

# KARNATAKA STATE LEVEL CA CONFERENCE

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**BANGALORE BRANCH OF SIRC OF ICAI**

*16th June 2018*

## **ICDS – Confusion & Distortion – Final Position**

[After Delhi HC verdict and Revalidation thro Finance Act 2018]

Including its

**Impact (₹) & Practical Issues (?)**

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**BANGALORE**

## ICDS – Confused & Distorted History

1. Started in draft as **Tax Accounting Standards**
2. ICDS notified U/s.145(2) in March 2015 WEF AY 2016-17 - **Later rescinded**.
3. **New amended ICDS notified** in Sep. 2016 **WEF AY 2017-18**.
  - ICDS - in case of conflict, provisions of Act would prevail over ICDS.
4. **FAQ-2 stated ICDS overrides judicial precedents** although several taxpayers deviated from ICDS treatment for AY 2017-18 by considering **Provisions of Act** (as interpreted by settled judicial precedents).
5. Above position of taxpayers affirmed in Nov 2017 by Delhi HC in “**CTC v. Union of India**”, which **struck down many provisions of ICDS** as ultra vires (as interpreted by judicial precedents).
6. **Finance Act 2018 WREF AY 2017-18** amended IT Act incorporating ICDS provisions.
  - a. Retrospective - unexpected  
**[Reason - many taxpayers already complied & not to put them into inconvenience !!]**
  - b. ICDS applicable to All taxpayers (other than individuals & HUFs who are not s.t tax audit U/s.44AB) following Accrual system for computing business income or IOS.  
**Unfortunately, amendments in IT Act wrt ICDS do not expressly provide that it applies only to assesseees to whom ICDS are applicable.**

**?? What does ICDS Version 2016 contain - What part of it was struck down - What part of it has been restored thro IT Act??**

## Final Notified 10 ICDS

AS	ICDS	Title	Delhi HC Struck down - X	Sec No. <i>(9 Sec. Amended ITA 2018)</i>
1	I	Disclosure of Accounting Policies	Fully	36(1)xviii) & 40A(13)
2	II	Valuation of Inventories	Fully	145A
7	III	Construction Contracts	Para 10 (a) Retention money & 12 incidental income	44AD, 50C, 43CA, 43CB
9	IV	Revenue Recognition	Para 5 export incentive & 6 PCM on Services	145A, 43CB & 145B
10	V	Accounting for <u>Tangible</u> Fixed Assets	-	2(11), 43(1), 43(6), 35D
11	VI	Effects of Changes in Forex Rates	Fully	43A, 43AA
12	VII	Accounting for Government Grants	Para 4(2) GG recd. cannot be postponed after receipt.	Expln.10 to S.43(1), 145B
13	VIII	Accounting for Investments / Securities	Part A Fully	Investment Vs. Business– Circular. 145A
16	IX	Borrowing Costs	Para 5 incidental income	S.36 (1) (iii), Expn.8 to S.43 (1), Rule 8D
29	X	Provisions, Cont. Liabilities &. Assets	-	S.43B, S.40A(7)
270	60	← Total Pages	53	

**Draft ICDS on Real Estate Transactions issued in May 2017. Not yet notified - ?!!??**

ADD back	(₹)
1. Disallowance of exp. debited on a/c of exercising <b>Prudence</b> @ 36(1)xviii) & 40A(13)	Delhi HC X @
a. Expected losses	
b. Marked to Market Loss [MTM Gains not to be considered - FAQ-8]	
c. Any other	
2. Disallowance of expenditure debited on account of <b>Materiality !!!</b>	

## Accounting Policy – ‘Removal of Prudence’ objected but not sustained !

### Delhi High Court

*Contrary to decisions in Triveni Engineering & Industries Ltd (2011) 49 DTR 253 (Del) & Advance Construction Co. Pvt. Ltd. (2005) 275 ITR 30 (Guj). – Expected loss must be allowed forthwith.*

ICDS-I, which does away with the concept of 'prudence' - contrary to the Act & binding judicial precedents - So unsustainable in law.

### IT Act 2018

- a. Deduction of MTM loss or other expected loss to be computed **as per ICDS** - S.36 (1) (xviii)
- b. No deduction/ allowance of any MTM loss or other expected loss shall be allowed, **except those which are allowable** as per provisions of S.36(1)(xviii) – S.40A(13)

Present position By inserting S. 36(1), jurisdiction of S. 37(1) is ousted wrt MTM / OE Loss.

