Common non-compliances in Schedule II & III of Companies Act, 2013

By:
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Schedule II

Abstract of accounting policy of a company on Depreciation of PPE

Non-compliance

- Depreciation on property, plant & equipment (PPE) is provided on Straight Line Method over their useful lives and in the manner specified in Schedule II to the Companies Act, 2013. However, in respect of certain Plant & Machineries and Electric Installations, depreciation is provided as per their useful lives assessed on the basis of technical evaluation by the external valuer, ranging from 20 to 40 years.

Requirement



Abstract of accounting policy of a company on Depreciation of PPE

Non-compliance

- Schedule II to Companies Act, 2013 introduced concept of useful life of asset instead of using specific depreciation rates as provided in Schedule XIV to Companies Act, 1956. Therefore, the company viewed that Schedule II to Companies Act, 2013 provides only straight line method of depreciation and any other method cannot be used.

Requirement



Abstract of accounting policy of a company on Depreciation of PPE

Non-compliance	Requirement
• Property, Plant and Equipment are stated at cost, net of recoverable taxes, trade discount and rebates less accumulated depreciation and impairment losses, if any, as computed in accordance with the method prescribed under Schedule II of the Co. Act, 2013; • Intangible Assets are stated at cost of acquisition net of recoverable taxes, trade discount and rebates less accumulated amortisation/depletion and impairment losses, if any, as computed as per the method prescribed under Sch. II of the Co. Act, 2013	

Abstract of accounting policy of a company on Depreciation of PPE

Non-compliance

- Depreciation on property, plant & equipment (PPE) is provided on Straight Line Method over their maximum useful lives as specified in Schedule II to the Companies Act, 2013, except where different useful lives are adopted on the basis of technical advice obtained by the company from independent experts

Requirement



Abstract of accounting policy of a company on Depreciation of PPE

Non-compliance

- Depreciation on those assets, whose actual cost does not exceed Rs. 5,000/=, has been provided @ 100% in accordance with Schedule II of the Companies Act, 2013

Requirement



Schedule III

AS Compliant Companies

Division I – Part – I : Balance Sheet

EQUITIES AND LIABILITIES
Shareholders' Funds (a) Share Capital (b) Reserves & Surplus (c) Money Reserved against share warrants
Share Application money pending Allotment
Non Current Liabilities (a) Long-term borrowings (b) Deferred tax liabilities (Net) (c) Other Long term liabilities (d) Long-term provisions
Current Liabilities (a) Short-term borrowings (b) Trade Payables:— (A) total outstanding dues of micro enterprises and small enterprises; and (B) total outstanding dues of creditors other than micro enterprises and small enterprises (c) Other current liabilities (d) Short-term provisions
TOTAL

Division I – Part – I : Balance Sheet

ASSETS

Non-Current Assets

(a) Property, Plant and Equipment [*and Intangible assets*]

- ~~(i) Tangible assets~~ *Property, Plant and Equipment*
- (ii) Intangible assets
- (iii) Capital work-in-progress
- (iv) Intangible assets under development

(b) Non-current investments

(c) Deferred tax assets (net)

(d) Long-term loans and advances

(e) Other non-current assets

Current Assets

(a) Current investments

(b) Inventories

(c) Trade receivables

(d) Cash and cash equivalents

(e) Short-term loans and advances

(f) Other current assets

TOTAL

Division I – Part – II : Statement of Profit & Loss

Particulars	Note No.	Figures at the end of current reporting period	Figures at the end of previous reporting period
Revenue from Operations			
Other Income			
Total ~~Revenue~~ *Income* (I + II)			
Expenses			
Cost of Material Consumed Purchases of Stock in Trade Changes in inventories of finished goods, Work in progress and stock in trade Employee Benefit expense Finance Costs Depreciation and amortization expense Other expenses			
Profit Before Exceptional and extraordinary items and tax			
Exceptional Items			

Division I – Part – II : Statement of Profit & Loss

Particulars	Note No.	Figures at the end of current reporting period	Figures at the end of previous reporting period
Profit Before extraordinary items and tax			
Extraordinary Items			
Profit Before Tax			
Tax Expense Current Tax Deferred Tax			
Profit (loss) for the period from continuing operations			
Profit (loss) from discontinuing operations			
Tax expense of discontinuing operations			
Profit(loss) from discontinuing operations (after tax)			
Profit (loss) for the period			
Earnings per equity share Basic Diluted			

