Accounting Standard
for Non – Corporate Entities

AS 10 – Property, Plant and Equipment
AS 16 – Borrowing Cost
AS – 9 Revenue Recognition

By S Sundar Raman, B.Com, FCA

For SIRC of ICAI, 12th May, 2023

AS -10
Property Plant and Equipments

- Scope
- Definition
- Recognition and Measurement
- Subsequent Measurement
- Depreciation
- Component Accounting
- De-recognition & Impairment
- Disclosure Requirements
- Key Differences AS & ICDS

Scope

- **Applied: Accounting for** all property, plant and equipment unless another Standard requires or permits a different accounting treatment. (Recognition, Carrying Amount, Depn & Impairment)

- **Does not Apply to:**
  - ✓ Biological Assets related to Agricultural activity other than Bearer Plants.
  - ✓ Mineral rights, mineral reserves, Exploration and extraction of Mineral Oils, Natural Gas and similar non-regenerative Resources.

- Also applies to **Investment Property** – Cost Model (AS13)

Meaning of PPE

Definition

Property, Plant and Equipment ('PPE') **are "Tangible items"**

Held For:

- Use In the production or supply of goods or services
- Rental to others
- Administrative purpose

and

Expected to be used during more than one period

12 months

spare parts, stand-by equipment are recognised as PPE when they meet the above definition of PPE

RECOGNITION AND MEASUREMENT

Recognition and Measurement

Property, Plant & Equipment shall be recognized as an asset when: (Para 7)

It is probable that future economic benefits will flow to the enterprise

Cost can be measured reliably

Criteria apply to all costs when incurred, including

Initial acquisition or construction costs

Subsequent Costs (Add, replace or Service) – Service may be R/M

Enterprise may expense item considering immaterial (para 9)

<u>Property, Plant Equipment is measured initially at cost.</u>

Benefits from related assets

Elements of Cost

Elements of Cost

Purchase Costs

- Purchase Price
- **Add:** Import Duties/ Non Refundable Taxes
- <u>Deduct:</u> Trade discounts/ rebates

Directly attributable Costs

any costs directly attributable to bringing the asset to the location and condition necessary for it to be capable of operating in the manner intended by management

- Cost of Employee benefits
- Cost of Site Preparation
- Initial delivery and handling Costs
- Installation and assembly costs
- Cost of testing
- Professional Fees

Other Costs

- Initial estimates of **dismantling costs**.
- Initial estimates of site restoration costs
- Major **inspection costs**
- Cost of Replacements

Not cost of an Item of PPE

Cost Element - Exclusion

- Costs of Opening a new facility – e.g inauguration cost
- Costs of introducing a new product or service or conducting business in a new location; (Including staff training)
- Administrative and other general overheads

Elements of Cost

- Initial operating losses charged to P&L
- Abnormal losses and profits in case of self constructed asset charged to P&L
- Incidental operations during construction period charged to P&L
- payment is deferred beyond normal credit terms, the difference between the cash price equivalent and the total payment is recognised as interest

Key impacts

- Trial run
- Interest income during construction period
- Expenses incurred by new company promoted to set up new plant.

Elements of Cost

Spare parts, stand-by equipment & Servicing Equipment

- ✓ These are recognized in accordance with this AS when they meet the definition of PPE
- ✓ Otherwise such items are classified as Inventory

Exchange of Assets

If PPE is ***acquired in exchange*** for other non monetary asset or for a combination of monetary asset

Measure costs at **Fair value**, unless:

- The exchange transaction has ***no commercial substances***,

or

- Fair value of neither the asset received nor given up can be reliably measured

If the acquired item is not measured at fair value, its cost is measured at the ***carrying amount of the asset given up***.

Commercial Substance: Configuration of Cash Flows, ESV Changes.