### ?? Issues ??

1. What MTM losses / Other EL allowable as per ICDS r/w S.36 & S.40A??
2. Disclose Accounting Policy or Computational Policy ??
3. How will absence of “Going Concern” Assumption impact Tax ??
4. “Materiality” not covered in ICDS - Will it impact tax computation materially ??

## Position wrt Issues in ICDS - I: Accounting Policies

### 1. What MTM losses or Other EL are allowable as per ICDS r/w. S.36 & S.40A??

Prudence followed on case to case basis in following cases and cannot be allowed generally.

*[as argued by the Dept in CTC case]*

- a. ICDS-2: **Cost or market price whichever is lower.**
- b. ICDS-3: **Contract loss allowed in proportion.**
- c. ICDS-4: **Revenue need not be recognized if there is no reasonable certainty of its collection.**
- d. ICDS-6: **Hedging losses allowed** (except for covering highly probable or firm commitment contracts).
- e. ICDS-8: **Securities held as stock measured at cost or NRV WIL** (but with “bucket principle valuation” only)
- f. ICDS-10: **Recognizes provision.**

### 2. Disclose Accounting Policy or Computational Policy ??

- ICDS is for computation of Income & not for maintenance of books of a/cs. [Preamble in all 10 ICDS]
- **FAQ-1** ICDS is Not for Accounting - but AP being fundamental shall be applicable for computing TI !!
- *TG of ICAI 3.6: “Computational Policy” !!!*

### 3. How will absence of “Going Concern” Assumption impact Tax ??

- Capital assets revaluations do not affect tax computations
- ICDS decline to recognize losses in valuation of assets on MTM basis

### 4. “Materiality” not covered in ICDS - Will it impact tax computation materially ??

- ICDS-1 requires True & Fair *[materiality embedded]* and NOT True & Correct
- *TG of ICAI 6.11 - ICDS is not driven by quantum considerations.*

ADD back	(₹)
<p>1. Change in value of Stock -</p> <p>A. If other than "FIFO or Weighted Average or Specific identification" Cost formula is applied.</p> <p><b>B. Distribution expenses also to be included in cost of inventory</b>  <i>TG of ICAI 10.4: If incurred at distribution depots - Don't consider.</i></p>	
<p>2. Consider Value of <b>inventory for service provider !!!!!</b>          [To the extent not recognized as revenue - See ICDS IV]  <i>TG of ICAI Says otherwise #</i></p>	
<p>3. <b>Inventory valued @ NRV on dissolution date, during dissolution of Firm, AOP or BOI <u>whether business is discontinued or not.</u></b></p>	Delhi HC X
<p>4. Like in AS - Standard cost technique now acceptable in ICDS <sup>v-2016</sup> along with Retail method - But in case of Retail Cost Tech. - "An Average percentage for each retail dept. is to be used." [Ver. 2016]</p>	

# Valuation of Inventories

## Delhi high court

In case of dissolution of firm	Value inventory @
If firm is continued	Cost or market value WIL – Sakthi Trading Co. -SC
If firm is discontinued	Market price only - A.L.A.Firm - SC

ICDS II is held to be ultra vires the Act and struck down as such.

[Delhi HC has struck down entire ICDS II for a defect in one para!!]

## IT Act, 2018 – S.145A:

i. Valuation of Inventory shall be at lower of actual cost or NRV computed **as per ICDS**.

ii. **Inclusive method continued and Extended to services also**

*Valuation of purchase & sale of goods **or services** and of inventory shall be adjusted to include the amount of **any tax, duty, cess or fee (by whatever name called)** actually paid or incurred by the assessee to bring the goods **or services** to the place of its location and condition as on the date of valuation.*

**Expl.1: For the purposes of this section, any tax, duty, cess or fee under any law for the time being in force, shall include all such payment notwithstanding any right arising as a consequence to such payment.**



## Position wrt Issues in ICDS - 2: Valuation of Inventories

### 1. What is the Tax Impact of “Inclusive method” of inventory valuation??

### 2. What is the Tax Impact of “Inclusive method” of Revenue Recognition??

ICDS also applies to non-corporate taxpayers who are not required to maintain books and/or covered by presumptive scheme of tax like S. 44AD, 44AE, 44ADA, 44B, 44BB, 44BBA, etc. [FAQ 3]

For computing presumptive income U/s.44AD, ICDS on Construction Contract or Revenue recognition applies for determining receipts or turnover.

