Implementation of IND AS -
Impact on Corporate Tax

CA Dinesh Patil
16 November 2019
Introduction, Features and Roadmap

Components of Financial Statements

Impact on income-tax

Liability and Assets

Inventories

Provisions, Contingent Liabilities and Contingent Assets

Key take-aways
Introduction, Features and Roadmap
Indian Accounting Standards (Ind AS)

**IFRS Adoption**
Implementing in exact form as issued by International Accounting Standards Board (IASB)

**IFRS Covergence**
Implementing IFRS with certain departures to suit the country

### Ind AS – India perspective
Companies (Indian Accounting Standard Rules), 2015

- **IFRS**
- **Carve-outs**
- **IND-AS**

**Has carve outs and carve ins as compared to IFRS**

**New standard on revenue recognition incorporated**
Salient features of IFRS converged Ind AS

<table>
<thead>
<tr>
<th>Feature</th>
<th>Description</th>
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</thead>
<tbody>
<tr>
<td>Principle-based Standards</td>
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<tr>
<td>More importance to concept of ‘substance over form’</td>
<td></td>
</tr>
<tr>
<td>Reliance on fair valuation, and measurements on time value of money</td>
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<tr>
<td>Require more disclosures of all relevant information and assumptions</td>
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<tr>
<td>Require higher degree of judgment and estimates</td>
<td></td>
</tr>
<tr>
<td>Restatement of previously issued Financial statements</td>
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</tr>
</tbody>
</table>
Roadmap of implementation of Ind AS in India

### MANDATORY IMPLEMENTATION OF IND-AS

#### PHASE I
- Listed Companies or Companies in the process of Listing and having net worth of INR 500 Crores or more (debt or equity, In or outside India listing)
- All other unlisted Companies having net worth of INR 500 Crores or more
- Holding, Subsidiary, Joint venture or Associates of companies covered above

Accounting period beginning from 1 April 2016 with comparatives for March 2016

#### PHASE II
- Listed Companies or Companies in the process of Listing and having net worth of less than INR 500 Crores or more (debt or equity, In or outside India listing)
- All other unlisted Companies having net worth of INR 250 Crores or more but less than INR 500 Crores
- Holding, Subsidiary, Joint venture or Associates of companies covered above

Accounting period beginning from 1 April 2017 with comparatives for March 2017

### VOLUNTARY IMPLEMENTATION

Any company can voluntarily adopt Ind AS from year beginning 1 April 2015 with comparative for 2014-15

### KEY MATTERS

- Companies listed in SMEs need not follow Ind AS
- Separate roadmap for Banks, Insurance Companies and NBFCs

Once Ind AS is followed, it should be followed for all subsequent years
Components of Financial Statements
Components of IND-AS Financial Statements

- Balance sheet at the end of the period
- Statement of profit and loss for the period (including Other Comprehensive income ‘OCI’)
- Statement of changes in equity for the period
- Statement of cash flows for the period
- Notes comprising summary of significant accounting policies and other explanatory information
- Comparative information in respect of the preceding period
## Format of Statement of Profit & Loss Account

