be recognized in future, then revenue for such advance amount shall be recognized based on exchange rate available on date of receipt of advance. (Refer Q204 of Question Bank)

4. Measurement of Inventory Purchased in Foreign Currency at BS date:

		Amount in ₹
Cost of Inventory	Foreign Currency X Spot Rate of Transaction Rate	₹ XXX
NRV in Foreign Currency	Determine NRV in Foreign Currency first and then translate it into Exchange rate available on the date of determination of NRV	₹ XXX
Cost or NRV (Amt. in ₹) whichever is lower as per Ind AS 2		₹ XXX

5. PPE purchased in Foreign Currency subject to Impairment Testing:

		Amount in ₹
Carrying Amount (CA) of PPE	Original Cost (already converted into SPOT Rate) less accumulated depreciation	₹ XXX
Recoverable Amount (RA) of PPE	Recoverable Amount (\$) x Ex. Rate on the date of Determination of RA	₹ XXX
CA or RA (Amt. in ₹) whichever is lower as per Ind AS 36		₹ XXX
CA - RA = Impairment Loss transfer to P&L		

Example: (Impairment Testing)

A foreign currency asset amounting to Euro 200,000 is recorded at the date of purchase when the exchange rate was ₹52 at ₹104 lacs.

The recoverable amount of the asset on the reporting date is calculated as Euro 175,000. The exchange rate on the date of valuation was ₹ 60 to a Euro.

The carrying value of the foreign currency asset will be determined based on the recoverable amount of the asset converted into functional currency at the exchange rate on valuation date which is ₹105 lacs.

The impairment loss of Euro 25,000 in foreign currency is not recognised.

6. Deferred Taxes on Exchange Gains/Losses:

- Tax Base of Assets and Liabilities may be different from the Carrying Amount of Assets and Liabilities after translation under Ind AS 21.
- This difference is a Temporary difference and DTA/DTL shall be recognised.
- Recognition of DTA/DTL through P&L or OCI depends on the source of Exchange Difference.

9. SUMMARY OF EXCHANGE DIFFERENCES

Different Situations	Transfer Ex. Difference to P&L	Transfer Ex. Difference to OCI
<u>Foreign Currency to Functional Currency:</u>		
a) Translation of FCMI Foreign Debtors, Creditors, Borrowings	Yes	No
b) Translation of Non-Monetary FC Items measured at other than Cost thru P&L e.g. Inventory or Investment measured at FVTPL	Yes	No
c) Translation of Non-Monetary FC Items measured at other than Cost thru OCI e.g. Upward Revaluation of PPE	No	Yes
d) Dividend from Foreign Subsidiary	Yes	No
<u>Functional Currency to Presentation Currency:</u>		
a) Translation of F/s of Foreign Operation by Parent Company	No	Yes Also some portion in NCI
b) Net Investment in Foreign Operation	No	Yes
c) Translation of F/s of Entity	No	Yes

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IND AS 33 EARNINGS PER SHARE

1. MEASUREMENT OF BASIC EARNINGS PER SHARE

Earning Per Share are of two types:

- 1) Basic EPS (BEPS)
- 2) Diluted EPS (DEPS)

Basic EPS is calculated as under:

$$\frac{\text{Profit/Loss attributed to Equity Shareholders}}{\text{Weighted Average Number of Equity Shares}}$$

Numerator for EPS - Profit/loss attributable to Equity Shareholders

Particulars	Amount	Remarks
Earnings Before Interest and Tax (EBIT)	XXX	
(-) Interest on Borrowings	(XX)	Actual Interest Rate or ERI if given
(-) Preliminary Exp or any other Income/Exp	(XX)	If not debited to P&L but required to be charged to P&L only
Earnings Before Tax (EBT)	XXX	
(-) Tax Expense	(XX)	CT +/- DT
Earnings After Tax (EAT/PAT)	XXX	
(-) Preference Dividend	(XX)	Assume Cumulative Preference Shares
(-) Premium on Redemption/Conversion of PS	(XX)	Even if it deducted from Sec. Prem A/c
Profit/Loss attributable to Ordinary ESH	XXX	

Important Points for Numerator:

Interest at ERI (%)	Any instruments such as redeemable preference shares which are classified as Liability then dividend/interest shall be deducted as per Effective Rate of Interest method.
Preference Dividend	If Cumulative Preference Shares then deduct the dividend always If Non-cumulative Preference Shares then deduct the dividend only when declared. Always assume cumulative if not specified in questions
Premium on Preference Shares	Premium/Settlement premium on redemption or conversion of preference shares and w/o from securities premium a/c or any other reserves shall also be deducted.
Any Income or Expense not debited to P&L	Any Income or Expenses which is otherwise required to be transferred to Profit and Loss, but not actually recognised in profit and loss and transferred to other reserves or written off from security premium

	(like Preliminary exp) shall also be considered while calculating EPS.				
OCI Items	OCI items are not considered while calculating EPS				
EPS in Consolidated Financial Statements (CFS)	<p>EPS for CFS shall be calculated as under:</p> $\frac{\text{Total Profit/Loss attributed to Equity shareholders of Parent Entity}}{\text{Weighted average number of Equity shares}}$ <p>Total Profit/Loss attributed to Equity shareholders of Parent Entity:</p>				
(Refer Practical Example 6)	<table> <tr> <td>Profit of Parent Entity (as per SFS)</td> <td>XXX</td> </tr> <tr> <td>Share of Parent in Profit of Subsidiary</td> <td>XXX</td> </tr> </table>	Profit of Parent Entity (as per SFS)	XXX	Share of Parent in Profit of Subsidiary	XXX
Profit of Parent Entity (as per SFS)	XXX				
Share of Parent in Profit of Subsidiary	XXX				

Example: (Premium on Preference Shares)

ABC Company issues 9% preference shares of FV of Rs 10 each on 1.4.20X1. Total value of the issue is Rs 10,00,000. The shares are issued at a discount of Rs 0.50 each, for a period of 5 years and would be redeemed at the end of 5th year. The shares are to be redeemed at Rs 11 each.