Revenue = Gross inflow R/w S.145A = **Revenue is always Inclusive of Tax.**

### 3. **Inventory Valuation on dissolution - Controversy continues** as ICDS cannot prescribe under which scenario inventory to be valued - when S.145A says it must be at cost or at NRV WIL.

### 4. **Is WIP required to be considered for Service Providers?**

TG of ICAI Says No as definition of Inventory does not cover inventory #

**In the light of amended S.145A, Will ICAI's stand gets vindicated?**

EAC of ICAI in 2006 and Ind AS differs with the above TG !!

#### # Inventories are assets:

- i. *Held for sale in the ordinary course of business;*
- ii. *In the process of production for such sale;*
- iii. *In form of material or supplies to be consumed in production process or in rendering of services.*


**Cost of inventories** shall comprise all **costs of purchase**, **costs of services**, costs of. conversion & other costs incurred in bringing inventories to its present location & condition

**Cost Of Services in the case of service providers** shall consist of **labor & other costs of personnel** directly engaged in providing service incl. supervisory personnel & **attributable OHs.**

## ICDS - III: Construction Contracts

ADD back	(₹)
1. Income to be recognized under <b>Percentage of Completion Method</b> <i>(if following completed contract method - CCM is not permitted under ICDS - Also in AS)</i>	<b>43CB</b>
2. Disallowance of <b><u>expected loss</u> on contract recognized</b> <i>(Loss allowed in the year in which it is actually incurred)</i>	
3. <b>Contract revenue to include Retention Money</b> <i>(s.t reasonable certainty of its ultimate collection - FAQ-11)</i>	Delhi HC X <b>43CB</b>
4. <b>Contract revenue to be recognized beyond 25% stage</b> , if not done <i>(AS states in subjective terms that early stage revenue must not be recognized - whereas ICDS states that Contract revenue must be recognized beyond 25%)</i>	
5. <u>Contract Revenue not recognized</u> becoz <u>Construction Cost Not recognized</u> as expenditure is <b>not capable of being measured reliably.</b>	How to meas ure?
6. Contract Revenue not recognized becoz <b>Estimating outcome of contract cannot be reliably measured.</b>	

## ICDS - III: Construction Contracts

ADD back	(₹)
7. <b><u>Contract Cost</u></b> , fully written off since its recovery is not probable, to be included as cost & rework Profits arising thereof using PCM.	
8. <b>Incidental revenue (<i>Interest /dividend/ Capital Gains</i>) taxed separately and not to reduce from contract cost.</b> <b>[AS 7: Costs may be reduced by incidental income]</b>	Delhi HC X  43CB
9. <b><i>WIP on transition date : To continue as per the method regularly followed by the assessee. [Ver. 2016] !!!</i></b> 	

## Construction Contracts

### IT Act 2018 – S. 43CB

- a) Profits from a construction contract shall be determined on percentage of completion method in accordance with ICDS notified U/s. 145(2);
- b)
  - i. Contract revenue shall include retention money and accordingly retention money will be considered for above purposes.
  - ii. Contract costs shall also not be reduced by any incidental income in the nature of interest, dividend or capital gains.

### Position wrt Issues in ICDS - 3: CC

1. Retention money to be recognized only if there is reasonable certainty of its ultimate collection. *[para 9 & FAQ 11]*
2. Can Retention money recognized U/s. 43CB be written off as Bad debt u/s. 36(1)(vii) if collection is not reasonably certain?  
Revenue recognized in ICDS but not in books - When such amounts are irrecoverable, such bad debts are allowed as deduction. [2nd Proviso to S.36(1)(vii)].
3. Can incidental income other than interest, dividend or CG be reduced be reduced from Contract Cost? *[say rental income from temp. renting of premises.] - No bar*

