INDIAN ACCOUNTING STANDARDS

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MEANING OF ACCOUNTING STANDARD

- A 'standard' means a generally accepted model or an ideal.
- Thus, accounting standard means generally accepted accounting principles.
- Accounting Standards are written documents containing the 'Generally Accepted Accounting Principles (GAAP)' issued by ICAI in India.
- There are 32 AS in India as on date
- The main objective of Accounting Standards is to standardise the different accounting policies and practices followed by different business concerns

- Accounting Standards Board (ASB) set up in 1977 by ICAI prepares accounting standards.
- The Central Council of the ICAI notifies the final standard, after consultations and discussions.
- Considerations:
  - ➢The Indian laws, customs and business environment
  - ➢International Accounting Standards given by IASB
  - ➢Purposes and limitations of published final accounts
  - ➢The role of the auditors

BENEFITS OF ACCOUNTING STANDARDS

- Reduce variations in accounting treatment
- Additional Disclosures
- Helps Comparison

LIMITATIONS OF ACCOUNTING STANDARDS

- Difficult choice
- Mechanical
- Differ from law

AS 1 – DISCLOSURE OF ACCOUNTING POLICIES

- This standard deals with the disclosure of significant policies followed in preparing and presenting final accounts.
- Accounting policies refer to the specific accounting principles and the methods of applying those principles adopted by the concern in the preparation and presentation of final accounts.
- The accounting policies followed change from concern to concern. The disclosure of accounting policies followed helps to properly study, compare and judge the figures in the final accounts.

AS 1

- AS 1 is a compulsory standard to be followed by all concerns (whether a firm, proprietorship or company)
- The fundamental accounting assumptions are Going Concern, Consistency and Accrual. The fundamental accounting assumptions are usually not specifically disclosed because their acceptance and use are assumed.
- Major factors to be considered while selecting and applying accounting policies are Prudence, Substance over form and Materiality.

AS 1

Areas in which different accounting policies may be adopted are:

- •Methods of depreciation
- •Treatment of expenditure during construction
- •Conversion of foreign currency items
- •Valuation of stock
- •Valuation of goodwill
- •Valuation of investment
- •Treatment of retirement benefits
- •Recognition of profit on long-term contracts
- •Valuation of fixed assets
- •Treament of contingent liabilities

AS 1

A concern should select such accounting policies as to enable it to present a true and fair view of its state of affairs.

Rules to be followed in disclosure of accounting policies :

- Any important change in an accounting policy should be disclosed
- Such disclosure should form part of the final accounts
- All policies should be disclosed in one place instead of being scattered at many places in several schedules and notes to the accounts.
- Any important change in an accounting policy should be disclosed.

AS 1

- The effect of such change on the value of any item in the final accounts should also be disclosed. If such amount cannot be ascertained, wholly or in part, such fact should be disclosed.
- A change likely to have an effect not in current but in later years should also be disclosed in the year in which the change is made.
- Disclosure of accounting policies or of changes therein cannot remedy a wrong or improper entry in the accounts.

AS 6 – Depreciation Accounting

Depreciation is a measure of the wearing out, consumption or other loss of value of a depreciable asset arising from use, efflux of time or obsolescence through technology and market changes.

Amortisation means depreciation of assets whose useful life is predetermined.

AS 6 – Depreciation Accounting

Depreciable assets are:

- ➢ Expected to be used during more than one accounting period
- ➢ Have a limited useful life
- ➢ Hold for use in production / supply of goods and services, for rental, or administrative purposes and not for sale

Not all fixed assets are depreciable eg. Land

AS 6

Useful life can be calculated based on:
Period of use
Number of production or similar units to be obtained from use

Depreciable amount of a depreciable asset is its historical cost, or other amount substituted for historical cost.
Depreciation is charged in each accounting period based on depreciable amount, even if market value has increased.

Cost of depreciable asset means the expenditure on its acquisition, installation and commissioning. It also includes cost of additions or improvement of the asset.

AS 6

Amount of depreciation depends on :
Cost of the asset
Expected useful life of asset
Estimated residual (scrap) value of asset

The depreciable amount of a depreciable asset should be allocated on a systematic basis to each accounting period during the useful life of the asset.

AS 6

Most common methods of depreciation used are Straight line method and Reducing balance method. The depreciation method selected should be applied consistently from period to period. Factors considered are type of asset, nature of use of asset, circumstances in business.

Methods or Rate of depreciation may be provided by law governing an enterprise eg. Companies Act, 1956. Management of company can adopt higher rate. But can adopt lower rate only if the Act so permits.

AS 6

Any addition which becomes an integral part of the existing asset should be depreciated over the remaining useful life of that asset. Where an addition has a separate identity, depreciation on the same should be provided independently on the basis of an estimate of its own useful life.

Where a depreciable asset is disposed off, scrapped, etc., the net surplus or deficiency should be disclosed separately.

AS 6

Change in method is treated as change in accounting policy and is disclosed accordingly. Method should be changed only if required by law or an accounting standard. In such case, depreciation is recalculated from the date of the asset coming into use. The deficiency or surplus should be adjusted in the Profit & Loss Account for the year in which the method of depreciation is changed.

Details to be disclosed in financial statements are historical or revalued cost, method of depreciation, depreciation for the period, accumulated depreciation.