At the end of the year 3, i.e. on 31.3.20X4, company finds that it has earned good returns than expected over last three years and can make the redemption of preference shares early. To compensate the shareholders for two years of dividend which they need to forego, company decided to redeem the shares at Rs 12 each instead of original agreement of Rs 11. Comment on the earnings for the year 20X3-20X4.

Solution

In the given situation, Rs 2 per share is the excess payment made by the company amounting to Rs 2,00,000 in all. The amount of Rs 2,00,000 will be deducted from the earnings of the year 20X3-20X4 while calculating the basic EPS of year 20X3-20X4.

Denominator for EPS - Weighted Average Outstanding Ordinary Shares

Number of Ordinary Shares are considered for Basic EPS adjusted by Time Factor (i.e. No. of days/months for which shares were outstanding during the year as against total days/months during the year)

Calculation of Weighted Avg. Ordinary Shares:

Particulars	W. Avg. No.	Remarks
No. of shares in the beginning of year		
(+) No. of shares issued during the year against cash consideration (Normal issue)		No. of days/months from issued date to year end ÷ 365 days or 12 months
(-) No. of shares buyback during the year Also called treasury shares		No. of days/months from BB date to year end ÷ 365 days or 12 months
(+) No. of Bonus shares issued during the year		12/12 always

(Refer Practical Example 1 & 2)

Deciding the date for issue of shares

Sr. No	Nature of transaction	Effective Date when
1	General Rule	From date of consideration receivable or date of issue
2	Exchange for cash	From date of consideration receivable or date of issue

3	Voluntary reinvestment of dividend	Date when Dividend is reinvested
4	Conversion of debt instrument	Date of Accrual of interest is stopped
5	In lieu of interest / principal	Date of Accrual of interest is stopped
6	Exchange of liability	Settlement Date
7	Consideration for acquisition of asset	Asset is recognised in books
8	Rendering of services	When Services are rendered
9	Business combinations	Acquisition date (Date of Acquisition of control)
10	Mandatory convertible instrument	Date of contract/issue of convertible instrument
11	Contingently issuable shares	When all necessary conditions for conversion are satisfied

Special Cases for denominator (Weighted Average outstanding ordinary shares):

Bonus/Share Split/consolidation	<ul style="list-style-type: none"> These shares are issued without any consideration to existing shareholders by capitalization of reserves. Such reserves are already available since beginning of previous year hence time factor should always be considered from beginning of PY. PY EPS shall also be restated (calculated again) for CY disclosure purpose by including Bonus shares in PY denominator.
Partly Paid-up Shares (Refer Practical Example 3)	<ul style="list-style-type: none"> First, check whether partly paid-up shares are entitled to dividend or not. If partly paid-up shares are not entitled to a dividend unless they become fully paid up, then do not consider them in BEPS working. They are treated as potential equity shares for DEPS working. If partly paid-up shares are entitled to a dividend, then calculate weighted average outstanding equity share capital (in ₹) instead of No. as under: $\frac{\text{No. of Fully Paid-up shares} \times \text{Face Value} \times \text{Time Factor} + \text{No. of Partly Paid-up shares} \times \text{Paid up Price} \times \text{Time Factor}}{\text{Total Weighted Avg. Equity Share Capital (in ₹)}}$ <p>Calculate Earnings Per Rupee (EPR): Profit/Loss attributable to ESH ÷ Total Weighted Avg. ESC</p> <p>Calculate EPS as under: EPR (in ₹) × Paid-up price or Face Value</p>
Right Issue (RI) (Refer Practical Example 5)	<p>Right issue of shares has bonus element hence follow the below steps:</p> <p>Step 1: Calculate Theoretical Ex right price per share if not available</p> <p><i>Formula</i></p> $= \frac{[\text{Fair Value (before right)} \times \text{No. of share (pre - right)}] + \text{Right issue proceeds}}{\text{Total shares post right}}$ <p>Step 2: Calculate Right Factor (RF) = $\frac{\text{Cum Right Price}}{\text{Ex Right Price}}$</p> <p>(Cum right price also know as Market price will be given in question)</p>