<table>
<thead>
<tr>
<th>Statement of Profit and Loss account</th>
<th>Current Period</th>
<th>Previous period</th>
</tr>
</thead>
<tbody>
<tr>
<td><strong>Revenue</strong></td>
<td></td>
<td></td>
</tr>
<tr>
<td>Revenue from Operations</td>
<td></td>
<td></td>
</tr>
<tr>
<td>Other income</td>
<td></td>
<td></td>
</tr>
<tr>
<td><strong>Total Income from operations</strong></td>
<td></td>
<td></td>
</tr>
<tr>
<td><strong>Expenses</strong></td>
<td></td>
<td></td>
</tr>
<tr>
<td>Cost of Materials consumed</td>
<td></td>
<td></td>
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<tr>
<td>Excise duty</td>
<td></td>
<td></td>
</tr>
<tr>
<td>Purchase of stock-in-trade</td>
<td></td>
<td></td>
</tr>
<tr>
<td>Changes in inventories of finished goods, stock-in-trade and work-in-progress</td>
<td></td>
<td></td>
</tr>
<tr>
<td>Employee Benefit expenses</td>
<td></td>
<td></td>
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<tr>
<td>Finance cost</td>
<td></td>
<td></td>
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<tr>
<td>Depreciation and Amortization expenses</td>
<td></td>
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<tr>
<td>Other expenses</td>
<td></td>
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<tr>
<td><strong>Total Expenses</strong></td>
<td></td>
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</tr>
<tr>
<td>Statement of Profit and Loss account</td>
<td>Current Period</td>
<td>Previous period</td>
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<tr>
<td>-------------------------------------</td>
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</tr>
<tr>
<td><strong>Profit before tax</strong></td>
<td></td>
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<tr>
<td>Tax expense</td>
<td></td>
<td></td>
</tr>
<tr>
<td>(i) Current tax</td>
<td></td>
<td></td>
</tr>
<tr>
<td>(ii) Deferred tax</td>
<td></td>
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</tr>
<tr>
<td>Profit (Loss) for the period from continuing operations</td>
<td></td>
<td></td>
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<tr>
<td>Profit/(loss) from discontinued operations</td>
<td></td>
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<tr>
<td>Tax expense of discontinued operations</td>
<td></td>
<td></td>
</tr>
<tr>
<td>Profit/(loss) from Discontinued operations(after tax)</td>
<td></td>
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<tr>
<td><strong>Profit/(loss) for the period</strong></td>
<td></td>
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<tr>
<td><strong>Other comprehensive Income</strong></td>
<td></td>
<td></td>
</tr>
<tr>
<td>A. (i) Items that will not be reclassified to profit or loss (revaluation, re-measurement of defined benefit plan etc.)</td>
<td></td>
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</tr>
<tr>
<td>(ii) Income tax relating to items that will not be reclassified to profit or loss</td>
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<td></td>
</tr>
<tr>
<td>B. (i) Items that will be reclassified to profit or loss (exchange difference in translation of financial statement of foreign operations)</td>
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<td></td>
</tr>
<tr>
<td>(ii) Income tax relating to items that will be reclassified to profit or loss</td>
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<tr>
<td><strong>Total comprehensive income for the period</strong></td>
<td></td>
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</tr>
</tbody>
</table>
Impact on income-tax
International view on impact of IFRS on tax computation

- Separate tax legislation that deals with IFRS conversion
- Computation of income is prepared based on domestic tax laws and IFRS adjustments are ignored

- Tax rules are largely based on GAAP. As the number of differences between IFRS and GAAP increase, the number of adjustments required increases
- Annual accounts is prepared on the basis of Dutch GAAP, tax return is based on these financials and taking into account business principles

Taxable profit is principally based on the legal entity’s statutory accounts, with adjustments in local tax law
## Tax impact calculations - reliance on books of accounts

<table>
<thead>
<tr>
<th>Topic</th>
<th>Description</th>
</tr>
</thead>
<tbody>
<tr>
<td>Forms basis of book profits for MAT taxation</td>
<td></td>
</tr>
<tr>
<td>Transfer pricing - determination of ALP, comparability, etc.</td>
<td></td>
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<tr>
<td>Limits on interest deduction paid or payable to AE</td>
<td></td>
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<tr>
<td>Impact on disallowance under section 14A</td>
<td></td>
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<tr>
<td>Determination of ‘accumulated profits’ for the purpose of deemed dividends</td>
<td></td>
</tr>
<tr>
<td>Ascertaining fair market value for the purpose of taxability under section 56(2)(x) / 50CA</td>
<td></td>
</tr>
<tr>
<td>Computation of cost of undertaking under slump sale</td>
<td></td>
</tr>
<tr>
<td>Properties/ Liabilities are transferred at books values in case of demerger</td>
<td></td>
</tr>
</tbody>
</table>
Interplay between Ind AS and Income Tax

