

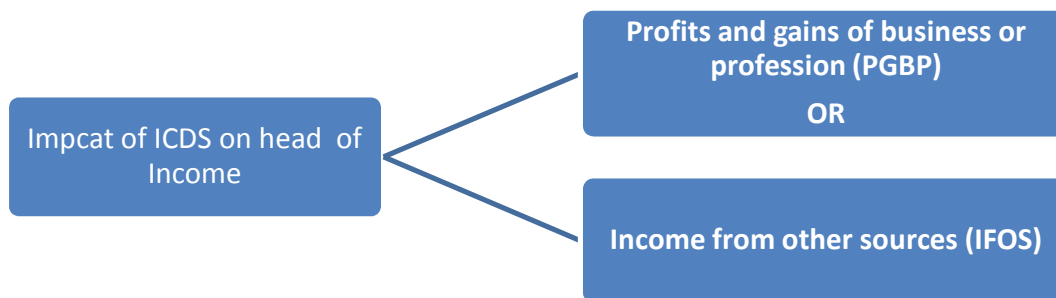
All about Income Computation and Disclosure Standards (ICDS)

1. Introduction

The Central Government recently notified **10 (number of ICDS)** Income Tax Computation & Disclosure Standards (**ICDS**) effective financial year 2015–16 (**P.Y.- 01.4.2015 / A.Y. - 2016-2017**). {Wide Notification No. 32/2015, F.No.-134/48/2010-TPL, Dated- 31st March, 2015 }

This will **affect the compliance practice** of all taxpayers following the mercantile system of accounting for computing income chargeable to income tax under **the heads:**

- ✓ **Profits and gains of business or profession**
- Or
- ✓ **Income from other sources**



2. Objective of ICDS

ICDS were developed with a view to **minimizing tax related disputes** by bringing greater consistency in the application of accounting principles governing the computation of income. These standards were developed using the old Indian General Audit and Accounting Practices (GAAP).

3. Main Features of ICDS

- In case of conflict between the provisions of the Income-Tax Act, 1961 and ICDS, then the provisions of the Income-Tax Act would prevail.
- No need to maintain separate books of accounts for ICDS. It only for income computation.

4. Applicability

- Applicable to all Assesses following Mercantile System of Accounting and chargeable to tax under the head “**Profit and Gains of Business or Profession**” (PGBP)
OR “**Income from Other Source**” (IFOS)
- It is applicable to **all** assesses
- Irrespective of applicability of Tax Audit
- Irrespective of Turnover

- Irrespective of Status of Individual (AOP, Firm, Resident, Non Resident etc.)

5. Non Compliance of ICDS

Every assessee is required to implement ICDS and **potential impact will be considered by companies while estimating advance tax liability for FY 15-16, due on 15 June 2015.** Noncompliance of ICDS will result in **best judgment assessment** by tax authorities, which may lead to protracted litigations.

6. List of ICDS

Sr. No.	No.	Income Computation and Disclosure Standards	Corresponding Accounting Standards
1	ICDS- I	Accounting Policies	AS-1
2	ICDS -II	Valuation of Inventories	AS-2
3	ICDS -III	Construction Contracts	AS-7
4	ICDS -IV	Revenue Recognition	AS-9
5	ICDS -V	Tangible Fixed Assets	AS-10
6	ICDS -VI	The Effect of Changes in Foreign Exchange Rates	AS-11
7	ICDS -VII	Government Grants	AS-12
8	ICDS -VIII	Securities	AS-13
9	ICDS -IX	Borrowing Cost	AS-16
10	ICDS -X	Provisions, Contingent Liabilities and Contingent Assets	AS-29

7. Impacted areas

1. ICDS – I (Accounting Policy)

- **No Concept of Materiality in ICDS** unlike, AS-1. In absence of materiality concept, considerable time and cost will be involved making adjustments in net profit to arrive at PGBP income.
- ICDS provides that expected losses or mark to market losses **shall not be** recognized. **However**, ICDS is silent on Mark-to Market (MTM) gains.