Pre-amendment [Clause 4(i)]

Depending upon the ~~*turnover*~~ of the company, the figures appearing in the Financial Statements ~~*may*~~ be rounded off as given below:—

~~*Turnover*~~	Rounding off
less than one hundred crore rupees	To the nearest hundreds, thousands, lakhs or millions, or decimals thereof
one hundred crore rupees or more	To the nearest lakhs, millions or crores, or decimals thereof

Post-amendment [Clause 4(i)]

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

Total Income	Rounding off
less than one hundred crore rupees	To the nearest hundreds, thousands, lakhs or millions, or decimals thereof
one hundred crore rupees or more	To the nearest lakhs, millions or crores, or decimals thereof

General Instructions For Preparation of Balance Sheet

Non-compliance	Requirement
• The Schedule III requires all items in the Balance Sheet to be classified as either Current or Non-current; • One of the underlying criteria for such classification is 'operating cycle' • No disclosure was made for 'operating cycle'	

General Instructions For Preparation of Balance Sheet

Non-compliance	Requirement
• In one case, notes to accounts stated that company's operating cycle is six months. The sale contract provides for a normal credit period of three months. However, the company does not expect to receive the payment within twelve months from the reporting date due to ongoing litigation with the customer; • Still the company classified trade receivable for such customer under 'current asset' category	

General Instructions For Preparation of Balance Sheet

Non-compliance

- In one case, investments were classified into ‘current’ and ‘non-current’ category under Schedule III;
- Whereas AS 13 requires to classify investments as ‘current’ and ‘long-term’;
- Still the company did not make appropriate disclosures about investments under Schedule III as to classification in tandem with AS 13

Requirement



General Instructions For Preparation of Balance Sheet

Non-compliance	Requirement
• In one case, Deferred Tax Liability was classified into current and non-current category; • In another case, Deferred Tax Asset was classified into current and non-current category; • Deferred Tax Asset/ Liability was classified into current and non-current category	

General Instructions For Preparation of Balance Sheet

Non-compliance	Requirement
• In one case, there was unpaid amount towards shares subscribed by the subscribers of the MOA; • The company hence gave a descriptive note for the same without any treatment in Financial Statements	

General Instructions For Preparation of Balance Sheet

Non-compliance	Requirement
• In one case, a reconciliation of the number of shares outstanding at the beginning and at the end of the reporting period was given; • The company, however, gave such reconciliation for total number of shares in aggregate, whereas the notes also stated that company has issued Equity Shares as well as Preference Shares	

General Instructions For Preparation of Balance Sheet

Non-compliance	Requirement
• In one case, shares in the company held by each shareholder holding more than 5% shares was given by specifying the number of shares held; • The company however gave such shareholding for total number of shares in aggregate whereas the notes also stated that company has issued Equity Shares as well as Preference Shares	

General Instructions For Preparation of Balance Sheet

Non-compliance	Requirement
• In one case, the loan payable by the company was converted into equity under an arrangement between the company and the lender; • The company disclosed the same as shares allotted as fully paid up pursuant to contract(s) without payment being received in cash • Note: Clause (i) of Note 6A of Part I of Schedule III requires separate disclosures for non-cash allotments	

General Instructions For Preparation of Balance Sheet

Non-compliance	Requirement
• In one case, the company made a separate disclosure of shareholding of its promoters including the percentage change therein during the year; • The company disclosed the same in the format prescribed under Schedule III which requires disclosure only in respect of shares held at the end of the year • Reference: Clause (m) of Note 6(A)	

General Instructions For Preparation of Balance Sheet

Non-compliance	Requirement
• In one case, the company received 'calls in advance' from some shareholders; • The company disclosed the same as a part of the paid-up capital • Reference: In terms of Section 50, a company, if so authorized by its Articles, may accept from any member the whole or a part of the amount remaining unpaid on any shares held by him, although no part of that amount has been called up	

General Instructions For Preparation of Balance Sheet

Non-compliance	Requirement
• In one case, the company was having long term borrowings; • The company no where separately disclosed the current maturities of such long-term borrowings	

General Instructions For Preparation of Balance Sheet

Non-compliance	Requirement
• In one case, the company was having secured long term borrowings; • The company disclosed that all long terms borrowings are secured against tangible assets owned by the company and personal security of promoters, shareholders and third parties	