Accounting under Ind AS

- Impact on MAT
  - Guidance under section 115JB and FAQ
    - Specific adjustment as prescribed to be made

- Impact under normal provision of Income tax Act
  - Treatment covered under ICDS* or Act
    - Follow treatment as per ICDS or Act or Binding Judicial precedents
  - Treatment neither covered by ICDS nor Act
    - Interpret using Judicial precedents

Given statutory recognition from AY 2017-18
Interplay between Ind AS and Income Tax

Key Principles for computing taxable income:

- Business income is computed in accordance with the method of accounting regularly employed by the taxpayer – could be either cash or mercantile / accrual

- Business income as per method of accounting adopted to be adjusted by the specific deductions / allowances / disallowances specified in the Act

- Real income is taxable and not hypothetical income
  - unrealized gains / losses not recognized for tax computation

- Concept of time value of money not recognized

- Notional expenses not allowable. However, provisions are allowed if created on a scientific basis

- Adjustments to be made to accounting profits as per notified Income Computation and Disclosure Standards (ICDS) - effective from FY 2016-17

Profits as computed following Ind AS to be the starting point for computing taxable income and further adjusted in the light of principles stated above.
## Impact on Income tax - Specific Ind AS

### Assets & Liabilities
- Financial Liability and Assets: Ind AS 32, Ind AS 109, Ind AS 107 & Ind AS 113
- Inventories – Ind-AS 2
- Provisions, Contingent Liabilities and Contingent Assets: Ind AS 37
- Property, Plant, Equipment's (IND AS 16)
- Intangible Assets (IND AS 38)

### Income and expense
- Revenue recognition - IND AS 115
- The Effect of Changes in Foreign Exchange Rates – Ind-AS 21
- Borrowing cost – Ind-AS 23
- Government Grants (IND AS 20)

### MAT Impact
Financial Liability and Assets: Ind AS 32, Ind AS 109, Ind AS 107 & Ind AS 113
Overview of the FI standards - Ind AS 32, 109, Ind AS 107 & Ind AS 113

- Liability and asset classification
  Ind AS 32: FI: Presentation

- Recognition and derecognition
  Classification & Measurement
  Derivatives
  Hedge accounting
  Ind AS 109- Financial Instruments

- Disclosures
  Ind AS 107: FI: Disclosures

- Fair value measurements- Ind AS 113
Financial Instrument - Definition

Any Contract that gives rise to

A financial liability or equity of another entity

A financial asset of one entity
Liability or equity: Classification per Ind AS 32

Contractual obligation to deliver cash or another financial asset or exchange financial assets/liabilities under potentially unfavourable conditions

Liability

Residual interest in the assets of the enterprise after deducting its liabilities

Equity

Substance over form
Preference shares - financial liability or equity?

Preference shares to be classified as a financial liability if all the following conditions are met:

- they are redeemable on a specific date
- they are redeemable at the option of the holder
- Issuer obligated to make payments in form of interest or dividend

Related dividend will appear above the line in the profit and loss account.
Substance over form or legal structure?

**Substance over Form**

Accounts and the accounting method followed by an assessee continuously for a given period of time needs to be presumed to be correct till the AO comes to the conclusion for reasons to be given that the system does not reflect true and correct profits;

*CIT vs. Woodward Governor (Supreme Court)*

**Legal Form**

The true effect of accretion made pursuant to the contract has to be judged not by artificial rules but from the intention of the parties to the contract....

*State of Andhra Pradesh v. Kone Elevators India PVt. Ltd (Supreme Court)*

Two exceptions are noted for recharacterisation for transaction where (i) where the economic substance of a transaction differs from its form and (ii) where the form and substance of the transaction are the same but arrangements made in relation to the transaction, viewed in their totality, differ from those which would have been adopted by independent enterprises behaving in a commercially rational manner.

*EKL Appliances Ltd (Delhi High Court)*
**Finnish Supreme Court**

- The taxpayer was a Finnish company (FI Co) which was 95.7% owned by a company resident in Luxembourg (LU Co).