SUBSEQUENT COST AND MEASUREMENT

Subsequent Measurement

- Can choose **Cost Model** or **Revaluation Model** as its **accounting policy**
- Adopted option as accounting policy will apply to **entire class** of PPE
- Revaluation shall be done **with sufficient regularity** to ensure that there is no significant gap between FV and Carrying Value
- Under revaluation model, carrying amount restated with reference to available **observable market data**

Revaluation Model

Revaluation

Upward

Owners Interest – Revaluation Surplus

Cr to P & L to provide for the previous revaluation decrease

Downward

Debit revaluation Surplus to the extent recognized previously and balance, if any, Charge to Profit or Loss A/c.

The revaluation surplus may be transferred to Revenue Reserves when the assets is derecognized or as it is used by the entity (not through Profit & Loss)

Subsequent Cost - Part Replacement

- Day to day servicing cost are charged to P&L
- Some items involve a series of linked parts which require regular replacement at different intervals and have different useful lives.
- Recognize the cost of replacing a part in the carrying amount, if recognition criteria are met.
- The carrying amount of replaced parts is derecognized
- For Example, a furnace may require relining after a specified number of hours of use, or aircraft interiors such as seats and galleys may require replacement several times during the life of the airframe.

Subsequent Cost – Major inspection/ Overhaul Costs

- Performing regular major inspections for faults, regardless of parts being replaced or not, may be a condition of continuing to operate an item of Property Plant and Equipment.
- Cost of each major inspection performed is recognized in carrying amount, as a replacement, if the recognition criteria are met.
- Any remaining carrying amount of the cost of the previous inspection is derecognized.

DEPRECIATION

Depreciation

- Depreciation **begins when** the asset is available for use (ie when it is in the location and condition necessary for it to be capable of operating in the manner intended by management) & **continues until** the asset is derecognized or classifies as held for sale.

- The **Residual value** –

  Amount can be obtained from disposal (–) costs of disposal

- The residual value & the useful life of an asset **shall be reviewed at least at each financial year end**, and if expectations differs from previous estimates, the change shall be accounted for as a change in accounting policy.

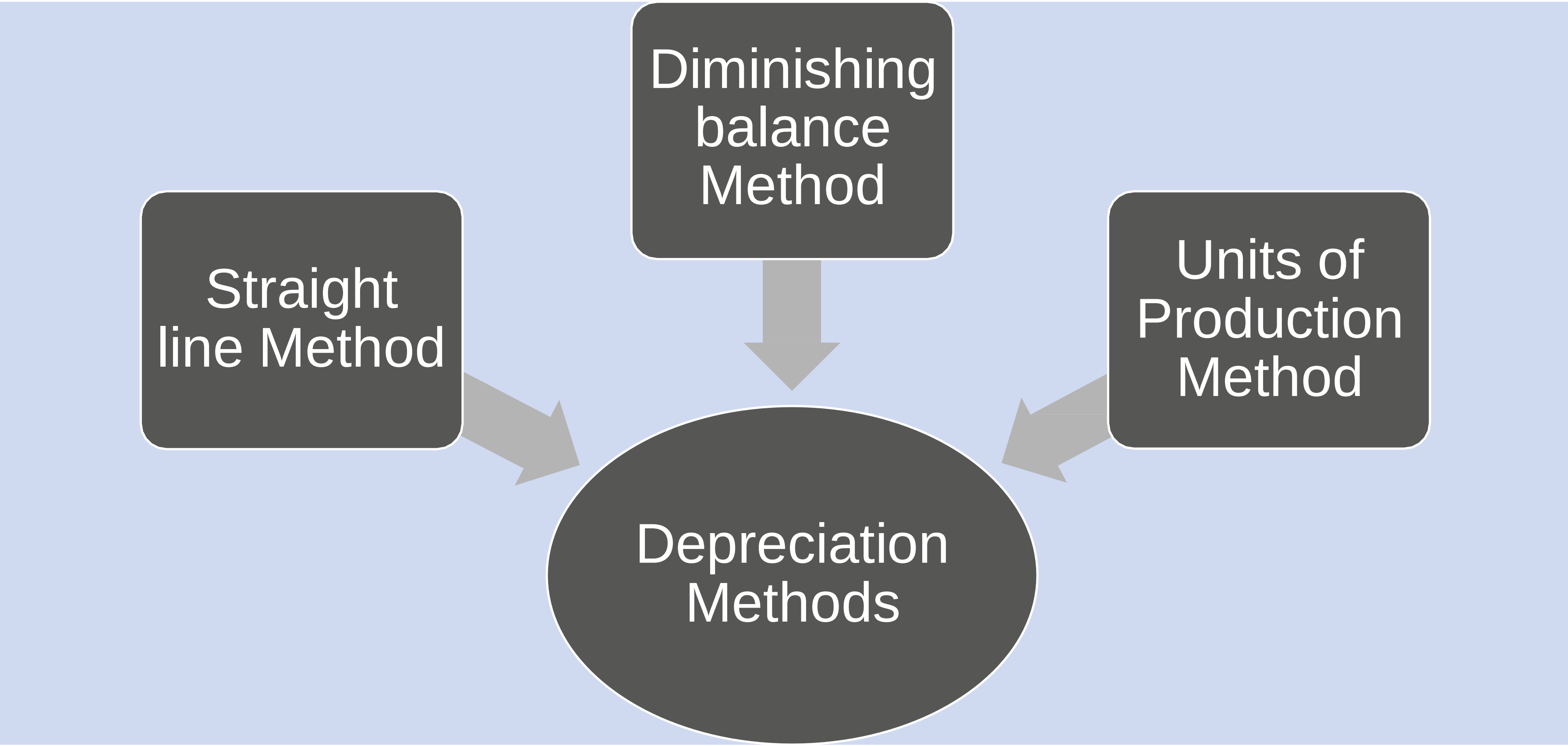
Depreciable Amount = Cost - Residual Value