	<p>Step 3: Weighted Average O/s Ordinary shares of current year: - $\frac{\text{No. of shares o/s (pre-right)} \times \text{RF} \times \text{No. of Months till the date of RI} \div 12}{\text{(+ No. of shares o/s (post-right)} \times \text{No. of Months after RI till end of year} \div 12)}$ Total weighted Avg. O/s ordinary shares</p> <p>Step 4: Calculate BEPS of CY as usual</p> <p>Step 5: Calculate Restated BEPS of PY also by considering above RF in weighted avg. calculation of PY</p>
Compulsory convertible debentures or preference shares	<ul style="list-style-type: none"> Mandatory/Compulsorily Convertible instruments (convertible into Equity shares) are to be considered while calculating Basic EPS from the date of contract i.e. from the date of issue of such instruments. However, interest paid on such instruments shall be treated in the normal way and deducted from Net Profit and Loss attributable to ESH. Always assume that convertible instruments are not mandatory. <p>(Refer Practical Example 4)</p>

2. EPS IN CASE OF DIFFERENT DIVIDEND RIGHTS

Absolute Dividend Rights for different class of Equity Shares	Proportionate Dividend Rights for different class of Equity Shares	Participating Preference Shareholders								
<p>Here absolute dividend means additional dividend rights are given in absolute amount</p> <p>Step 1: Calculate Additional Dividend Amount for each class of Equity Shares</p> <p>Step 2: Calculate Total Earnings excluding above step 1</p> <p>Step 3: Calculate Normal EPS based on Step 2 for each class of Share</p> <p>Step 4: EPS (for each Class) = Normal EPS + Additional Dividend Per</p>	<p>Here proportionate dividend rights means each class of share is eligible on specified proportion of normal dividend right</p> <p>Step 1: Assume Normal Dividend is "X" %</p> <p>Step 2: Calculate Dividend Right for each class as proportion to normal dividend as per the given information</p> <p>Step 3: Apply Dividend Right of each class to Share Capital of each class.</p>	<p>Participating Preference Shares are those preference shares who are eligible to undistributed earnings (after payment of equity dividend).</p> <p>Step 1: Calculate Undistributed Earnings</p> <table style="width: 100%; border-collapse: collapse;"> <tr> <td style="width: 80%;">EAT</td> <td style="text-align: right;">XXX</td> </tr> <tr> <td>(-) Pref. Dividend</td> <td style="text-align: right;">(XX)</td> </tr> <tr> <td>(-) Equity Dividend</td> <td style="text-align: right;">(XX)</td> </tr> <tr> <td>Undistributed Earn.</td> <td style="text-align: right;">XXX</td> </tr> </table> <p>Step 2: Allocate the undistributed earnings to ESH and Participating PSH as per the questions information</p>	EAT	XXX	(-) Pref. Dividend	(XX)	(-) Equity Dividend	(XX)	Undistributed Earn.	XXX
EAT	XXX									
(-) Pref. Dividend	(XX)									
(-) Equity Dividend	(XX)									
Undistributed Earn.	XXX									

<p>Share</p> <p>(Refer Q501)</p>	<p>Step 4: Allocate the Total Earnings to each class in the ratio of step 3</p> <p>Step 5: Calculate EPS for each class separately.</p> <p>(Refer Q502)</p>	<p>Step 3: EPS for Equity Share = Dividend distributed per share (+) Allocated Undistributed Earning Per Share</p> <p>Step 4: Earning per share for Pref. Shareholders = Dividend Distributed Per Share (+) Allocated undistributed earning per share.</p> <p>(Refer Q504)</p>
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3. DILUTED EARNINGS PER SHARE

1. Diluted EPS is calculated when there are outstanding potential equity shares.
2. Potential Equity Shares are those securities which can be converted into ordinary equity shares in future.
E.g. Convertible Preference Shares, Convertible Debentures, Share warrants, ESOPs, Call Options, Partly paid-up shares if not eligible for dividend unless they become fully paid-up, Contingently issuable shares
3. Diluted EPS means reduction of Basis EPS if same earnings will continue with additional no. of shares when potential equity shares will be converted into ordinary shares.
4. Conversion into Ordinary shares may increase the Numerator and Denominator as under:

Numerator	Denominator
Saving of Interest after Tax due to conversion of Debentures.	Increase in No. of Shares due to conversion of Preference shares, Debentures, Warrants, ESOPs and Call Options.
Saving of Preference Dividend due to conversion of Debentures.	

5. Above Change in Numerator and Denominator may increase or decrease the existing Basic EPS.
If there is a Decrease in EPS = It is Diluted EPS
If there is a Increase in EPS = It is Anti Diluted EPS
6. Anti diluted EPS is not required to be reported. In that case, DEPS = BEPS

7. DEPS formulae:

Numerator	Denominator
Profit/loss attributable to ESH (+) Savings due to Conversion of Potential Equity Shares (after Tax if required)	Weighted Avg. O/s Ordinary Shares (+) Weighted Avg. O/s Potential Eq. Shares

How to Calculate DEPS - Following calculation is required:

- Identify Potential Equity Shares first. (Whether any security which is pending for conversion is outstanding and resources thereof have been used in the business)
- Identify Dilutive potential equity shares by applying following steps:

Step 1: Identify Potential Equity Shares (PES) first.