General Instructions For Preparation of Balance Sheet

Non-compliance	Requirement
• In one case, the company was having some 'leasehold improvements'; • The company disclosed 'leasehold improvements' by clubbing the same under 'Assets held under Lease'	

General Instructions For Preparation of Balance Sheet

Non-compliance	Requirement
• In one case, the company was having some investments in LLPs; • The company disclosed the same under the sub-heading “investments in partnership firm”; • Note: Schedule III requires disclosure in regard to investments in the capital of partnership firms, the names of the firms (with the names of all their partners, total capital and the shares of each partner)	

General Instructions For Preparation of Balance Sheet

Non-compliance	Requirement
• In some cases, the company has given capital advances for procurement of PPE; • One company disclosed the same under the sub-heading “Capital Work-in Progress”; • Another company disclosed the same as ‘Short-Term Advance’ as the PPE was expected to be received in next months from the reporting date.	

Issue: Cash and Cash Equivalents

- **Deposits with original maturity of three months or less** only should be classified as **cash equivalents** – AS 3;
- Thus, Bank balances held as **margin money or security against borrowings** are neither in the nature of demand deposits, nor readily available for use by the company, and accordingly, **do not meet the aforesaid definition of cash equivalents**;
- However, under **Schedule III – Cash and Cash Equivalents** comprise of:

  "Balances with banks held as margin money or security against borrowings, guarantees, etc. and bank deposits with more than 12 months maturity."

Cash and Cash Equivalents

- **Question:** How to deal with this apparent conflict between the requirements of the Schedule III and the AS with respect to which items should form part of Cash and cash equivalents
- **Answer:**
  1) AS would prevail over the Schedule III;
  2) Company to make necessary modifications in the F.S.;
  3) Accordingly, the conflict should be resolved by **changing the caption "Cash and Cash Equivalents"** to **"Cash and Bank Balances,"** which may have **two sub-headings:**
     a) "Cash and Cash Equivalents" and
     b) "Other Bank Balances."
  4) The former should include only the items that constitute Cash and cash equivalents defined in accordance with AS 3 (and not the Schedule III), while the remaining line-items may be included under the latter heading

Newly Incorporated Company and Subscription Money

Case Study

- RST Limited was incorporated on 28th December, 2024
- The subscribers undertook to bring in Rs. 5,00,000 towards the subscription money in terms of Section 10A of the Companies Act, 2013
- The amount was not received as at 31st March, 2025
- How should this be reflected in the financial statements of RST (P) Limited for the FY 2024-2025
- What is the auditor's responsibility if:
  a) The amount was still not received, and the audit report was signed on 18th June, 2025;
  b) The amount was still not received, and the audit report was signed on 18th July, 2025

Applicability of CARO vis-à-vis Small Company

Applicability

- **Not Applicable to Private Company**, if:
  i. Its not a subsidiary or holding of a Public Co.; **AND**
  ii. (Paid up Capital + Reserves & Surplus) <= Rs. 1 crore as on Balance Sheet Date; **AND**
  iii. Total Borrowings from Banks/ F.I. <= Rs. 1 crore at any point of time during the financial year; **AND**
  iv. Total Revenue (including revenue from discontinuing operations) under Schedule III <= Rs. 10 crores during the financial year as per the financial statements

Applicability

- **Not Applicable to Small Company [Sec. 2(85)]:** a Company having:
  a) Paid up share capital ≤ 4 cr.; ***and***
  b) Turnover as per preceding year P & L ≤ 40 cr.

  Following do not qualify as a Small Company:
  a) Public company;
  b) Holding or a subsidiary company;
  c) Section 8 Company;
  d) Co. or body corporate governed by any special Act

  Note: Rule 2(1)(t) as amended by the Companies (Specification of Definitions Details) Amendment Rule, 2022, **w.e.f. 15-9-2022**:
  a) Paid up share capital ≤ 4 cr.; ***and***
  b) Turnover as per preceding year P & L ≤ 40 cr.

Question 1

Particulars for XYZ (P) Limited	2024-2025	2023-2024
Paid-up Capital	48 Lakhs	48 Lakhs
Reserves and Surplus	5 Lakhs	3 Lakhs
Total	53 Lakhs	51 Lakhs
Borrowings from Banks/ F.I.	3 Cr.	3 Cr.
Total Revenue/ Turnover	38 Cr.	44 Cr.
CARO Applicable	?	Yes (assumed)
Reason	?	