Useful Life of Asset- Key Factors

All the following factors are considered in the determining the useful life of an asset:

- Expected usage of the asset.
- Expected physical wear and tear depending on operational factors
- Technical or commercial obsolescence arising from :
  - Changes or improvement in production;
  - Change in Market demand for production
- Legal or similar limits on the use (E.g. Expiry dates of related leases)
- Asset Management policy may involve disposal of asset after a specified time Therefore, useful life may be shorter than economic life
- Repairs and Maintenance policies may also affect useful life.

Depreciation Method



Method selected should closely reflects the pattern of consumption of economic benefits expected to be consumed by entity

Depreciation Method

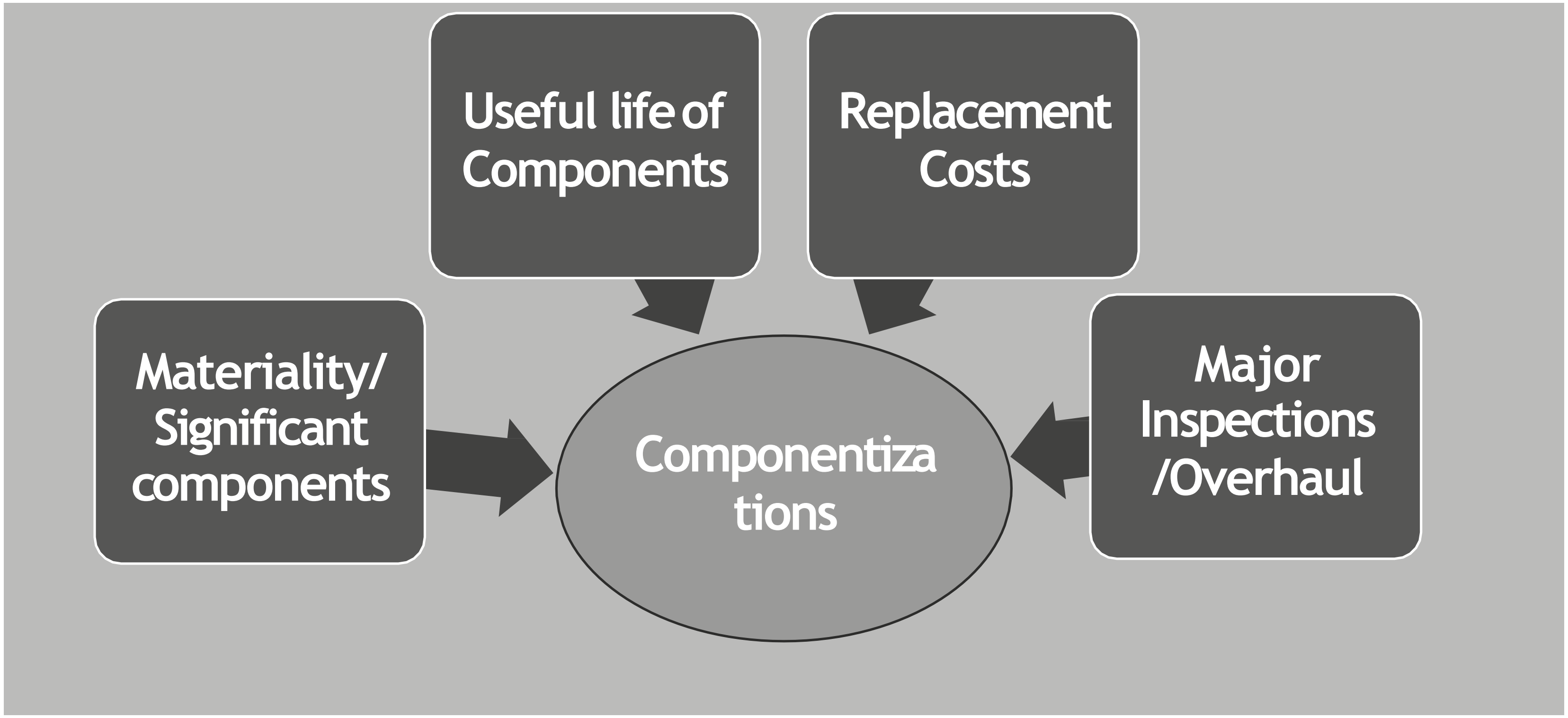
- The depreciation method applied to an asset should be reviewed at least at each financial year-end and,

- 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.

- Such a change should be accounted for as a change in an accounting estimate in accordance with AS 5.

Component Accounting

Key Considerations



Each major part of an item of PPE with cost being significant in relation to total cost of the item – should be **depreciated separately**, even though it may not have different useful life, but may be grouped for determining depreciation charge.

De-recognition and Impairment

De-recognition

- Derecognize the carrying amount:
  - On disposal; or
  - When no future benefits are expected from its use.
- Any gain or loss arising from the De-recognition to be included in profit or loss.
- Gains (or proceeds) are not classified as revenue.

Impairment

- Compensation from third party for item of PPE that is impaired / Lost / Given up shall be included in P&L when compensation becomes receivable.
- Impairment of Assets including PPE dealt by IND AS 28

DISCLOSURES

Disclosures

- ***Measurement basis*** for determining gross carrying value
- Depreciation methods used
- Useful lives or depreciation rates used
- Gross carrying amount and accumulated depreciation at the beginning and end of the period
- ***Reconciliation of the carrying amount*** at the beginning and end of the period (Addition, Deletion, Assets classified as held for sale, Business Combination, Revaluation, impairment, exchange difference & Other charges)
- ***Comparative information*** required
- Existence and amounts of ***restrictions on title*** to assets
- Property Plant and equipments ***pledged as security*** for liabilities

Disclosures

- Amount of expenditures recognized in the course of construction
- ***Contractual commitments*** for acquisition of Property Plant and Equipment
- Amount of compensation from third parties for items of property plant and equipments (if not disclosed separately in P&L)