Step 2: Calculate Incremental EPS for every single potential equity share as under:

$$\frac{\text{Adjustment in Earnings due to Conversion of PES}}{\text{Adjustment in Shares due to PES}}$$

Step 3: Arrange IEPS in Increasing Order. Lowest IEPS will get 1st Position and so on
It is called Most Dilutive PES

Step 4: Calculate DEPS as under:

	Particulars	Numerator	Denominator	EPS
a)	Basic EPS	XXX	XXX	XX
b)	(+) PES with Rank 1	XXX	XXX	
c)	Total (a+b)	XXX	XXX	DEPS
d)	(+) PES with Rank 2	XXX	XXX	
e)	Total (c + d)	XXX	XXX	DEPS
f)	(+) PES with Rank 3	XXX	XXX	
g)	Total (e + f)	XXX	XXX	DEPS
h)	(+) PES with Rank 4	XXX	XXX	
i)	Total (g + i)	XXX	XXX	DEPS

Final Diluted EPS will be lowest of All DEPS calculated as above.

Special Cases of DEPS:**Call Options, ESOPs, Share Warrants**

Earnings (Numerator) = Zero i.e. no adjustment
No. of Potential Eq. Shares (Denominator) =
Total Options (-) $\frac{\text{Total options} \times \text{Exercise Price}}{\text{Market Price}}$

Time weight shall be from date of option granted to date of exercise

Contingently Issuable Shares

- Shares to be issued at little or no consideration on fulfillment of future uncertain condition.
- If condition is satisfied but shares are still not issued actually, to be considered in Basic EPS and DEPS.
- If condition is satisfied at Balance sheet date but the final compliance date of condition is in future, treat it as potential equity and include in DEPS only.

(Refer Practical Question 703)

Example: (Call Options)

If company issues 100 options to be exercised at Rs 45 each after 31st March 20X1. The market value of the share on 15th April 20X1 is Rs 50 each. In such cases the holder option will be interested in exercising the option because he will get the shares at Rs 45, when the market value outside is Rs 50. He can sell the shares outside and get a profit of Rs 5 each on each share held, i.e. $100 \times \text{Rs } 5 = \text{Rs } 500$.

On the other hand, assume that the market value of 15th April 20X1 is Rs 35 only. In such case the holder of option/ warrant will not be interested in exercising the option because it will be a loss making proposal for him.

In first case where the strike price of call option is less than the market value of the share it is termed as "in the money" option whereas in second case when exercise price of call option is more than the market value of the share it is termed as "out of the money: option.

While calculating the diluted EPS, the options/ warrants need to be considered only if they are dilutive.

Example: (contingently issuable shares)

ABC company will issue the shares only if the company achieves the after tax profitability of 15%. In such case, achievement of profitability is a contingent event. Therefore, company should not include the number of shares in calculation of Basic EPS, unless company actually achieves 15% profitability. In the F.Y. 20X0-20X1 company achieves the profitability of 13% only. The company will not include the shares while calculating EPS. But if in 20X1-20X2, company achieves the profitability of 17%. Then while calculating the EPS for 20X1-20X2 the shares will be considered for the calculation of basic EPS even if the shares are actually not issued.

Example: (contingently issuable shares)

PQR Company entered into contract that it will issue the shares only after completion of 3 years from the date of contract. Here the condition to be satisfied is the completion of 3 years. There is no other condition, then passage of time. Passage of time is definite event. There is no uncertainty involved in passage of time. Therefore, such shares will be included in the calculation of basic EPS because there is no contingently issued shares.

4. GROUP EPS OR CONSOLIDATED EPS

- 1) Under Consolidated Financial Statements, Consolidated BEPS and DEPS is required to be shown.
 2) Basic EPS for Consolidated financial statements is calculated as under:

Numerator	Denominator
Parent's Own Earnings Attributable to ESH (+) Equity Shares held by P in S \times BEPS of S (+) Pref. Shares held by P in S \times Pref. DPS Total Earnings attributable to the owners of Parent	Weighted Avg. O/s No. of Ordinary Shares issued by Parent

- 3) Diluted EPS for Consolidated financial statements is calculated as under:

Numerator	Denominator
Parent's Own Earnings Attributable to ESH Parent's own adjustments in Earnings due to its PES (+) Equity Shares held by P in S \times DEPS of S (+) Pref. Shares held by P in S \times DEPS of S (+) PES of held by P \times DEPS of S Total Earnings attributable to the owners of Parent After adjusting effect of PES	Weighted Avg. O/s No. of Ordinary Shares issued by Parent (+) Weighted Avg. O/s No. of PES issued by Parent Total Weighted Avg.

(Refer Question 806)

5. PRESENTATION OF EPS

- 1) The Entity shall present BEPS and DEPS in the **face of a Statement of Profit and Loss**.
 2) EPS should be presented in the following headings:
 i) Basic EPS for continuing operation
 ii) Basic EPS for Discontinued Operation
 iii) Basis EPS for Total Business
 3) EPS in case of SFS and CFS:

Sr. No.	Type of Financial statements	Consolidated EPS	Separate EPS
1	Consolidated	Must disclose	Don't disclose
2	Separate	Don't disclose	Must disclose

- 4) **Net Loss in Continuing Operation:**

DEPS from continuing operation shall be calculated without considering Potential Equity Shares otherwise it gets anti-diluted.

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IND AS 102

SHARE BASED PAYMENT

1. WHAT IS SHARE BASED PAYMENT ?

Share Based Payment (SBP) is a contract between the employer and employee (or) supplier and customer whereby employer/customer promises to pay its own equity shares or cash based on the price of its own equity shares against Goods or Services received by them.