- In 2009, FI Co received a loan of EUR 15 million from LU Co and wanted to deduct EUR 1,337,500 as interest expenses paid to LU Co.

- The loan was given without any collateral and did not have any provisions for repayment by a definite date. The interest rate was fixed at 30% and the interest was added to the principal. The loan could be paid back only upon FI Co’s request and was under IFRS accounting rules treated as equity (hybrid loan).

- The Finnish tax authorities recharacterized the loan as equity investment and consequently, disallowed the interest deduction.

**Issue**

Whether the loan could be re-characterized as equity investment and, consequently, the interest paid for such loan could be disallowed.
Amortised cost and effective interest method

Amortised cost = Initial recognition amount - Cash received -/+ Interest income / expense - Impairment

Amortised cost is calculated using the effective interest rate method

**Example**
1. Loan of Rs. 1000 received after reducing upfront fees of Rs. 100.
2. The loan is repayable after 2 years, without payment of interest.
3. Assuming interest discounting rate of 10% p.a., the amortised cost of Rs. 900 (Rs. 1000 – Rs. 100) would be at Rs. 744.
4. Balance amount i.e. Rs. 156 (900-744) would be considered as interest.
## Financial liabilities treatment

<table>
<thead>
<tr>
<th>Instrument</th>
<th>Indian GAAP</th>
<th>Ind AS</th>
<th>Tax/ MAT</th>
</tr>
</thead>
<tbody>
<tr>
<td>Non-convertible debentures</td>
<td>• No specific accounting standard</td>
<td>• Classified at amortised cost</td>
<td>• Actual interest expense deductible on accrual basis subject to the provision of section 36(1)(iii) of the Act</td>
</tr>
<tr>
<td></td>
<td>• Fees / costs paid on origination recognized as expense upfront</td>
<td>• Interest expense recognized based on effective interest rate resulting into amortization of upfront fees / costs</td>
<td>• Notional interest expense to be disallowed.</td>
</tr>
<tr>
<td></td>
<td></td>
<td>• Interest expense recognized based on effective interest rate resulting into amortization of upfront fees / costs</td>
<td>• The deductibility of issue expenses (i.e. fees etc.) should be dealt with basis the basic principle of taxation (i.e. accrual) and the prevailing judicial precedents</td>
</tr>
<tr>
<td>Term loans / CC /OD</td>
<td></td>
<td>• Interest expense recognized based on effective interest rate resulting into amortization of upfront fees / costs</td>
<td>• No adjustment to be made in MAT computation (including for notional interest).</td>
</tr>
<tr>
<td>Trade payables</td>
<td></td>
<td>• Interest expense recognized based on effective interest rate resulting into amortization of upfront fees / costs</td>
<td></td>
</tr>
<tr>
<td>Convertible Preference shares</td>
<td>• No specific accounting standard</td>
<td>• May be treated as a compound instrument- requirement to split between equity and liability component</td>
<td>• Any amount debited to profit and loss account towards interest or dividend to be disallowed.</td>
</tr>
<tr>
<td></td>
<td>• Fees / costs paid on origination recognized as expense upfront</td>
<td>• Interest expense recognized based on effective interest rate resulting into amortization of upfront fees / costs</td>
<td>• Issues expenses, such as fees/ costs, etc. to be disallowed under normal tax computation.</td>
</tr>
<tr>
<td></td>
<td></td>
<td></td>
<td>• Under MAT - Dividend/ interest debited to be added back to the Book profit (FAQ-8).</td>
</tr>
</tbody>
</table>
Financial Asset is

<table>
<thead>
<tr>
<th>Cash</th>
<th>An equity instrument of another entity</th>
</tr>
</thead>
<tbody>
<tr>
<td>A contractual right to</td>
<td></td>
</tr>
<tr>
<td>Receive cash or other financial asset or</td>
<td>Exchange financial assets or financial liabilities with another entity under conditions that are potentially favourable to the entity</td>
</tr>
<tr>
<td>Certain contracts that may be settled in the entity’s own equity instruments</td>
<td></td>
</tr>
</tbody>
</table>
*Initial Measurement*