Question 2

Particulars for XYZ (P) Limited	2024-2025	2023-2024
Paid-up Capital	48 Lakhs	48 Lakhs
Reserves and Surplus	5 Lakhs	3 Lakhs
Total	53 Lakhs	51 Lakhs
Borrowings from Banks/ F.I.	3 Cr.	3 Cr.
Total Revenue/ Turnover	38 Cr.	34 Cr.
CARO Applicable	?	Yes (assumed)
Reason	?	


Share
Application
Money

Areas not to be overlooked - Question

RST (P) Limited Equity and Liabilities (Extract)	As at 31.3.2025 (in Lakhs)	As at 31.3.2024 (in Lakhs)
Share application money pending allotment (money was received through Banking channels on 15th January, 2024)	100	100

What does Companies Act say

- A company making **shall allot its securities within 60 days** from the date of receipt of the application money.
- If the company is not able to allot the securities within that period, it shall **repay the application money to the subscribers within 15 days** from the date of completion of 60 days.
- If the company fails to repay the application money within the aforesaid period, it shall be liable to **repay that money with interest @12% p.a.** from the expiry of 60th day – Section 42(6).
- If the securities for which application money or advance for such securities was received **cannot be allotted within 60 days from the date of receipt of the application money** and such application money is not refunded to the subscribers within 15 days from the date of completion of 60 days, **such amount shall be treated as a deposit** – Rule 2(1)(c)(vii) of Companies (Acceptance of Deposits) Rules, 2014

What does CARO say

Para 3(v)	Para 3(xiv)
in case, the company has accepted deposits, whether the directives issued by the Reserve Bank of India and the **provisions of sections 73 to 76 or any other relevant provisions of the Companies Act, 2013 and the rules framed thereunder**, where applicable, **have been complied with?** If not, the nature of such contraventions be stated	whether the company has made any preferential allotment or private placement of shares or fully or partly convertible debentures during the year under review and if so, as to **whether the requirement of section 42 of the Companies Act, 2013 have been complied with** and the amount raised have been used for the purposes for which the funds were raised. If not, provide the details in respect of the amount involved and nature of non-compliance

Disqualification of Directors – Section 164(2)

Any Co. (***other than Govt. Co.***)

Made defaults in

Filing of annual F.S. or annual returns for 3 continuous F.Y.