## ICDS - IV: Revenue Recognition

ADD back	(₹)
Revenue recognition criteria in ICDS-III -CC shall apply Mutatis Mutandis.	
1. Revenue from <u>service transactions</u> to be recognized under <b>Percentage of Completion Method</b> (for service contracts with duration > 90 days -Ver 2016) (if following completed contract method, which is a permitted option in AS)	Delhi HC X - 43CB
2. When services are provided by an indeterminate no. of acts over a specific period of time, revenue <u>may be</u> recognized on a SLM basis over the specific period, <del>unless there is evidence that some other method better represents the pattern of performance.</del>  [2nd point inserted in Ver.2016. While AS-9 has the above para with the words in strike through portion, which means in ICDS there is no optional treatment.]	43CB
3. Revenue not recognized becoz <b>Amount of Revenue cannot be measured.</b> <del>or collectability</del>	How measured?
4. <b>Interest on statutory refund- Recognize on receipt basis. [Ver. 2016]</b>	

**Para 5 of ICDS IV** - Recognize income from Escalation of price & export incentive in year of making claim if there is 'reasonable certainty' of its ultimate collection.

**SC in CIT Vs. Excel Ind Ltd [2013] 358 ITR 295** held that right to receive coincides with right to pay - until such time no income is accrued. **Delhi HC X - 145B**

## Revenue Recognition

### IT Act 2018 – S. 43CB

- In respect of contract for providing services –
  - i. If contract duration is < 90 days, profits **shall be** determined using project completion method;
  - ii. If contract involves indeterminate no. of acts over a specific period of time, profits shall be determined using straight line method.
  - iii. Which is not covered by (i) or (ii) above, profits shall be determined on percentage of completion method in **accordance with ICDS notified U/s.145(2)**.

**Position wrt Issues in ICDS - IV : For Contract duration of < 90 days - Is there an option to follow PCM?? ICDS Provides it but S.43CB does not !!**

### IT Act 2018 – S. 145B - Year of taxability of certain income

ICDS provides for taxability of certain incomes even before it has accrued. To validate such provisions of ICDS, corresponding provisions incorporated in S.145B as follows:

Type of Income	PY in which it shall be taxed
Any claim for escalation of price in a contract or export incentives	PY in which reasonable certainty of its realization is achieved

**FAQ-13** Condition of reasonable certainty of ultimate collection is not laid down for taxing interest, royalty & dividend. Should they be taxed even when its collection is uncertain?  
*[But is available for Sale of Goods & Rendering of services (thro CC)]*

As a principle, interest accrues on time basis & royalty accrues on contractual terms. **Subsequent non recovery in either cases can be claimed as deduction in view of amendment to S.36 (1) (vii).** Further, Act (ex. S.43D) shall prevail over provisions of ICDS.

- What if it to be taxed under IoS?

**S.57 (iii)** - Any other expenditure (not being in the nature of capital expenditure) laid out or expended wholly and exclusively for the purpose of making or earning such income;

## ICDS - V: Tangible Fixed Asset

ADD back	(₹)
1. Disallowance of any <b>asset debited as expense on account of materiality</b> (FA - not material also needs to be capitalized as per ICDS)	
2. Depreciation effect in general continues but in particular the following - <b>Exchange of Asset</b> - Actual cost of asset acquired would be FV of TFA so acquired, as per ICDS. (AS-10 gives option of recording it at FMV of the asset given up, if it is more clearly evident)	
3. Depreciation to be provided as per Books to be added back and that allowed by the IT Act to be allowed.	

### In ICDS

- FA definition - **Consistent with 'Block of Asset' in Act** (*Exception -land*)
- **Valuation of individual asset if bought for consolidated price on a fair basis.** *AS-10 states as "determined by competent valuer"- Not told in ICDS.*



## Issues in ICDS - V Tangible Fixed Assets

### 1. A rare situation where Tax profit could be lower than Accounting profit !!

#### i. Replacement & Improvements:

AS-10(R) - Expense Current Repairs - Capitalize if it meets PPE criteria.

ICDS like Pre AS-10 - Capitalise if future benefit increases beyond its previously assessed standard of performance. Else? *(No Guidance in ICDS but allowable U/s.37)*

#### ii. FA Spares

AS 10(R) - Capitalise if it meets PPE criteria

ICDS like Pre AS-10 - Spares used with a particular FA & irregularly only must be capitalised - other Spares are Inventory.

### 2. **Can initial estimate of “Decommissioning, restoration & similar liabilities” be added to FA in IT?**

AS-10(R) - Capitalised initially and depreciated (with discounting)

ICDS V like Pre AS-10 - silent on this aspect but ICDS X - Provisions requires a provision made shall be the best entitlement of expense recorded to settle present obligation at the end of that year (without Discounting).