**Transaction Costs**: For any asset that is not measured at FVTPL, the initial value will include transaction costs.

- **FVTPL** Immediate expense
- FVTOCI Transfer to OCI and Disposal or impairment
- Financial Assets At amortized cost Using effective interest rate
- Financial Liabilities at amortized cost Using effective interest rate

"Fair value is the **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.**"
Case study - Loan to Subsidiaries at less than market rate

### Ind AS

#### Accounting of loan to Subsidiaries

- A two year interest free loan of INR 1,000 to a subsidiary is recasted in books of accounts to recognize INR 900 as principal and INR 100 as interest

<table>
<thead>
<tr>
<th>In the books of Parent</th>
<th>Accounting of loan to subsidiaries as per Ind AS</th>
</tr>
</thead>
<tbody>
<tr>
<td>Loan to Subsidiary account Dr</td>
<td>900</td>
</tr>
<tr>
<td>Investment in Subsidiary account Dr</td>
<td>100</td>
</tr>
<tr>
<td>To Bank account Cr</td>
<td>1000</td>
</tr>
</tbody>
</table>

<table>
<thead>
<tr>
<th>In the books of Subsidiary</th>
<th>Accounting of loan from holding company as per Ind AS</th>
</tr>
</thead>
<tbody>
<tr>
<td>Bank account Dr</td>
<td>1000</td>
</tr>
<tr>
<td>To Loan from Parent Dr</td>
<td>900</td>
</tr>
<tr>
<td>To Equity account Cr</td>
<td>100</td>
</tr>
</tbody>
</table>

<table>
<thead>
<tr>
<th>Accounting of interest income (yearly)</th>
<th>Accounting of interest expense (yearly)</th>
</tr>
</thead>
<tbody>
<tr>
<td>Loan to Subsidiary account Dr</td>
<td>50</td>
</tr>
<tr>
<td>To Interest income account (Interest income recognized every year for 2 years)</td>
<td>50</td>
</tr>
<tr>
<td>Interest expense Dr</td>
<td>50</td>
</tr>
<tr>
<td>To Loan from parent account Cr (Interest expense recognized every year for 2 years)</td>
<td>50</td>
</tr>
</tbody>
</table>
Income & Expenses - Factors to be tested

**Income**

- Whether defined under the Act – Section 2 (24)?
- Whether covered by deeming provisions?
- Whether represents accrual in wealth or increase in profits?
- Whether represents real profits?

**Expenses**

- Whether represents actual outgo?
- Whether can be categorized as losses?
- Whether allowable on deemed basis?
- Whether merely an accounting entry?
Interplay between Ind AS and Income Tax - Certain issues

Issue 1:
If Ind AS results in notional income or expenses to be recognized in the P&L Account and there is no specific guidance under the Act / ICDS, what treatment to be adopted?

Solution:
The SC vindicated this position in the case of C.I.T. v. Shoorji Vallabhdas & Co. holding as under –

“Income-tax is a levy on income. No doubt, the Income-tax Act takes into account two points of time at which the liability to tax is attracted, viz. the accrual of the income or its receipt; but the substance of the matter is the income. If income does not result at all, there cannot be a tax, even though in book-keeping, an entry is made about a hypothetical income, which does not materialise. Where income has, in fact, been received and is subsequently given up, in such circumstances that it remains the income of the recipient, even though given up, the tax may be payable. Where, however, the income can be said not to have resulted at all, there is obviously neither accrual nor receipt of income, even though an entry to that effect might, in certain circumstances, have been made in the books of account.”

Thus, based on above argument it is clear that Notional Income or notional expenses cannot be taxed or allowed under Income Tax
Real expenditure or Notional expenditure

What is material for the purpose of section 145 is, the method to be such that the real income, profit and gain can be properly deduced therefrom. If the method adopted does not afford true picture of profit, it would be rejected, but then such rejection should be based on cogent evidence and would be done with caution.