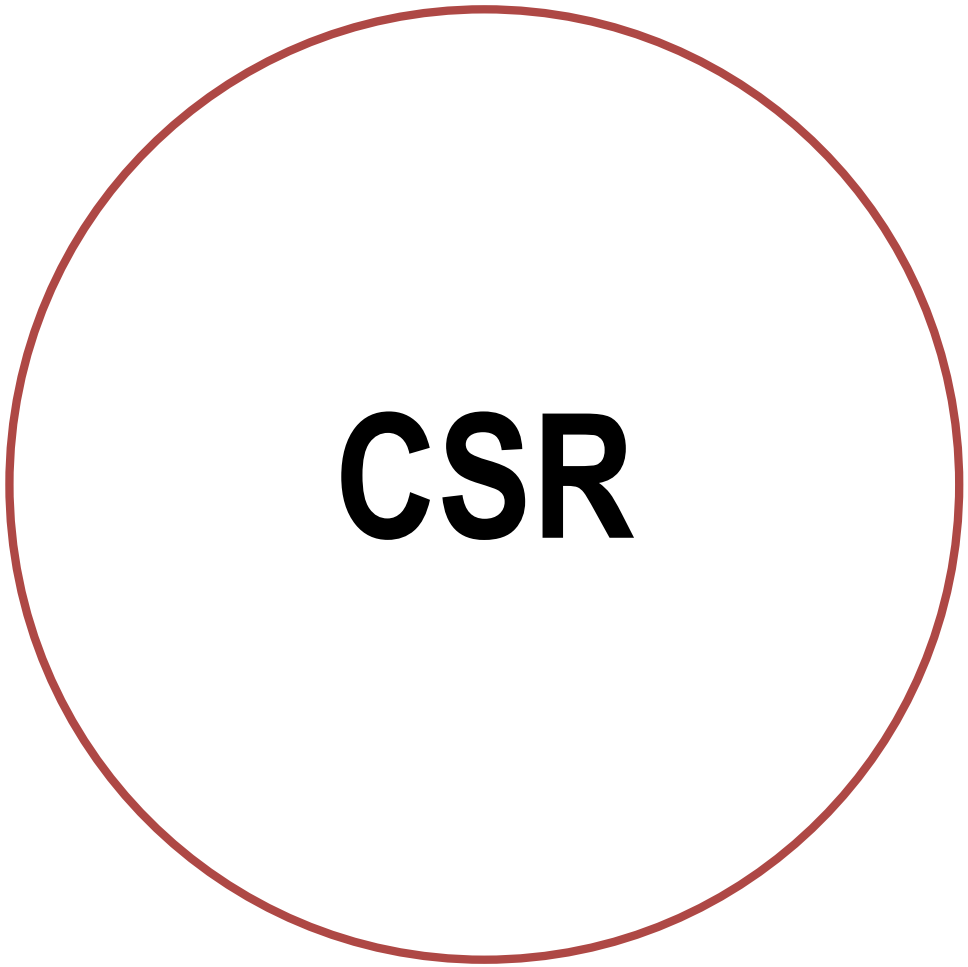
Or

Repayment of **Deposits/ Interest** thereon/ **Debentures/ Interest** thereon/ **Dividend**

≥ 1 year from due date

Then directors of such company

Cannot be re-appointed as director of such company or appointed in other company for next 5 years


CSR

CSR Applicability Thresholds

- Applicable to every company having :
  - Net worth ≥ Rs. 500 crore, or
  - Turnover ≥ Rs. 1000 crore, or
  - Net profit ≥ Rs. 5 Crore

  during immediately preceding financial year – Section 135(1)

P & L (extract) of XYZ Limited for 2023-2024 (in Cr.)

Revenue from Operations	₹100.00
Other Income	₹2.00
Total Income	**₹102.00**
Cost of Materials Consumed	₹70.00
Employee Benefits Expense	₹10.00
Finance Costs	₹2.00
Depreciation and Amortization Expense	₹5.00
Other Expenses (including provision for bad debts ₹1.00	₹10.00
Unrealized Fair Value Loss (Investments)	₹1.00
Total Expenses	**₹98.00**
Profit Before Tax (PBT)	**₹4.00**
Less: Tax Expense	₹1.00
Profit After Tax (PAT)	**₹3.00**

Practice Pointer

- Section 135 Explanation states that:

  "For the purposes of this section "net profit" shall not include such sums as may be prescribed, and shall be calculated in accordance with the provisions of section 198."

Number of years

- Section 135(5) states that the Board of every company referred to in sub-section (1), shall ensure that the **company spends, in every FY**,
- at least **2% of the average net profits** of the company made:
  - ✓ during the **3 immediately preceding FYs**, **or**
  - ✓ where the company has **not completed the period of three FYs** since its incorporation, **during such immediately preceding FYs**,
- in pursuance of its CSR Policy

Illustration 2.1

- XYZ Limited was incorporated on 5th Jan., 2021. Compute the CSR Spending for the FY ending on 31st March, 2025 on the basis of following information:
  a) N.P. for the first FY: ₹60 crores
  b) N.P. for the second FY: ₹80 crores
  c) N.P. for the third FY: ₹100 crores

Solution 2.1

FY	Duration	Months	N.P.	Weighted Amount
21-22	5th Jan 2021 to 31st Mar 2022	15	₹60	₹60 × 15 = ₹900
22-23	1st Apr 2022 to 31st Mar 2023	12	₹80	₹80 × 12 = ₹960
23-24	1st Apr 2023 to 31st Mar 2024	12	₹100	₹100 × 12 = ₹1,200
	Total	**39**		**3,060**
	Weighted Average			**78.46 [3,060/ 39]**
	CSR Obligation			**1.57 [2% (x) 78.46]**

Academic Question

- Wipro Limited
- Azim Premji Foundation ~ section 8 company was established
- Wipro Limited is holding company of Azim Premji Foundation
- Wipro carried out CSR activities and spending through its such subsidiary
- Question:
  - What are the accounting disclosures for holding company vis-à-vis subsidiary
  - Whether such subsidiary needs to be consolidated with Wipro
  - What are the audit report requirements under CARO, 2020

What are the accounting disclosures for holding company vis-à-vis subsidiary	• Disclose related party transactions in notes to accounts as per AS 18 or Ind AS 24
Whether such subsidiary needs to be consolidated with Wipro	• No consolidation ~ why • Accounting Standard 21/ Ind AS 110 ~ no consolidation if subsidiary cannot distribute profits to its members
What are the audit report requirements under CARO, 2016/ 2020	• Report CSR compliances