2. NON - APPLICABILITY

This Standard is not applicable to the following:

- a. Right Issue of Equity shares to the employees in the capacity of existing shareholders;
- b. Share issued under Business Combinations (Acquisitions) or Joint Ventures

3. TYPES OF SHARE BASED TRANSACTIONS

1. **Equity settled** Share based Payment transactions with Employees;
2. **Cash settled** Share based Payment transactions with Employees; and
3. **Equity settled with Cash alternative** - where employee have a choice between share settlement or cash settlement.

4. IMPORTANT DEFINITIONS

1. **Grant Date:** Date on which Share based payment is offered or announced.
2. **Vesting Condition:** Conditions to be satisfied by employees to be eligible for Share Based Payment Plans.
3. **Vesting Date:** Date on which employee becomes eligible for Share based payment plans (means on this date the conditions are fulfilled)
4. **Vesting Period:** Period from Grant Date to Vesting Date. (It may be more than 1 year)
5. **Exercise Period:** This Period starts after the vesting date, during which employee can exercise the Share based payment plan.
6. **Exercise Price:** Price at which employees can purchase the Share options (this is discounted price)

5. VESTING CONDITIONS

Some share-based payment transactions include VESTING CONDITIONS that must be satisfied before any payment is made. IND AS 102 recognizes 2 types of Vesting Conditions:

1. Service Conditions:

They require the counterparty to complete a specified period of service. A service condition does not require a performance target to be met.

2. Performance conditions:

They require the counterparty to complete a specified period of services **AND** specified performance targets to be met.

Performance conditions are of two types:

- 1) Non-market performance conditions: exercisability of option depends on employee's hard work
- 2) Market-based performance conditions: exercisability of option depends on market price of entity's share.

How to deal with Vesting Conditions?

<u>Vesting Condition doesn't exist</u>	<u>Vesting Condition exist and given in the Question</u>
<p>No Vesting Condition means Share option is vested Immediately on grant date.</p> <p>Entire expense is recognised immediately in Profit and loss A/c.</p>	<p>Option will be vested (eligible) only when condition is fulfilled during the vesting period.</p> <p>Expense is deferred and amortised during the vesting period based on best available estimate.</p>
	<p><u>If Vesting Condition is not satisfied:</u> Expense should not be recognised because of failure of condition. Any expense recognised till date shall be reversed.</p> <p style="color: #C00000;">(Refer Practical Example 2)</p> <p><u>All Vesting Conditions are satisfied except Market based performance condition:</u> Here expense shall be recognised over the vesting period even though the option could not be exercised because of non fulfilment of market conditions.</p> <p style="color: #C00000;">(Refer Q204 of QR Question Bank Compiler)</p>

6. EQUITY SETTLED SHARE BASED PAYMENT WITH EMPLOYEES

- Employee benefit expense is calculated based on **fair value of Options** announced.
- Fair value is calculated by using the **Option pricing model** and it is **always given in the question**.
- Fair value is considered on **Grant Date only**. Any change in fair value after the grant date is ignored.
- Every year's expense is calculated as under:

A	No. of Employees expected to fulfill the Vesting Conditions X No. of Options per Employee X Fair Value of option at grant date (This is to be done every year)	XXXX
B	Total Vesting Period (VP) (sometimes VP is estimated and revised accordingly based on changes in the expectations)	XX
C	$(A \div B) \times$ No. of years lapsed till date	XXXX
D	Expense already Recognised till Previous Year	XXXX
E	Expense for the year (C - D) If this amount is negative, then it means it is to be reversed.	XXX

- **Journal Entries:**

1	At each year end (during vesting period) Employee Benefit Expenses (P&L) A/c Dr. To Share Based Payments Reserve A/c
2	When Option is exercised after Vesting Period: Share Based Payment Reserve A/c Dr. Bank A/c Dr. To Equity Share Capital A/c To Security Premium A/c
3	When Option is not vested (condition is not satisfied) Share Based Payment Reserve A/c Dr. To Employee Benefit Expense (P&L) A/c
4	When Option is vested but lapsed (not exercised) Share Based Payment Reserve A/c Dr. To Retained Earnings (General Reserves) A/c

(Refer Practical Example 1)

(Also Refer Series 200 Questions from QR Question Bank Compiler)

7. HOW TO DEAL WITH CHANGES IN EQUITY SETTLED PAYMENTS

Sometimes, an entity might change the terms of the share-based payment transaction. These are as follows:

(a) **MODIFICATION: (also known as Repricing)**

- It means making some changes in the option in favor of employees.
- It increases the benefits for employees
- It is treated as a separate Plan, hence the original SBP plan is continued as it is.
- Accounting for Separate Plan:
 1. Calculate incremental fair value as on the date of Repricing:

Fair Value of Modified Option as on repricing date	XX
(-) Fair Value of Original Option as on repricing date	XX
 2. Incremental Fair Value is recognised as an additional expense from modification date to end of vesting date on SLM basis just like original plan.

(Refer Practical Example 3) (Also Refer Series 500 Questions of QR Question Bank Compiler)

Note:

Under Modification: If the fair value of the new instrument is **lower** than the fair value of the old instrument, the modification is ignored. Only original plan shall continue.

(b) **CANCELLATION OF EQUITY SETTLED OPTIONS:**

If an entity **cancels or settles** the equity instruments, then it is treated as Vested to all current employees immediately on the date of cancellation.