Sanjeev Woollen Mills (Supreme Court)

Expenditure relates to something paid out or spent which indicates a sort of volition, something which comes out of the pocket and spent.


Neither a debit for a notional amount

K. Sankaranarayana Iyer & Sons v. CIT, (1980) 14 CTR (Mad) 219, 220
Interplay between Ind AS and Income Tax - Certain issues

Issue 2:
Can assessee choose one method for accounting and a different method for tax purposes?

Possible Views subject to ICDS specific adjustments:
View 1: Assessee has option to choose ICAI AS for tax purpose
View 2: Assessee has to mandatorily follow Ind AS for tax purpose

Analysis:
Under Income-tax Act, Sec. 44AA & 44AB takes care of requirement to maintain books of accounts & tax Audit

Landmark Judgment of Hon’ble SC in United Commercial Bank vs. CIT held that
- Books of accounts prepared in statutory form may not be decisive and conclusive in determining real income;
- Preparation of Balance Sheet in accordance with statutory provision would not disentitle assessee in submitting income tax return on the real taxable income

• Further, Cos. Act cannot override taxability based on accounting
• Thus, if real income can be obtained from ICAI AS, one may opt for the same

Practical points for consideration:
- Separate set of ICAI AS needs to be prepared
- Without audited figures, it would be difficult to prove authenticity of accounts prepared as per ICAI AS when asked by tax authorities
- Also, if tax authorities accept the books as per ICAI AS, reconciliation may be asked by tax authorities
- Thus, better view is to follow Ind AS treatment in practical scenario
<table>
<thead>
<tr>
<th>Instrument</th>
<th>Indian GAAP</th>
<th>Ind AS</th>
<th>Tax / MAT</th>
</tr>
</thead>
<tbody>
<tr>
<td>Equity shares (excluding subsidiaries, associates and JV)</td>
<td>• Current investments at lower of cost and fair value and long term investments at cost less other than temporary diminution</td>
<td>• FVTPL</td>
<td><strong>Income Tax:</strong>&lt;br&gt;<strong>Stock in Trade/ Current investment (i.e. FVTPL)</strong>&lt;br&gt;• FV loss computed category wise allowed as deduction (part A of ICDS VIII) under the head business income&lt;br&gt;• FV gain to be disregarded. Subsequent FV loss (to the extent of FV gain disregarded in the past) to be ignored&lt;br&gt;<strong>Securities held as capital assets/ non-current investments (i.e. FVOCI or amortized cost)</strong>&lt;br&gt;• FV through OCI should be disregarded for computing the income under the head ‘Business Income’&lt;br&gt;• Any cost incurred for acquiring capital asset/ investment be added to the cost of capital asset/ investment. Amortised cost, if any, to be added back in the computation.&lt;br&gt;• Actual gain/ loss taxable as LTCG / STCG on transfer of securities/ assets depending upon the period of holding&lt;br&gt;<strong>MAT:</strong>&lt;br&gt;• No adjustment required for MTM gain/ loss recognized through profit and loss account (FVTPL) (FAQ-1)&lt;br&gt;• Any amount credited/ debited towards FV through OCI under ‘Items that will not be re-classified to P/L (except for gains/ losses from investments in equity instruments designated at fair value through OCI)’ to be added/ reduced for computing MAT liability&lt;br&gt;• Impact of gains/ losses from investments in equity instruments to be considered for MAT in the year of disposal/ retiring, etc. of such equity instruments</td>
</tr>
<tr>
<td>Preference shares</td>
<td></td>
<td>• Amortised cost; or</td>
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<tr>
<td></td>
<td></td>
<td>• FVTPL</td>
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<td></td>
<td></td>
<td>Based on the terms e.g. redemption, conversion</td>
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<tr>
<td>Non convertible bonds / Government securities</td>
<td></td>
<td>• Amortised cost; or</td>
<td></td>
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<tr>
<td></td>
<td></td>
<td>• FVTPL; or</td>
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<td>• FVOCI</td>
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<td>Based on the terms e.g. redemption, conversion</td>
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<tr>
<td>Convertible debentures</td>
<td></td>
<td>• FVTPL</td>
<td></td>
</tr>
<tr>
<td>Mutual funds, VC Funds</td>
<td></td>
<td>• FVTPL</td>
<td></td>
</tr>
</tbody>
</table>
### Financial Assets - Measurement (2/2)