Disclosure for Revalued Assets

- Effective date of Revaluation
- Whether an independent valuer was involved
- Methods and significant assumptions applied in estimating fair values.
- Extent to which fair value were determined based on observable prices or other valuation techniques
- Carrying amount of each class of revalued Property Plant and Equipment if the cost model had been applied
- Revaluation surplus, including movement and any restrictions on distribution of balance to shareholders

Disclosure (Encouraged) – Para 87 – Relaxed for Level III and IV

- Carrying amount of temporarily idle PPE
- Gross carrying amount of any fully depreciated PPE that is still in use
- For each revalued class of PPE, the carrying amount that would have been recognised had the assets been carried under the cost model
- Carrying amount of PPE retired from active use and not held for disposal

ICDS Vs AS

ICDS V VS AS – 10
Tangible Fixed Assets

ICDS V: Tangible Fixed Assets	AS -10: Accounting for fixed assets
The definition of actual cost is narrow and may allow the taxpayer room to deduct the expenditure on acquisition whereas it should be capitalised	Cost of fixed asset includes actual cost, non refundable taxes and all other costs that are required to bring it to its working condition
When a tangible fixed asset is acquired in exchange for other asset, the fair value of the tangible fixed asset so acquired shall be its actual cost	When a fixed asset is acquired in exchange or in part exchange for another asset, the cost of acquired asset should be recorded either at FMV or NBV of asset given up, adjusted for any balancing payment or receipt of cash or other consideration.

ICDS V VS AS – 10 Cont…

ICDS V: Tangible Fixed Assets	AS -10: Accounting for fixed assets
When a tangible fixed asset is acquired in exchange for shares or other securities, the fair value of the tangible fixed asset so acquired shall be its actual cost	Fixed asset acquired in exchange for shares or other securities in the enterprise should be recorded at its FMV, or the FMV of the securities issued, whichever is more clearly evident.
When several assets are acquired at consolidated basis, the costs shall be apportioned on a fair basis. Hence, this might make the value subjective	When several assets are acquired on a consolidated basis, the cost shall be determined by competent valuers.

AS -16
Borrowing Cost

- Scope
- Definition
- Explanation
- Recognition
- Borrowing Costs Eligible for Capitalisation
- Commencement of Capitalisation
- Suspension of Capitalisation
- Cessation of Capitalisation
- Disclosure

Scope

This Standard should be applied in accounting for borrowing costs.

This Standard does not deal with the actual or imputed cost of owners' equity, including preference share capital not classified as a liability.

Definitions

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

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

Explanation:

- What constitutes a substantial period of time primarily depends on the facts and circumstances of each case.

- However, ordinarily, a period of twelve months is considered as substantial period of time unless a shorter or longer period can be justified on the basis of facts and circumstances of the case.

- In estimating the period, time which an asset takes, technologically and commercially, to get it ready for its intended use or sale is considered.

Recognition

- ***Borrowing costs that are directly attributable to the acquisition, construction or production of a qualifying asset should be capitalised as part of the cost of that asset.***

- ***The amount of borrowing costs eligible for capitalisation should be determined in accordance with this Standard. Other borrowing costs should be recognised as an expense in the period in which they are incurred.***

Borrowing Costs Eligible for Capitalisation

To the extent that funds are borrowed specifically for the purpose of obtaining a qualifying asset, the amount of borrowing costs eligible for capitalisation on that asset should be determined as the actual borrowing costs incurred on that borrowing during the period less any income on the temporary investment of those borrowings.

To the extent that funds are borrowed generally and used for the purpose of obtaining a qualifying asset, the amount of borrowing costs eligible for capitalisation should be determined by applying a capitalisation rate to the expenditure on that asset.

The capitalisation rate should be the weighted average of the borrowing costs applicable to the borrowings of the enterprise that are outstanding during the period, other than borrowings made specifically for the purpose of obtaining a qualifying asset.