Hence the entire remaining expense (unrecognized amount) is recognised immediately.

Entity shall apply following steps to account cancellation of SBP option:

Step 1: Recognise full remaining expense on the date of Cancellation of option:

Employee Benefit Expenses A/c Dr.
To Share Based Payment Reserve A/c

Step 2:

Convert SBP Reserve A/c into SBP Liability (Compensation due to cancellation) at Fair Value of Option on the date of cancellation:

Share Based Payment Reserve A/c Dr.
To SBP Liability A/c

Step 3: Remaining Balance of SBP Reserve is reclassified to retained earnings:

Share Based Payment Reserve A/c Dr.
To General Reserve (R/E) A/c

Step 4:

Discharge the Actual Compensation at actual promised amount (which may be different from fair value of option) and transfer the difference to Profit and loss A/c:

Share Based Payment Liability A/c Dr.
 Profit and loss A/c Dr. (difference)
 To Bank (Compensation paid) A/c
 To Profit and Loss A/c (difference)

(Refer Series 600 Questions of QR Question Bank Compiler)

8. CASH SETTLED SHARE BASED PAYMENT PLAN

- Cash Settled Share based payment is also known as **Share Appreciation Rights (SAR)**
- Employees are **entitled to cash payment** in the future based on the **increase of the entity's share price** over specified period of time from a specified level.
- Such increase in share price is known as **"Intrinsic Value"** (Market Price at Exercise Date less Grant Date Exercise Price)
- Cash Settled SBP are recognised as **the Liability** of the Entity since there is a cash outflow.
- The fair value of the liability must be **remeasured at each reporting date** until this liability is settled and **any changes of fair value** are recognized in **profit or loss**.
- Calculation of each year's expense is same as Equity Settled plan, however **fair value of option must be considered for each balance sheet date**.
- **Journal Entries:**

1	At each year end (during vesting period) Employee Benefit Expenses (P&L) A/c Dr. To Share Based Payments Liability A/c
2	When Option is exercised after Vesting Period: Share Based Payment Liability A/c Dr. (Carrying Amount) To Bank A/c (Actual Payment) Difference in above entry is transfer to P&L A/c
	<ul style="list-style-type: none"> • Actual Payment means payment made at intrinsic value of share which is treated as actual appreciation. • If intrinsic value is not given then actual appreciation is calculated as follow: Market Price on Exercise date (-) Grant Date Exercise Price

(Refer Series 300 Questions of QR Question Bank Compiler)

Note: -

Repricing shall be done only in the case of equity settled option. If the cash settled option is given in question and question talks about reprising, then no need to recognize additional expense since under cash option we always take revised Fair Value for liability. **(Refer Q404)**

9. EQUITY SETTLED TRANSACTION WITH CASH ALTERNATIVES

Here, the entity provides choice to employees between Equity Option and Cash Option.

Apply following Steps to recognise the Expense:

Step 1: Calculate **Fair Value of Equity Option** as on Grant date as under:

No. of Equity Settled options offered X Fair Value for Equity Option

(Fair Value for Equity option will be given after considering any restrictions attached to that option)

Step 2: Calculate **Fair Value of Cash Alternative** as on Grant date as under:

No. of Options under Cash alternative X Fair Value for Cash Option

Step 3: If Fair Value of Equity Option (Step 1) is higher than Fair Value of Cash Option (Step 2), difference will be Recognised as **Expense under Equity Option** over the Vesting Period as per the Fair Value on Grant date only. (i.e. create SBP Reserve).

(If Step 2 is more than Step 1 then we shall not create SBP reserves)

Step 4: Amount equal to Step 2 will be Recognised as **Expense under Cash Option** over the Vesting Period as per the Revised Fair Values as on each Balance Sheet Date. (i.e. create SBP Liability).

Now after the vesting period is over, either Equity Option or Cash option will be exercised as per the counter party's choice. Apply following treatment as under:

If Cash Option is exercised	If Equity Option is exercised
<u>Transfer the balance of SBP reserve to retained earnings:</u> SBP Reserve A/c Dr. To General Reserve (R/E)	<u>Transfer entire SBP liability to SBP Reserve:</u> SBP Liability A/c Dr. To SBP Reserve A/c
<u>Make Payment of SBP Liability:</u> SBP Liability A/c Dr. (Carrying Amt.) To Bank A/c (Actual Payment) Difference is transfer to P&L	<u>Issue the Shares:</u> SBP Reserve A/c Dr. To Equity Share Capital A/c To Securities Premium A/c

(Refer Series 400 Questions of QR Question Bank Compiler)

10. GROUP SHARE BASED PAYMENT PLAN

Situation 1: Parent issues its own shares for the share-based payment plan announced by its Subsidiary co.

1. Books of Subsidiary Co.:

- Subsidiary co. must recognize "Employees Benefit Expenses"
- If subsidiary co. will compensate holding co. in cash, then **Bank A/c** will be credited.
- The remaining balance will be transfer to "other equity" in the name of (Eg.: Contribution by Holding Co.)

Recognition of Expense	Employee Benefit Exp. (P&L) A/c Dr. To Bank A/c (if paid) To Equity Contribution by Parent co. A/c
------------------------	--

2. Books of Holding Co.:

- That part of Employee expense which is reimbursed by subsidiary will be debited to Bank A/c
- That part of Employee expense which is not recoverable is debited to Investment in Subsidiary A/c.
- The credit will be given to Equity Share Capital and Security Premium A/c.