<table>
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<th>Tax / MAT</th>
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</thead>
<tbody>
<tr>
<td>Others, e.g. Trade receivables, loans and advances, deposits</td>
<td>No specific requirement, generally at cost less any impairment</td>
<td>Generally amortised cost</td>
<td>The deductibility/ taxability of the cost/ amortised cost should be dealt with basis the basic principle of taxation (i.e. accrual).</td>
</tr>
</tbody>
</table>
**Expected Credit Losses (‘ECL’) - Taxation**

- **Banks, NBFCs, Financial Institution/ Corporation**
  - Deduction allowable in accordance with the provision of section 36(1)(vii) and (viia) of the Act.

- **Other Companies**
  - Provision towards ECL to be disallowed
  - Write-off, if any, should be deductible under section 36(1)(vii) r.w.s 36(2) of the Act.

- MAT – to be added back to the book profit under clause (i) of Explanation 1 to section 115JB(2)
Inventories: Ind AS 2
Measurement

Initial Measurement

At

Cost

Subsequent Measurement

At Lower of

Cost

Net realisable value

Include:

- All costs of purchase
- Costs of conversion / production
- Other costs incurred in bringing the inventories to their present location and condition

Exclude:

- Trade discounts, rebates and similar items
- Financing element of deferred settlement beyond normal credit terms
### Key differences between IGAAP, Ind AS & ICDS

<table>
<thead>
<tr>
<th>Particulars</th>
<th>Indian GAAP</th>
<th>Ind AS</th>
<th>ICDS</th>
</tr>
</thead>
<tbody>
<tr>
<td>Deffered Settlement basis</td>
<td>• No guidance</td>
<td>• Excess over normal price is to be accounted as interest over the period of financing</td>
<td>• ICDS is also silent on deferred settlement basis.</td>
</tr>
<tr>
<td>(Credit facility)</td>
<td></td>
<td></td>
<td>• Definition of interest under Section2(28A) of the Income Tax Act, 1961, inter alia, includes interest payable in respect of credit facility which has not been utilized.</td>
</tr>
<tr>
<td></td>
<td></td>
<td></td>
<td>• Interest expense to be separately claimed as an deduction?</td>
</tr>
</tbody>
</table>

### Points for consideration
- Legal form of the transaction – The Sale of Goods Act
- Withholding tax on interest
- Multiple reconciliations – Income Tax Act, GST, Ind AS books
Provisions, Contingent Liabilities and Contingent Assets: Ind AS 37
Scope

Applies to all entities in accounting for provisions, contingent liabilities and contingent assets

Excludes

- Resulting from executory contracts, unless they are onerous; or
- Covered by another standard, e.g.:
  - Financial instruments (Ind AS 109)
  - Employee benefits (Ind AS 19)
  - Income taxes (Ind AS 12)
  - Leases (Ind AS 17)
  - Business combinations (Ind AS 103)

Executory contracts are contracts under which neither party has performed any of its obligations or both parties have partially performed their obligations to an equal extent.
# Key differences between IGAAP, Ind AS & ICDS - Provisions