ADD back	(₹)
<p><b>1. Disallowance of MTM Losses / Gains on Premium, discount or ED intended</b></p> <p>a. For Trading or Speculation or</p> <p>b. Hedging FC Risk of firm commitment or highly probable forecast transaction  [Excl. those entered to hedge FC risk of Existing A/L]  <i>(MTM shall be allowed on such transactions at the time of settlement)</i></p>	<p>1.a Delhi HC X  43AA</p>
<p><b>2. Translation difference of assets of Non-Integral Foreign operations routed thro FCTRA</b> <i>(ED to be recognized thro P&amp;L as per ICDS)</i></p> <p><u>FAQ:</u> FCTR bal. on 1.4.2016 pertaining to ED on monetary items for NIFO, shall be recognised in AY 2017-18 if not recognised as income earlier.</p> <p><i>Ver.2016 makes no mention of IFO &amp; NIFO and Para 7 states FS of a Foreign Operation to be translated like other cases, as if, the transaction of FO had been those of the person himself. In effect for ICDS all FO to be treated like IFO only.</i></p>	<p>Delhi HC X  43AA</p>

# Effects of Changes in Foreign exchange rates

## IT Act, 2018 – S.43AA

Gain or loss in Foreign Exchange rates to be treated as Income or loss, under new S. 43AA, except for provisions contained in S.43A. Such gain or loss shall be computed in accordance with ICDS and shall be in respect of all foreign currency transactions, including those relating to –

- a) Monetary items and non-monetary items
- b) Translation of financial statements of foreign operations
- c) Forward exchange contracts
- d) Foreign currency translation reserve

### Position wrt Issues in ICDS - VI

1. FAQ that OB in FCTR on transition will be entirely taxed in AY 2017-18 is objectionable. Is it sustainable as no mention of it in Act or ICDS?
2. S.43A - Applicable only when Import of FA + Forex Loan taken - Else S.43AA

## Effects of Changes in Foreign Exchange Rates [*AS – 11* Vs. *ICDS-VI*]

***AS 11*** FO is a **SAJ or B** of reporting ent., activities of which are conducted in country other than country of reporting ent.

Particulars	I FO	NIFO (SAJ-B)
Monetary Assets – Long term receivables or Loans - repayment neither planned nor likely to occur in foreseeable future	P & L	B/S (FCTR A/c) @
Monetary Assets – Trade receivables / payables		P & L
Non-Monetary Assets - Investments	Not required	B/S (FCTR A/c) @

***ICDS #*** FO is a **Branch**, by whatever name called, activities of which are conducted in a country other than India

Particulars	IFO	NIFO	
		Sub-Asso-JV	Branch
All Monetary Assets	P & L	P & L	P & L
Non-Monetary Assets	Not required	Not required	P & L

### @ Until disposal of Net investment

**# Para 7 of ICDS:** FS of a FO shall be translated using principles & procedures in para 3 to 6 as if the transactions of FO had been those of the person himself.

**So - No distinction in treatment between IFO & NIFO.**

**In fact - No distinction between Forex translation between Indian operation & FO. [Ver.2016]**

## ICDS - VII: Government Grants

ADD back	(₹)
1. Grant received taxable - whether capital or revenue or promoter contribution. <i>(except if pertaining to fixed asset and reduced from its carrying value - Option of Capital approach as in AS-12 not provided in ICDS)</i>	
2. Govt. grants <b>postponed beyond the date of actual receipt</b> - as conditions required may not be complied.	<b>Delhi HC X</b>  <i>145B</i>

### **IT Act, 2018 – S.145B**

**Year of taxability of certain income** referred to in S. 2(24) (xviii) i.e., **subsidy, grant etc.** shall be **taxed in the PY in which it is received**, if not charged to tax in any earlier previous year.