Share Settlement	Bank A/c Dr. (if Compensation received) Investment in Subsidiary A/c Dr. (to the extent of loss) To Equity Share Capital A/c To Security Premium A/c
------------------	---

Situation 2: Subsidiary issues its own shares for the share-based payment plan announced by its Parent co.

Books of Subsidiary Co.:

Treat Dividend distribution to Parent	Dividend Exp. A/c Dr. To SBP Reserve A/c SBP Reserve A/c Dr. To Equity Share Capital A/c To Securities Premium A/c
---------------------------------------	--

2. Books of Holding Co.:

Recognition of Employee Expense & Dividend Income	Employee Benefit Expense A/c (P&L) Dr. To Dividend Income A/c
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(Refer Series 700 Questions of QR Question Bank Compiler)

11. SHARE BASED PAYMENT TRANSACTION WITH OTHER PARTIES (Other than Employees)

Example: Purchase of Goods, PPE or Taking services.

Equity Settled Option	Cash Settled Option
PPE/Expenses Dr. To SBP Reserve A/c	PPE/Expenses Dr. To SBP Liability A/c
SBP Reserve A/c To Equity Share Capital A/c To Securities Premium A/c	SBP Liability A/c To Bank A/c
Services may be received on continuous basis, in that case recognise the expense on monthly basis as per SLM.	

(Refer Q101 & Q102 from QR Question Bank Compiler)

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IND AS 7

STATEMENT OF CASH FLOWS

1. WHY INDAS - 7?

The statement of cash flows shows:-

- the ability of any company to generate cash.
- HOW MUCH CASH the company generated over the year
- from WHERE the cash was generated
- movements in cash and cash equivalents

2. WHAT COMPRISES CASH AND CASH EQUIVELANT?

Cash comprises cash on hand (e.g., petty cash) and demand deposits (e.g., bank accounts).

Cash equivalents are short-term, highly liquid investments that are readily convertible to known amounts of cash and which are subject to an insignificant risk of changes in value.

Here, the investment with short maturity (up to 3 months) would qualify for cash equivalent - for example, state Treasury note. However, most shares and other equity instruments are excluded from cash equivalents.

Under Ind AS 7 "where bank overdrafts which are repayable on demand form an integral part of an entity's cash management, bank overdrafts are included as a component of cash and cash equivalents. However, Bank overdraft, in the balance sheet, will be included within financial liabilities.

3. HOW THE STATEMENT OF CASH FLOWS SHALL BE PRESENTED?

In the Cash Flow Statement, Cash flows during the period are classified by operating, investing and financing activities.

In the notes to the financial statements, an entity shall disclose the components of cash and cash equivalents.

STATEMENT of CASH FLOW

Particulars	Amount
Cash flow from Operating Activity	XXX
(+/-) Cash flow from Investing Activity	XXX

(+/-) Cash flow from Financing Activity	XXX
Net cash flow	XXX
(+) Opening balance of cash and cash equivalent	XXX
Closing balance of cash and cash equivalent	XXX

4. OPERATING ACTIVITIES

Operating activities are the **principal revenue-producing activities** of the entity and other activities that are not investing or financing activities.

Cash flows from operating activities might be **different for different entities**.

For example, manufacturing company would report advance given for the acquisition of PPE as investing activity, but the bank would report similar advance as an operating activity based on its specific purpose.

Examples of Operating activities are:

- Cash receipts from the sale of goods and the rendering of services.
- Cash receipts from royalties, fees, commissions and other revenue.
- Cash payments to suppliers for goods and services.
- Cash payments to and on behalf of employees.
- Cash receipts and cash payments of an insurance entity for premiums and claims, annuities and other policy benefits.
- Cash payments or refunds of income taxes unless they can be specifically identified with financing and investing activities; and
- Cash receipts and payments from contracts held for dealing or trading purposes.

DIRECT AND INDIRECT METHOD

A company may select from **2 methods** of reporting cash flows from operating activities:

1. **Direct method:** here, you need to disclose major classes of gross cash receipts and gross cash payments; or
2. **Indirect method:** here, you start with the profit or loss before tax and then you adjust it for the effect of:
 - **Working capital changes over the period (inventories, operating receivables, payables);**
 - **Non-cash items (depreciation, unrealized foreign exchange gains or losses, etc.);**
 - **Items associated with investing or financing activities.**

INDIRECT METHOD (Format)

Particulars	Amount
Net profit before tax	XXX
(+/-) <u>Adjustment for non-cash & non-operating item</u>	
(+) Depreciation/ Amortisation	XX
(+) Bad-debts / provision for Bad-debts	XX

(+/-) Forex Gain / Loss	XX
(+) Impairment loss	XX
(+) Finance Cost (Interest)	XX
(-) Interest Income and dividend	XX
(+/-) Gain or loss on sale of any asset	XX
(+) Share based payment expense (non-cash)	XX
(+/-) Loss / gain on Remeasurement of financial instrument (non-cash)	XX
Cash Flow before Working capital changes	XXX
(+/-) <u>Adjustment for Working capital changes</u>	
(+) Decrease in current asset	XX
(-) Increase in current asset	XX
(+) Increase in current liability	XX
(-) Decrease in current liability	XX
(-) Tax paid	XX
Net cash flow from Operating activity	XXX

Direct method provides more understandable information not disclosed under indirect method. However, in reality, **indirect method** is far more preferred because it's easier to get the information based on your accounting records. (in most cases).