<table>
<thead>
<tr>
<th>Particulars</th>
<th>AS 29</th>
<th>Ind AS</th>
<th>ICDS/ Tax impact</th>
</tr>
</thead>
</table>
| **Recognition of provisions** | A provision is recognised only when a past event has created a legal or constructive obligation, an outflow of resources is probable, and the amount of the obligation can be estimated reliably. | A provision shall be recognised when all of the following conditions are met:  
  a) an enterprise has a present obligation as a result of a past event;  
  b) it is probable that an outflow of resources embodying economic benefits will be required to settle the obligation; and  
  c) a reliable estimate can be made of the amount of the obligation. | As per ICDS, Provisions shall be recognised if it is reasonably certain that outflow of economic resources will be required.  
  • Provision is not discounted to NPV  
  • The criteria for recognition of provisions on the basis of the test of ‘probable’ (i.e. more likely than not criteria) replaced with the requirement of ‘reasonably certain’.  
  • In the absence of definition and scope of ‘reasonably certain’ criteria, an ambiguity would arise on assessment of ‘reasonably certain’ criteria.  
  • In the Act, there is no specific provision for recognition of provisions. However, provisions are allowed based on accrued liabilities as per ordinary principles of commercial accounting. |

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Provision for Warranty is allowed as an expenditure upholding the test of ‘probable’ warranty obligation in the following judgments:

- Rotork Controls India P. Ltd. (2009) 314 ITR 62 (SC)
- Himalaya Machinery (P) Limited v DCIT 334 ITR 64
- CIT vs. Luk India P. Ltd. 52 DTR 117.
- Siemens Public communication Networks Limited v CIT
- CIT v Indian Transformer Limited. 270 ITR 259
### Constructive Obligation

**Meaning**
An obligation derived by an established ‘pattern of past practice’ or a ‘sufficiently specific current statement’ or an obligation created by a ‘valid expectation’

**Cases**

<table>
<thead>
<tr>
<th></th>
<th>IGAAP</th>
<th>IND AS</th>
</tr>
</thead>
<tbody>
<tr>
<td>Announcement of Voluntary Retirement Scheme (‘VRS’)</td>
<td>Provision will be created when agreement is in place</td>
<td>Provision will be created when it is announced to the public</td>
</tr>
<tr>
<td>Publishing clean up policy</td>
<td>Provision to be created only when contractual obligation is created</td>
<td>Provision to be created when a policy has been communicated to the concerned parties</td>
</tr>
</tbody>
</table>

**Deduction of Constructive Obligation**
Provision shall be deductible only if it is created scientifically. Whether such provision is created out of an obligating event or constructive obligation, it shall be deductible only if it is scientifically made.
Case study - Discounting of provisions

- Ind AS 37 mandates creation of provision considering time value of money.
- Discounting of provisions is required in such a scenario.

<table>
<thead>
<tr>
<th>Accounting under IGAAP</th>
<th></th>
</tr>
</thead>
<tbody>
<tr>
<td>Expense account</td>
<td>Dr 100</td>
</tr>
<tr>
<td>To Provision account</td>
<td>Cr 100</td>
</tr>
</tbody>
</table>

<table>
<thead>
<tr>
<th>Accounting under Ind AS for creation of provision</th>
<th></th>
</tr>
</thead>
<tbody>
<tr>
<td>Expense account</td>
<td>Dr 90</td>
</tr>
<tr>
<td>To Provision account</td>
<td>Cr 90</td>
</tr>
</tbody>
</table>

<table>
<thead>
<tr>
<th>Accounting under Ind AS for interest charge YoY</th>
<th></th>
</tr>
</thead>
<tbody>
<tr>
<td>Interest account</td>
<td>Dr 4</td>
</tr>
<tr>
<td>To Provision account</td>
<td>Cr 4</td>
</tr>
</tbody>
</table>

Whether for tax computation, provision to be considered at discounted value or at the original value (i.e. Without considering the discounted factor)
### Key take-aways

**Real Income**
- Difference in “accounting accrual” and “tax accrual”
- Only real income taxable as per section 4/ 5 of the Act

**Evaluate**
- Every amount debited/ credited to profit and loss account to be evaluated to determine the tax impact

**Reconcile**
- Reconcile the stand for the tax purpose vis-a-vis the disclosures made in the financial statements

**Parallel Records**
- The tax treatment relating to financial instruments will require companies to maintain memorandum accounts for control purpose
Any Questions?

Questions & Answers
Thank You

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