## ICDS VII - GOVERNMENT GRANTS - Treatment as per ICDS

	Nature of Grant	Treatment
1	For depreciable asset	Reduced from actual cost / WDV.
2	For non-depreciable asset (S.t fulfilment of obligations)	Recognised as <b><u>deferred income</u></b> . <i>over which cost of meeting such obligations is charged to income.</i>
3	Other Grants (Residuary clause)	Recognised as income in year of receipt. <i>Definition of Income U/s. 2(24) amended to bring clarity &amp; align with ICDS.</i>
4	Non-monetary assets given at concessional rate	To be accounted on basis of their acquisition cost
5	Govt. Participation in ownership of enterprise.	ICDS not applicable

## ICDS - VIII: Securities

**ICDS Deals with securities held as “Stock-in-trade” - AS-13 deals with Current & LT Investments - excludes stock-in-trade from its scope**

ADD back	(₹)
<p><b>1. Valuation difference routed thro P&amp;L account wrt - <u>unlisted or unquoted listed securities</u></b>  <i>(Difference becoz AS-13 Valuation is based on whether it is Current or LT whereas ICDS permits only Cost based valuation)</i></p>	
<p><b>2. Difference due to amounts routed thro P&amp;L account becoz of following difference:</b></p> <p>a. <b>Listed Securities - Comparison of cost or NRV of securities as per ICDS done <u>category wise</u> and not individually as permitted in AS-13.</b>  <i>(individual option loss could be higher - significant change in result from current practice)</i></p> <p>b. <b>Investment acquired in exchange of Asset - Actual cost of Investment acquired would be FV of Investment so acquired in ICDS.</b>  <i>(AS-13 also gives an option of recording it at FMV of the asset given up, if it is more clearly evident)</i></p>	<p><b>2.a</b>  <b>Delhi HC X</b></p> <p><b>145A</b></p>

**ICDS VIII [part A] - NA to - Insurance Cos, MF, VCF, Banks & PFI.**  
**NBFCs have to comply with ICDS on Securities.**

**ICDS VIII [part B] - Applicable to – Scheduled Banks & PFI – Classification, recognition & measurement to comply with the extant guidelines issued by RBI.**

# Securities

## IT Act, 2018 – S.145A

In case of securities held as inventory, it shall be valued as follows:

Type of Securities	Method of Valuation
<u>Unlisted Securities</u> or <b>listed but not quoted</b> with regularity from time-to-time @?	At <u>actual cost</u> initially recognised <b>in accordance with the ICDS</b>
<u>Securities listed</u> and quoted on recognized stock exchange with regularity from time-to-time	At lower of actual cost or NRV <b>in accordance with ICDS</b> ; Comparison of actual cost & NRV value shall be made <b><u>category- wise</u></b>
<b>Securities held by a scheduled bank or public financial institution</b>	<b>in accordance with ICDS</b> notified after considering extant guidelines issued by RBI in this regard.

### Issues in ICDS - VIII

@? Unlisted Securities or listed but not quoted with regularity from time-to-time

**what constitutes regularity?**



## ICDS - IX: Borrowing Costs - BC

ADD back	(₹)
1. BC debited to P&L on TFA & IA not being qualifying asset (SPT < 12 period for construction) as per AS-16 [Such BC needs to be capitalized as per ICDS - Presently also so due to proviso to S.36(1)(iii)]	
2. BC debited to P&L "being incurred on TFA & IA whose active development is suspended" as per AS-16 [Such BC needs to be capitalized for Income Tax purpose]	
3. BC debited to P&L "being certain ED on forex loans to extent regarded as adjustment to interest cost" as per AS-16 [para 4(e)] [No such adjustments in ICDS]	
4. BC incurred on funds borrowed generally and utilized for Qualifying assets to be capitalized <u>as per formula given</u> in ICDS if different in A/cs.  Qualifying Asset Vs. Qualifying Asset Vs. Qualifying Asset	? complicated
5. Income from temporary use of unutilized borrowed funds - otherwise deducted from BC as per AS-16.	Delhi HC X @
6. BC on assets from 'Date ready to use' to 'actual date it is put to use'	

@ No corresponding amendment in Finance Act - Therefore, Delhi HC verdict can be said to be tacit approval of the legislation !!

**FAQ 20-** BC capitalized under ICDS-IX must exclude portion of BC disallowed U/s. like 14A, 43B, 40(a)(i), 40(a)(ia), 40A(2)(b), etc under such specific provisions.

## Capitalization of General Borrowing costs

[AS – 16 Vs. ICDS-IX]

### AS -16

- General BC to be capitalized determined by applying a **capitalization rate** being **weighted average of BC other than BC made specifically for obtaining a qualifying asset (QA)**.