Year	Loss	Anticipated Income	Computation		Remarks
			Income tax	Books of Accounts	
1	Expected loss = (5000)	Anticipated income = 1000	1000	(5000)	Foreseeable loss is not allowed as per ICDS in year 1. But tax is required to be paid on anticipated profit.
2	Actual loss = (5000)	Actual income = 1000	(5000)	1000	As per ICDS, the actual loss will now be allowed in year 2 and actual gain will be regarded as income. However provision of MAT is

					also applicable.
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II. ICDS – II (Valuation of Inventories)

Valuation in case of Business Concern

- Value of Opening Inventory should be same **as proceeding's year closing inventory**. In case of new business cost of inventory will be considered.
- Cases of conversion of Capital asset into Stock in trade will remain unaffected because of overriding provision of sec 45(2).
- If the case is of Slum Sale then price paid will be the **cost** of Opening Inventory.

Valuation in case of Service provider

- Value of Service Inventory to be lower of **Cost OR NRV**.
- Cost to Include Labour and other Cost of personnel directly engaged in providing services

Impact:-

Difficulty would arise in case of services whose chargeability depends upon the success of service.

Valuation of inventory in case of AOP/BOI/Firm/Dissolution

- In case of dissolution of AOP/BOI/Firm, notwithstanding whether the **business is discontinued or not**, the inventory on date of dissolution shall be valued at **NRV**

Impact:-

This is contrary to Law Settled by Court in case of **Shakti Trading Co vs. CIT** in which it was held that at time of dissolution if business is not discontinued then stock should be valued at lower of **NRV or Cost**.

III. ICDS – III (Construction Contracts)

• Recognition of Contract Revenue

Contract revenue to be recognised when there is reasonable certainty of its ultimate collection. The criteria **“If it is possible to reliably measure the outcome of contract”** have been omitted.

• Retention Money

Contract revenue shall comprise of initial amount of revenue including **Retentions**.

• Incidental Income

Contract cost shall be by any incidental income, not being in nature of interest, dividends, capital gains etc. However these incomes like interest, dividend, and capital gain shall be taxed as income.

• Recognition of Foreseeable losses

ICDS does not allow recognition of foreseeable/Expected losses on a contract.

• Situation when outcome of contract cannot be reliably estimated

ICDS provides that early stage of contract shall not exceed 25% of stage of Completion. In other words, up to 25% of stage of completion if the outcome cannot be reliably measured, contract revenue is recognised only to extent of its cost.

- **Recognition of Claims/Incentive payments**

If Incentive payments & Claims are reliably measurable and it is probable that it will result in revenue then ICDS states that we need to recognise them.

IV. **ICDS – IV (Revenue Recognition)**

- As per AS-9 revenue from service transaction are recognised as percentage completion method or by completed service contract method but ICDS provides only for **percentage completion method** for recognition of service transactions. No recognition is done as per Completed service contract method.

- For a transaction undertaken on or before 31st March 2015 but not completed shall be recognised as per ICDS.

V. **ICDS – V (Tangible Fixed Assets)**

- **Asset acquired against non-monetary consideration**

- When a tangible asset is acquired for other asset, the **FMV** of tangible asset **acquired** shall be actual cost.
- When a tangible asset is acquired for shares or other securities, the **FMV** of tangible asset **acquired** shall be actual cost.

- ICDS applies only to fixed assets, **doesn't cover goodwill**.

- ICDS use the word **Actual Cost** as comparative to word **Cost** defined in AS-10. Such a narrow definition in ICDS might encourage the taxpayer to contend that expenditure on acquisition which is not part of actual cost should be deductible as revenue instead of capitalising.

- As per AS-10 if several assets are purchased for consolidated price, consideration is apportioned on fair basis as determined by **competent valuers**. But in ICDS there is no concept of competent valuers. The consideration shall be apportioned to various assets on **fair basis**.

- Right now there is no statutory requirement of maintaining fixed asset register for non-corporate entities subjected to that they will not cover under tax audit. But ICDS specifies the parameter to consider while maintaining the fixed asset register i.e. description of assets, location, actual cost subject to some adjustment, date of asset first put to use.

VI. **ICDS – VI (The Effect of Change in Foreign Exchange Rate)**

- Exchange difference arising on settlement thereof or on conversion of **monetary items** at the last day of previous year shall be recognised as **income or expense** in that previous year by converting into reporting currency using **closing rate**.