In case of revaluation, provision for depreciation is based on revalued amount on remaining useful life.

AS 9 REVENUE RECOGNITION

- This AS specifies the timing of recognition of revenue, i.e. when the income should be credited to Profit & Loss Account.
- According to AS-9, revenue means the amounts earned from customers for sale of goods, services given, or for use of funds or assets.
- Total revenue is computed by adding up the sale price of goods sold, fees for services, interest on loans given, dividend on shares and royalty for use of patents, know-how, etc.

AS 9

- Revenue from sale of goods is recognised when the seller has transferred the property in the goods to the buyer for a price. The transfer of property is said to take place when the risks and rewards of ownership are transferred to the buyer and the seller has no longer any effective control over the goods.
- Revenue from services is recognised either by the Proportionate Completion Method or the Completed Service Contract Method.
- Interest on cash or debts due to the concern accrues and is booked on time basis taking into account the principal outstanding.

AS 9

- Royalty on patents, trademarks, copyrights, know-how accrues and is booked as per the terms of the relevant agreement.
- Dividends on shares are booked when the right to receive payment is established.

Revenue should be recognised only when no significant uncertainty exists regarding the amount of the consideration that will be derived and about its ultimate collectability.

AS 10 ACCOUNTING FOR FIXED ASSETS

- As per AS 10, Fixed asset is an asset held for the purpose of producing or providing goods or services and not for sale in the normal course of business.
- Fixed assets often comprise a significant portion of the total assets of an enterprise, and therefore are important in the presentation of financial position.
- Fair market value is the price that would be agreed, in an open and free market, between knowledgeable, willing and unrelated parties.

AS 10

- Gross book value of a fixed assets is its historical cost. When this amount is shown net of accumulated depreciation, it is termed as net book value.
- Stand-by equipment and servicing equipment are normally capitalised.
- Machinery spares are usually charged to the Profit & Loss A/c as and when consumed.

AS 10

- Machine and its major component are treated as two separate fixed assets if one of them is likely to have a shorter useful life than the other.
- The cost of an item of fixed asset comprises its purchase price, including import duties and other non-refundable taxes or levies and any directly attributable cost of bringing the asset to its working condition for its intended use; any trade discounts and rebates are deducted in arriving at the purchase price. Examples of directly attributable costs are:

(i) site preparation;
(ii) initial delivery and handling costs;
(iii) installation cost, such as special foundations for plant; and
(iv) professional fees, for example fees of architects and engineers.

AS 10

- Financing costs for acquisition of fixed assets should be capitalised under AS 16 Borrowing costs.
- Administration and other general overhead expenses are usually excluded from the cost of fixed assets unless they relate to the acquisition of a particular fixed asset.
- The expenditure incurred on start-up and commissioning of the project, including the expenditure incurred on test runs and experimental production, is usually capitalised. The expenditure incurred after the plant has begun commercial production is not capitalised and is treated as revenue expenditure.

AS 10

- If the interval between the date a project is ready to commence commercial production and the date at which commercial production actually begins is prolonged, the expenditure incurred during this period is also sometimes treated as deferred revenue expenditure to be amortised over a period not exceeding 3 to 5 years.
- Cost of self-constructed fixed assets is calculated on same basis as purchase of fixed asset.
- Cost of fixed asset acquired in exchange is taken as the fair market value of either the asset given or the asset acquired whichever is more reasonable.

AS 10

- The cost of an addition or extension to an existing asset which is of a capital nature and which becomes an integral part of the existing asset is usually added to its gross book value.
- Any addition or extension, which has a separate identity and is capable of being used independently after the existing asset is disposed of, is accounted for separately.
- When several fixed assets are purchased for a consolidated price, the price should be divided among various assets on a fair basis, with the help of expert valuers.

AS 10

- Commonly accepted and preferred methods of restating fixed assets are 1) appraisal, normally undertaken by competent valuers, 2) indexation, or 3) reference to current prices.
- The revalued amounts of fixed assets are presented in financial statements either by

i) restating both the gross book value and accumulated depreciation so as to give a net book value equal to the net revalued amount or ii) by restating the net book value by adding therein the net increase on account of revaluation.

AS 10

- An increase in net book value arising on revaluation of fixed assets is normally credited directly to revaluation reserves. A decrease in net book value arising on revaluation of fixed assets is charged to profit and loss statement.
- An item of fixed asset is removed from the financial statements on disposal. Gains or losses arising on disposal are generally recognised in the profit and loss statement.

AS 10

- If there is profit or loss on sale of revalued asset, such difference amount is charged to revaluation account.
- Goodwill, in general, is recorded in the books only when some consideration in money or money's worth has been paid for it.
- Whenever a business is acquired for a price which is in excess of the value of the net assets of the business taken over, the excess is termed as 'goodwill'.

AS 10

Further disclosures that are made in financial statements include:

(i) gross and net book values of fixed assets at the beginning and end of an accounting period showing additions, disposals, acquisitions and other movements;

(ii) expenditure incurred on account of fixed assets in the course of construction or acquisition; and

(iii) revalued amounts substituted for historical costs of fixed assets, the method adopted to compute the revalued amounts, the nature of any indices used, the year of any appraisal made, and whether an external valuer was involved in carrying out the revaluation.

THE END