General Instructions For Preparation of Statement of Profit and Loss

Non-compliance	Requirement
• In one case, the company has incurred CSR expenditure; • The company has disclosed the CSR expenditure under the heading 'Other Expenses' with a sub-heading 'CSR Expenditure for the year'	

General Instructions For Preparation of Statement of Profit and Loss

Non-compliance	Requirement
• In one case, the company was engaged in manufacturing of cars and has made sale of scrap which was generated during the manufacturing process; • The company disclosed the sale of scrap as 'other non-operating income'	

General Instructions For Preparation of Statement of Profit and Loss

Non-compliance	Requirement
• In one case, the company was having interest from customers on amounts overdue; • The company has disclosed the same as 'other operating revenue'	

General Instructions For Preparation of Statement of Profit and Loss

Non-compliance	Requirement
• In one case, certain penalties were levied upon the company under PF Law; • The company has disclosed the same under 'Employee Benefit Expenses' as 'contributions to provident fund'	

General Instructions For Preparation of Statement of Profit and Loss

Non-compliance	Requirement
• In one case, the company has taken certain assets on finance lease and was paying lease rent for the same; • The company has disclosed the finance charges on finance leases under the heading 'Miscellaneous Expenses'	

General Instructions For Preparation of Statement of Profit and Loss

Non-compliance	Requirement
• In one case, the company has paid some interest on shortfall in payment of advance income-tax; • The company has clubbed such interest with ‘current tax’ under the heading ‘Tax Expense’	• GN states that interest on shortfall in payment of advance income-tax is in the nature of finance cost and hence should not be clubbed with the Current tax; • The same should be classified as Interest expense under finance costs. However, such amount should be separately disclosed.

Issue: Earning Per Share

Para 15 of Accounting Standard 20, "Earnings Per Share", requires that ***BEPS should be calculated by dividing net profit for the period attributable to the equity shareholders by weighted average number of equity shares outstanding during the period***.

From the above Para 15 of AS 20, an entity should use weighted average number of equity shares outstanding during the period. It can't use number of equity shares outstanding either at the beginning or at the end of the year, ***except when there is no increase/ decrease in equity share capital during the period***.

Referring to above, in the instant case Company Z has not computed BEPS correctly.

- RST Limited
- 1st April, 2021 – Equity Shares – 10,000 shares
- 1st Oct, 2021 – fresh issue – 1,000 shares (additionally issued)
- 31st March, 2022 – outstanding equity shares – 11,000 shares
- PAT = Rs. 1,10,000
- BEPS = 1,10,000/ 11,000 = Rs. 10 = is it correct ?

- RST Limited
- 1st April, 2021 – Equity Shares – 10,000 shares
- 1st Oct, 2021 – fresh issue – 1,000 shares (additionally issued)
- 31st March, 2022 – outstanding equity shares – 11,000 shares
- PAT = Rs. 1,10,000
- BEPS = 1,10,000/ 11,000 = Rs. 10 = is it correct ? = no
- Weighted Avg. Number of Equity Shares = [(10,000 (x) 12/12) + (1,000 (x) 6/12)] = ’10,500’ number of shares
- BEPS = 1,10,000/ ’10,500’ = Rs. 10.48 = this is correct position as per AS 20

Other Observations

Units of Measurement

Non-compliance

- It was observed from note relating to RP Disclosures given in the Annual Report of a company that the amounts of corporate guarantees given on behalf of RPs were disclosed in foreign currencies.
- It was observed that whereas in the given case the financial statements have been reported in rupees, certain transactions under related party disclosures have been reported in terms of US dollars (USD), Australian Dollars (AUD) and Japanese Yens (JPY)

Requirement



Issue: Cash Flow Statement

In the cash flow statement an entity has categorised its cash flows during a particular period into four categories, which are, Cash flow from Operating Activities, Cash flow From Investing Activities, Cash Flow from Financing Activities and Cash flow from Other Activities.

Whether the entity has categorised its cash flows correctly as per AS 3/ Ind AS 7, Cash Flow Statements?