The amount of borrowing costs capitalised during a period should not exceed the amount of borrowing costs incurred during that period

Commencement of Capitalisation

asset should commence when all the following conditions are satisfied

- Expenditure for the acquisition, construction or production of a qualifying asset is being incurred
- Borrowing costs are being incurred; and
- Activities that are necessary to prepare the asset for its intended use or sale are in progress.

Suspension of Capitalisation

Capitalisation of borrowing costs should be suspended during extended periods in which active development is interrupted.

For example, capitalisation continues during the extended period needed for inventories to mature or the extended period during which high water levels delay construction of a bridge, if such high water levels are common during the construction period in the geographic region involved.

Cessation of Capitalisation

Capitalisation of borrowing costs should cease when substantially all the activities necessary to prepare the qualifying asset for its intended use or sale are complete.

When the construction of a qualifying asset is completed in parts and a completed part is capable of being used while construction continues for the other parts, capitalisation of borrowing costs in relation to a part should cease when substantially all the activities necessary to prepare that part for its intended use or sale are complete.

Disclosure

The financial statements should disclose:

1. **The accounting policy adopted for borrowing costs; and**

2. **The amount of borrowing costs capitalised during the period.**

ICDS Vs AS 16

ICDS IX Vs AS- 16 Borrowing Cost

ICDS IX: Borrowing Cost	AS – 16: Borrowing Costs
Borrowing costs does not include exchange differences	Borrowing costs include exchange differences arising from foreign currency borrowings to the extent they are an adjustment to interest costs

Illustration:

E.g. XYZ Ltd. has taken a loan of USD 10,000 on April 1, 201X, for a specific project @5% p.a., payable annually. On April 1, 201X, the exchange rate Rs. 45/USD. The exchange rate, as at March 31, 201X, is Rs. 48/USD. The corresponding amount could have been borrowed by XYZ Ltd. in local currency @11% p.a. on April 1, 201X.

- Interest - USD 10,000 × 5% × Rs. 48/USD = Rs. 24,000.
- Increase in the liability towards the principal amount = USD 10,000 × (48-45) = Rs. 30,000.
- Interest had the loan been taken in Indian currency = USD 10000 × 45 × 11% = Rs. 49,500.

ICDS IX Vs AS- 16

ICDS IX: Borrowing Cost	AS – 16: Borrowing Costs
Qualifying Assets means: • Tangible Assets – land, plant, etc. • Intangible Assets – patents, licenses, etc. (asset that necessarily takes a period of 12 months or more for its acquisition, construction or production) • Inventories – that require 12 months or more to bring them to saleable condition.	Qualifying Asset is an asset that takes substantial period of time to get ready for its intended use or sale
As per ICDS, till qualifying asset is put to use, capitalization shall be continued. Suspension of Capitalisation during interruption is not provided here	Capitalisation of a qualifying asset shall be continued up to substantial completion of activity

ICDS IX Vs AS- 16

ICDS IX: Borrowing Cost	AS – 16: Borrowing Costs
Commencement of Capitalization: a)specific borrowings – Date on which funds were borrowed b)General borrowings – Date on which funds were utilised. Hence, capitalization commences early	Commencement of Capitalization: The date of fulfilment of three conditions viz. incurrence of capex, incurrence of borrowing costs and preparatory activities are in progress.
The income from temporary deployment of unutilised funds from specific loans shall be taxable as Income from other sources under the ICDS.	AS-16 requires income from temporary deployment of unutilised funds to be reduced from borrowing cost.
SC ruling in Tuticorin Alkali Chemicals (227 ITR 172) requires that interest income earned from temporary deployments of funds has to be offered to tax immediately as IFOS. Hence above deviation has no tax impact.	

AS -9
Revenue Recognition

Revenue Recognition

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

- The sale of goods,
- The rendering of services, and
- The use by others of enterprise resources yielding interest, royalties and dividends.