- **Non-monetary items** in foreign currency shall be converted into reporting currency by using exchange rate at **the date of transaction** and exchange difference shall **not** be recognise as **income or expense**.

- **Premium or Discount** arising in foreign exchange contract shall be amortised over life of contract and exchange difference shall be recognised as income or expense in that period.

VII. ICDS – VII (Government Grants)

- **AS-12** said that when the government grant relates to a depreciable fixed asset or assets of a person, the grant shall be deducted from **the actual cost of asset or from the Written down value** of block of asset to which concerned asset is belonged.

Where **ICDS** emphasize on deduction of grant from **the original cost**, IND AS-20 prescribe for setting of grant as deferred income and transfer to statement of profit and loss on systematic basis.

- Further AS-12 provides for postponement of government grant beyond the date of actual receipt where condition attached are not fulfilled but as per ICDS no postponement is possible.

Impact:- ICDS requires recognition of **any subsidy** as income which is conflicting with the act. To circumvent the same it is proposed to amend the definition of income under section 2(24) by inserting a new sub clause (xviii) to provide that assistance in form of subsidy or grant or cash incentive or drawback or reimbursement by Government in cash or kind shall be **the income of assessee (other than one consider under explanation 10 of section 43(1))**

VIII. ICDS – VIII (Securities)

- ICDS states that securities held as stock in trade shall be valued at actual cost or NRV whichever is lower (Cost shall be determined on the basis of FIFO method).
- AS-13 and ICDS both requires the adjustment of pre-acquisition interest from cost
- ICDS states that when a security is acquired in exchange of other security then, **FMV of security so acquired** will be the actual cost.
- ICDS states that valuation will be done on **category basis** no individual basis will be followed. Valuation of unlisted shares or listed but not quoted on recognised stock exchange shall be done at **actual cost**.

Shares	Cost	NRV	AS-13 (Cost or NRV whichever is lower)	ICDS
XYZ	50	60	50	—
ABC	100	50	50	—
DEF	200	300	200	—
TOTAL	350	410	300	350

IX. ICDS – IX (Borrowing Cost)

- The Income tax act provides for deduction of interest except in respect of capital borrowed for acquisition of asset for extension of existing business or profession. ICDS provides for **capitalisation** of borrowing cost without any exception.
- AS-16 requires income from temporary deployment of unutilised funds to be reduced from borrowing cost but ICDS **does not** provide the same. Income from temporary Investment will be considered under the head **Income from Other Sources**.
- Borrowing Cost incurred during the period in which active development of asset is interrupted can also be
- **Cessation of Capitalisation**
 - Qualifying Asset- Asset first put to use.
 - Inventory- Substantially all activities necessary to prepare for its intended sale are complete.
- ICDS defines what is Qualifying Asset which means
 - Tangible Assets – Land, Plant etc.
 - Intangible Assets – Patents, Licences etc.
 - Inventories that requires 12 months or more to bring them to saleable condition.

Impact:

- Specified Tangible & Intangible assets are qualifying assets regardless of substantial period of condition
- ICDS includes Land in definition of qualifying assets, unlike AS-16

X. ICDS – X (Provisions, Contingent Liabilities and Contingent Assets)

- Provision shall be recognised if it is **reasonably certain** that outflow of economic resources will be required. Criteria for recognition of provision on basis of ‘probable’ replaced with requirement of ‘reasonably certain’. However, in the absence of definition and scope of **reasonably certain**, an ambiguity would arise on assessment of its criteria.
- Provision made on obligations recognised out of customary business practices or voluntary obligations may not be allowed (e.g. informal refund policy to dissatisfied customer etc.)
- Contingent asset/ claims to be recognised if inflow of economic benefit is **reasonably certain**.

❖ CONCLUSION:-

- ✓ The ICDS should also entail appropriate modification in Income tax return and Form 3CD.
- ✓ The ICDS seem to be based on the current AS issued by ICAI. However listed Companies are required to adopt IND AS from 1st April 2016. Thus, the accounting policies for these companies under IND AS could be significantly different from ICDS.
- ✓ Thus, providing clarity on tax position in ICDS in alignment with IND AS is also essential.

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