Particulars	Amount (Rs.)	Amount (Rs.)
Net Profit before Tax	1,000	
Non-cash items and working capital adjustments	(100)	
Cash from Operating Activities (A)		900
Cash from Investment Activities (B)		500
Cash from Financing Activities (C)		(200)
Net increase in cash and cash equivalents [(A) + (B) + (C)]		**1,200**
Cash and cash equivalents at beginning of period (D)		**1,800**
Cash and cash equivalents at end of period (E)		**3,100**
Changes during year on account of (D) and (E)		**1,300**

Particulars	Amount (Rs.)	Amount (Rs.)
Net Profit before Tax	1,000	
Non-cash items and working capital adjustments	(100)	
Cash from Operating Activities		900
Cash from Investment Activities		500
Cash from Financing Activities		(200)
Cash from Other Activities		**100**
Net increase in cash and cash equivalents		**1,300**
Cash and cash equivalents at beginning of period		**1,800**
Cash and cash equivalents at end of period		**3,100**

Issue: Related Party Disclosures

As per AS 18/ Ind AS 24, if there have been transactions with related parties, during the existence of a related party relationship, ***the entity should disclose a description of the relationship between the parties***.

In the instant case, C Ltd. has disclosed description of relationship only in case of transactions with KMP and their relatives, but has not disclosed the type of relationship in case of transactions with other related parties.

Therefore, related party transactions in this case have not been properly disclosed.

Issue: Govt. Grants related to revenue

A company (say Company X) is engaged in the business of manufacturing and selling of tea. During the previous financial year it had received subsidy on fertilisers from the government. While preparing financial statements for previous year, X has clubbed the amount of subsidy with revenue of that year.

Is accounting treatment of governmental subsidy correct?

- As per AS 12/ Ind AS 20, Government grants related to revenue should be recognised on a systematic basis in the profit and loss statement over the periods necessary to match them with the related costs which they are intended to compensate. **Such grants should either be shown separately under 'other income'** or deducted in reporting the related expense.
- Therefore, the company X should disclose the subsidy on fertilisers as other income or should net off the amount of subsidy from the expenditure incurred on purchase of fertilisers.

Issue: Provision for gratuity

An entity has a rule that no gratuity shall be payable to an employee if he or she leaves service before completion of five years. The company believes that no liability should be accrued for gratuity till the first five years of an employee.

Is the contention of the company correct ?

- Albeit the gratuity benefit may not vest in first five years, yet there is a probability that certain employees shall complete five years and shall become eligible for gratuity. Merely because a benefit has not vested does not mean that the obligation does not exists. **The 'probability' concept account for percentage of employees for which the benefit will/ will not vest.** Accordingly provision should be created during the first five years of service.
- In other words, **the benefit of gratuity although becomes payable after 5 years but the obligation accrues over a period of 5 years.** Hence an entity must estimate the number of employees who will become eligible for gratuity (depending upon the attrition percentage across different levels) and accordingly estimate the amount of provision required each year even if the employees are not eligible for gratuity as on date.

Issue: Interest on borrowed funds, initially capitalized as per accrual concept but later waived off by lenders

A company is engaged in business of manufacturing and sale of chemicals. The company borrowed funds for purchasing of assets in the preceding years. Interest cost on the borrowed funds was capitalised in accordance with the laws and regulations till the time of commercial production. Later on after the start of commercial production, no interest was paid to lender because of the financial problems. During the current year the company repaid the principal amount to the lenders and as per the arrangement the lenders waived off the interest which was already capitalised. The company recognised the waived interest as capital reserve. How should such interest waiver be treated in books of account ?

- No, the interest waiver cannot be recognised as a capital reserve. Instead, **the interest that has been capitalised as part of the historical cost of the asset and has subsequently been waived off, should be reduced from the fixed asset cost and accumulated depreciation**. The adjustment should be carried out as on the date of waiver. The rationale is that, since the asset has been correctly capitalised based on actual cost incurred, but subsequently not paid, the capitalised amount of the fixed asset should be reduced - EAC opinion Query 23 Volume 23

Issue: Disclose whether entity has conducted any impairment test

In the financial statement a company (F Ltd.) has not disclosed any information to indicate that it has conducted any impairment test of its assets during the financial year.

Is it correct disclosure?

- As per AS 28/ Ind AS 36, "Impairment of Assets“ an entity should assess at each balance sheet date whether there is any indication that an asset may be impaired.
- So, **an entity should disclose either its accounting policy in respect of impairment of assets** or whether the entity has conducted impairment test during the financial year. In the instant case, F Ltd. also should disclose the same.

Thank you

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