5. INVESTING ACTIVITIES

Investing activities are the acquisition and disposal of long-term assets and other investments not included in cash equivalents.

Examples of cash flows classified in investing activities are:

- Cash payments to acquire property, plant and equipment, intangibles and other long-term assets (including capitalized development costs and self-constructed PPE);
- Cash receipts from sales of PPE, intangibles and other long-term assets;
- Cash payments to acquire and cash receipts from sales of equity or debt instruments of other entities and interests in joint ventures (but not for trading or dealing purposes);
- Cash advances and loans made to other parties, and cash receipts from their repayment (other than advances and loans made by a financial institution - these would go to operating part);
- Cash payments for and cash receipts from various derivative contracts except when the contracts are held for dealing or trading purposes, or the payments are classified as financing activities.

6. FINANCING ACTIVITIES

Financing activities are activities that result in changes in the size and composition of the contributed equity and borrowings of the entity.

Examples of cash flows arising from financing activities are:

- Cash proceeds from issuing shares or other equity instruments;
- Cash payments to owners to acquire or redeem the entity's shares;
- Cash proceeds from issuing debentures, loans, notes, bonds, mortgages and other short-term or long-term borrowings;
- Cash repayments of amounts borrowed; and
- Cash payments by a lessee for the reduction of the outstanding liability relating to a finance lease.

7. IMPORTANT AND SPECIAL AREAS

REPORTING CASH FLOWS FROM INVESTING AND FINANCING ACTIVITIES

Cash flows from investing and financing activities shall always be **reported GROSS**, so no netting off. (Unless there is an intention to settle on **NET BASIS**)

Example

If in the year 20X1-20X2, some land is purchased for Rs. 2.5 crores and another land is sold for Rs. 3.5 crores then while presenting the information, entity shall show separately outflow of Rs. 2.5 crores and inflow of Rs. 3.5 crores.

However, INDAS - 7 gives you **2 exceptions** where you actually can present net:

- Cash receipts and payments **on behalf of customers** when the cash flows reflect the activities of the customer rather than those of the entity. For example, some real estate company can collect rents from tenants and pay them over to the property owners.
- Cash receipts and payments for **items in which the turnover is quick, the amounts are large, and the maturities are short**. For example, changes in principal amounts relating to credit card customers.

Also, financial institutions can report certain transactions on the net basis.

FOREIGN CURRENCY CASH FLOWS

- When there are foreign currency cash flows, then you need to translate them to your functional currency by applying the **exchange rate at the date of the cash flow**.
- **Exchange Gains/Losses recognised as per Ind AS 21 are not cash flows**.
- If exchange gains/losses are related to cash or cash equivalents, then these should be **presented separately for the final reconciliation**.

Example

Entity A (Indian Company) purchased goods for resale from France during January for EUR 10,000 (Exchange rate: 1 EUR = Rs. 70) on a credit period of 4 months. It accounted for the purchase of inventory at Rs. 7,00,000 (10,000 × 70). On 31st March, the exchange rate has changed to 1 EUR = Rs. 65. This would mean an unrealised gain due to exchange fluctuation of Rs. 50,000 (since the payables will be recorded at Rs. 6,50,000 (at closing exchange rate).

Assuming that the inventory is unsold at that date, the movement is reported as under:

Profit	Rs. 50,000
Less: Increase in Inventory	Rs. (7,00,000)
Add: Increase in Payables	Rs. 6,50,000
Net Cash flows from operating activities	Rs. 0

INTEREST AND DIVIDEND

	Financing Company	Other Company
Interest Paid	Operating Activities	Financing Activities
Interest and Dividend Received	Operating Activities	Investing Activities
Dividends Paid	Financing Activities	Financing Activities

TAXES ON INCOME

- Generally, cash flows arising from income taxes are classified as cash flows from **operating activities**.
- However, if they can be specifically identified for either financing or investing such as long term capital gain tax on sale of property, then it should be reported under cash flows in investing or financing activities.

PROPERTIES BUILT FOR LET OUT

- Cash payments to manufacture or acquire assets held for rental to others and subsequently held for sale are cash flows from **operating activities**.
- The cash receipts from rents and subsequent sales of such assets are also cash flows from **operating activities**.

OPERATIONS OF FINANCIAL COMPANIES AND BANKS

Cash flows arising from the **cash advances and loans made**, purchase and sale of **securities and loans for dealing or trading purposes** are classified as **operating activities**.

INVESTMENTS IN SUBSIDIARIES, ASSOCIATES AND JOINT VENTURES

- Investment in Subsidiary/Associate/Joint Venture is cash outflow under **Investing Activity**.
- Sale of Investment in Subsidiary/Associate/Joint Venture without loss of control is cash outflow under **Financing Activity**.

- Sale of Investment in Subsidiary/Associate/Joint Venture with loss of control is cash outflow under **Investing Activity**.
- Investment entity such as Venture Capital Co. or Mutual Fund Co., if they obtain or sale any investment then it is **Operation Activity**.

(Refer Practical Example 1 for All Important Adjustments at one place)