### ICDS- IX

- Capitalization of general borrowings cost as per formula below:

$$A \times \frac{B}{C}$$

**A. BC incurred during PY on General borrowings**

**B. “QA (\*) less QA (\*) funded by specific borrowing”** – Considered as follows:

- **Average of above** on the first day and last day of PY or
- **Half of above** (in case where above does not appear in BS on the first day) OR
- **Simple average of above** appearing on first & date of put to use or completion  
(in case above does not appear on the last day of PY).

**C. Average of “Total assets less Assets funded by specific borrowing”**  
appearing in BS on first & last day of PY.

(\*) For this para, QA = Asset that necessarily requires > 12 M for its acquisition, construction or production.

<b>Borrowing Cost</b>					
<b>Balance Sheet</b>				(Rs. In Lakhs)	
<b>Liabilities</b>			<b>Amount</b>	<b>Interest</b>	
Equity & Reserve			1,000	-	
10% Debt on Plant & Machinery			500	50	
12% Debentures General 1			200	24	} 63
13% Loan General 2			300	39	
<b>Total</b>			<b>2,000</b>	<b>113</b>	
<b>Assets</b>			<b>Amount</b>		
Plant & Machinery	Being Used	400	600	1.40	
	CWIP - QA	200			
Land & Building	Being Used	500	800	12.60	
	CWIP - QA	300			
Inventory			400		
Investment			100		
Loans & Advances			100		
<b>Total</b>			<b>2,000</b>	<b>14.00</b>	
63 x	500 - 167	=	333.33	14.00	
	2000 - 500		1500		

		(Rs. In Lakhs)			
Particulars		Specific	General	QA	
P & M	Used	333	67		2.80
	WIP	167	33		1.40
L & B	Used	-	500		21.00
	WIP	-	300		12.60
		500	900	1,400	37.80
Inventory		-	400		16.80
Investment		-	100		4.20
Loans & Advances		-	100		4.20
		500	1,500		63.00
Interest		50	63		
63 x	1400 - 500	=	900	37.80	
	2000 - 500		1500		

14.00

**FAQ 22- Capitalization of general borrowing cost under ICDS-IX shall be done on asset-by-asset basis.**

## ICDS - X: Provisions/ Cont Assets & Liabilities

ADD back	(₹)
1. Disallowance of <b>Provision for loss on Onerous Contracts.</b>	
2. Disallowance of Provision in P&L due to its existence considered as <b>Probable</b> as per AS-29 Vs. <b>Reasonable certainty as per ICDS</b> Ex: Provision for warranty at higher than the past trend done out of extra caution / prudence.	
3. Effect of recognizing <u>contingent asset</u> to <u>asset &amp; related income</u> due to its Inflow of economic benefits being "Reasonably certain" as in ICDS Vs. <b>Virtual certainty as per AS-29</b> <b><u>Reimbursement recognize</u></b> <i>Under ICDS when reasonably certain but under AS when virtually certain.</i>	

**FAQ 24-** Provisioning for employee benefit which are otherwise covered by AS 15 shall continue to be governed by specific provisions of the Act and are not dealt with by ICDS-X.

# **ICDS - DISCLOSURE TEMPLATES**

## General Impact (₹) of ICDS - **All Taxpayers**

### ICDS does not consider:

- **Prudence** as in AS-1
- **Accounting of foreseeable losses** as in AS-7
- **Onerous Contracts** as in AS-29
- **Materiality** as in AS-1

### Accounting profit V Tax profit (ICDS) - General Rule

- AS - Expense unless justified
- ICDS - Capitalize unless justified AS - 1/2/7/9/10/11/12/13/16/29

Accordingly in several situations would –

- Result in earlier recognition of income or
- Later recognition of expenses compared to AS;
- Thereby Advancing of tax cash outflows.
- **May cause DTA or reduce DTL**

## Sector wise impact (₹) of ICDS

1. Non-corporates, not following ANY AS.
2. Non-corporates, paying under AMT. [No impact on MAT but MAT Credit impacted] →
3. Companies following Ind AS. →
4. Assesses with huge distribution expenses, whereby Inventory valuation would be higher.
  - TG of ICAI 10.4: If incurred at distribution depots - Don't consider.
5. Service Transactions where Revenue must be recognized under PCM for > 90 days  
Service Contracts beyond 25% stage and until then to account it as inventory.
6. Contractors / service providers for whom revenue must include **"Retention Money"**.
7. Assesseees with huge balances under **"Non Integral Foreign Operations"**.
8. **All Govt. Grants taxable** – whether capital or revenue or promoter contribution except for FA.
9. Assesseees **trading in securities** wherein Value of Securities held as SIT must be valued @
  1. Cost if it is unlisted / Listed but unquoted securities
  2. Cost or NRV WIL (Category wise) for listed securities
10. **Real Estate Transactions** (with introduction of Draft ICDS)
11. **For ALL CAs (!!) - Tax Auditor is watchman for ICDS Compliance – Disclosure only in TAR and not in ITR !!**
  - Inform changes in law to the client – Don't keep the fear to yourself.
  - Charge FEE commensurate to Cost, Risk & Time spent – Incl. for attending this seminar.