Not Applicable:

- Revenue arising from construction contracts;
- Revenue arising from hire-purchase, lease agreements;
- Revenue arising from government grants and other similar subsidies;
- Revenue of insurance companies arising from insurance contracts.

Not included in Revenue:

- Realised gains resulting from the disposal of, and unrealised gains resulting from the holding of, non-current assets e.g. appreciation in the value of fixed assets.

- Unrealised holding gains resulting from the change in value of current assets, and the natural increases in herds and agricultural and forest products.

- Realised or unrealised gains resulting from changes in foreign exchange rates and adjustments arising on the translation of foreign currency financial statements.

- Realised gains resulting from the discharge of an obligation at less than its carrying amount.

- Unrealised gains resulting from the restatement of the carrying amount of an obligation.

Definitions

1. **<u>Revenue</u> is the gross inflow of cash, receivables or other consideration arising in the course of the ordinary activities of an enterprise4 from the sale of goods, from the rendering of services, and from the use by others of enterprise resources yielding interest, royalties and dividends. Revenue is measured by the charges made to customers or clients for goods supplied and services rendered to them and by the charges and rewards arising from the use of resources by them. In an agency relationship, the revenue is the amount of commission and not the gross inflow of cash,receivables or other consideration.**

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

3. **<u>Proportionate completion method</u> is a method of accounting which recognises revenue in the statement of profit and loss proportionately with the degree of completion of services under a contract.**

Main Principles

Revenue from sales or service transactions should be recognised when the requirements as to performance set out in paragraphs 11 and 12 are satisfied, provided that at the time of performance it is not unreasonable to expect ultimate collection.

If at the time of raising of any claim it is unreasonable to expect ultimate collection, revenue recognition should be postponed.

In a transaction involving the sale of goods, performance should be regarded as being achieved when the following condition shave been fulfilled: (Para 11)

1. The seller of goods has transferred to the buyer the property in the goods for a price or all significant risks and rewards of ownership have been transferred to the buyer and the seller retains no effective control of the goods transferred to a degree usually associated with ownership; and

2. No significant uncertainty exists regarding the amount of the consideration that will be derived from the sale of the goods.

(Para 12)

In a transaction involving the rendering of services, performance should be measured either under the completed service contract method or under the proportionate completion method, whichever relates the revenue to the work accomplished.

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

Revenue arising from the use by others of enterprise resources yielding interest, royalties and dividends should only be recognised when no significant uncertainty as to measurability or collectability exists. These revenues are recognised on the following bases

- **<u>Interest :</u> on a time proportion basis taking into account the amount outstanding and the rate applicable.**

- **<u>Royalties :</u> on an accrual basis in accordance with the terms of the relevant agreement.**

- **<u>Dividends from :</u> when the owner's right to receive payment is established.**

Disclosure

In addition to the disclosures required by Accounting Standard (AS) 1, Disclosure of Accounting Policies, an enterprise should also disclose the circumstances in which revenue recognition has been postponed pending the resolution of significant uncertainties.

ICDS Vs AS 9

ICDS IV Vs AS – 9
Revenue Recognition

ICDS IV: Revenue Recognition	AS – 9: Revenue Recognition
Revenue from service transaction has to be recognised **only in percentage completion method.** **Exception:** **a. Service over indeterminate number of acts over a specific period of time – Straight Line basis for revenue recognition** **b. Service contract with duration of not more than 90 days – When rendering of service under that contract is completed or substantially completed.**	Revenue from service transaction are recognised in ***percentage completion method or completed service contract method.***

ICDS IV Vs AS – 9
Revenue Recognition

ICDS IV: Revenue Recognition	AS – 9: Revenue Recognition
Royalty income can be recognised even as per others basis, apart from term of agreement	Royalty income can be recognised only as per the terms of agreement
Dividends are recognised as per Income tax Act, 1961	Dividends are recognised when the right to receive is established
Interest needs to be recognized on time basis (except in case of refund of tax, duty or cess) – Cash basis to be followed.	

THANK YOU!