## ICDS – Impact (₹) on MAT & AMT [FAQ-6]

- Since MAT computation is based on profit as per Schedule III to Cos. Act, **ICDS provisions Shall not apply to MAT.**
  - *Early recognition of income or late recognition of exp. compared to AS – will impact Cos. Paying “MAT” in later years, as they are already taxed in an earlier year.*
  - *May impact construction business, esp. if separate SPV is created for a new project.*
- AMT U/s 115JC is computed on “Adjusted TI” derived by making specified adjustments (incl. ICDS) to TI computed as per regular provisions of the Act.
  - **Hence, ICDS provisions shall apply for AMT.**

Alternate Minimum Tax (AMT) on **Adjusted Total Income (ATI)**

Applicable for all assesses (other than companies) incl. LLPs ' if IT < 18.5% of ATI

**ATI = Total Income + Deductions claimed**  
**under Part C of chapter VI A (U/s 80HH to 80RRB Except S. 80P)**  
**+**  
**u/s 10AA (profits of SEZ units) + U/s.35AD s.t S.32 adj**  
**+**  
**ICDS adjustments**

C/ f Period of MAT credit – 10 years

## Conceptual changes - AS Vs. Ind AS

1. **Greater Transparency through disclosures.**
  - Comparatives truly comparative – Prior period adj. in 3<sup>rd</sup> BS.
2. **More judgmental elements involved.**
3. **More use of Fair Valuation.** *[current over historic value]*
  - Permits recognition of intangible assets at Fair Value
4. **Substance over form.** *[Accuracy over legal form]*
  - Effective Interest Method for revenue recognition and other deferred settlements using **discounting**.
  - Amortising upfront fee on term loans over the loan term.
  - Higher provisioning in Banks under Expected Credit Loss – ECL based on probability of default - PD instead of historical 90 days actual default experience. ECL gives weightage to macro economic factors also.
  - CFS as a rule *[CFS based on effective control (based on SH agreement, etc.) instead of >50% SH]*
  - Split Convertible Debn. as Equity & Redeemable pref. shares as Debt
  - Perpetual & Interest free debt classified as equity
5. **Discounting of provisions permitted.**
6. **Extraordinary & exceptional item.**
7. **Disclosure of Contingent Asset in B/S permitted.**
8. **OCI & Statement of Changes in Equity**

### Deferred Settlement

Separate Interest element	Yes	No
PPE	AS-10 & Ind AS	ICDS
Inventory / Purchase / Revenue	Ind AS	ICDS & AS 2/9

# Objections & Suggestions on ICDS

Income “*CONFUSION*” & “*DISTORTION*” Standards

- ❑ Absolutely no need to notify different set of ICDS for computing TI.
  - Taxpayers may be permitted to compute TI as per relevant AS applicable to them.
  - Different set of standards leading to Fatigue.**
- ❑ AS already in harmony with Act – Computing TI starts with accounting profit.
  - Deviations from AS is due to specific allowances & disallowances provided in Act.
  - So amend Act and not AS – if harmony is to be achieved.**
- ❑ Executive encroaching on powers of legislature – **Delegated Legislation.**
  - Changes by mere notification - without amendment in Act.
  - ICDS utilized to overcome judgments against revenue without recourse to amendments in law.
- ❑ ICDS gives rise to enormous litigation - **ICDS Vs. settled judicial precedents ?**
- ❑ Introduce ICDS in **phased manner** Or SME's could altogether be exempt .
- ❑ **Disclosure** requirements to be deleted from ICDS.
- ❑ Need for additional computations & reconciliations b/w 2 standards - Could result in need for **maintaining additional records** esp. for large & multi-location cos.

**Scrap ICDS - Bring all computational requirements in IT Act (code) itself.**



Wishing you Substance & form.

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