AS 22
ACCOUNTING FOR TAXES ON INCOME-

August 11,2009

Overview

- Objectives, Scope and Definitions
- Recognition and Measurement
- Conditions for recognition of Deferred Tax Assets
- Presentation
- Disclosure
- Transitional Provisons

Objectives, Scope & Definitions

OBJECTIVE

- Prescribe Accounting Treatment for Taxes on Income
  - Taxes on income are to be matched with the revenues and expenses to which they relate

Why AS-22 ?

Case Study			Computer Pur. value			Depreciation Rate				Tax Rate		
			(Rs. In Crores)			Co's Act		IT Act				
			50.00			0.16		0.60		0.30		
As as 31st March		**1.00**	**2.00**	**3.00**	**4.00**	**5.00**	**6.00**	**7.00**	**8.00**	**9.00**	**10.00**	
PBT - AI		100.00	100.00	100.00	100.00	100.00	100.00	100.00	100.00	100.00	100.00	1000.00
Add: Depreciation - A/c's		8.11	8.11	8.11	8.11	8.11	9.47					50.00
Less: Depreciation - IT		30.00	12.00	4.80	1.92	0.77	0.31	0.12	0.05	0.02	0.01	50.00
Total Income - TI		78.11	96.11	103.31	106.19	107.34	109.16	99.88	99.95	99.98	99.99	1000.00
CT -30% of IT		23.43	28.83	30.99	31.86	32.20	32.75	29.96	29.99	29.99	30.00	300.00
PAT		76.57	71.17	69.01	68.14	67.80	67.25	70.04	70.01	70.01	70.00	700.00

Scope

- Applied to accounting for all taxes on income (including domestic and foreign taxes and possibly taxes such as FBT)
- Accounting for taxes includes
  - Determination of the amount of expense or saving
  - Disclosure
- Excludes taxes on distributions including Dividend Distribution Tax

Definitions

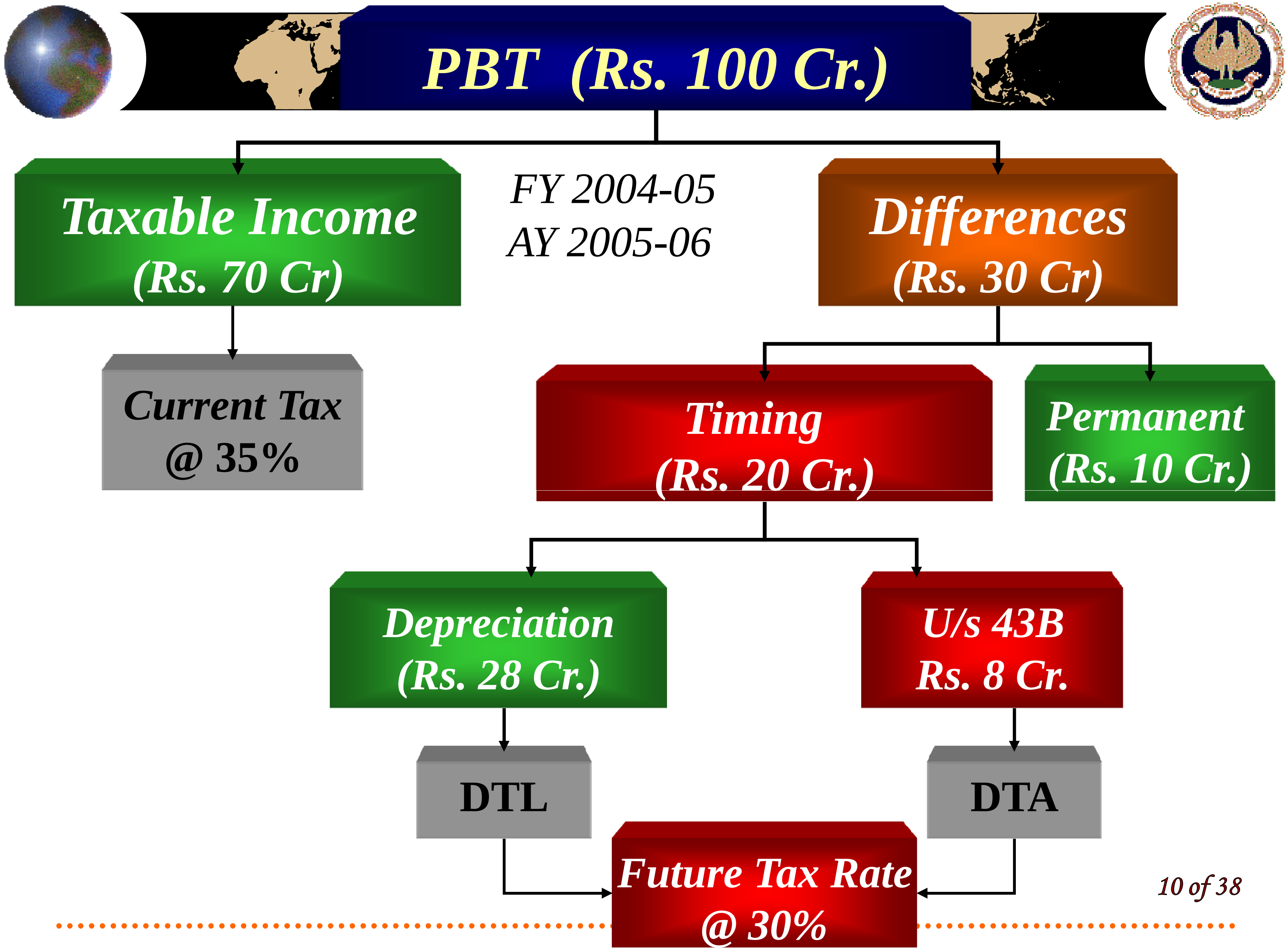
- AI: accounting Income is the Net Profit or Loss before tax (expense or savings)
- TI: Taxable Income is the taxable income as computed under the tax laws on which the tax has to be paid.
- TE/TS: Tax Expense/ Tax Savings= Current Tax + Deferred Tax

Definitions

- CT: Current Tax is the amount of tax payable (or recoverable) on the taxable income (or loss) for the period.
- DT: Deferred Tax is the tax effect of the timing differences

Timing differences -TD- Differences between TI and AI for a period that originate in one period and are **capable of reversal** in one or more subsequent periods.

Permanent differences -PD- are the differences between TI and AI for a period that originate in one period and **do not** reverse subsequently.


PBT (Rs. 100 Cr.)
FY 2004-05
AY 2005-06
Taxable Income
(Rs. 70 Cr)
Current Tax
@ 35%
Differences
(Rs. 30 Cr)
Timing
(Rs. 20 Cr.)
Permanent
(Rs. 10 Cr.)
Depreciation
(Rs. 28 Cr.)
U/s 43B
Rs. 8 Cr.
DTL
DTA
Future Tax Rate
@ 30%

Timing Difference – Ex..

- **Difference in net block of fixed assets between tax and accounts -**
  - **Difference in Depreciation due to**
    - **Different rates / methods**
    - **Pro rata treatment Vs. 180 days (in I year)**
    - **Exchange fluctuation of FC liability incurred for FA purchase. - As-11(R) Vs. Sch.VI Vs. S. 43A**
    - **Up to Rs. 5000 assets write off under Companies Act**
  - **Impairment Loss as per AS-28**
  - **Sale Proceeds Cr. to Block of Asset as per IT Act Vs. Profit / Loss on sale of FA's recognised in P&L A/c**
  - **Purchase of Scientific Research Assets [35(2)]**

Timing Difference – Ex..

- **Expenses Dr. to P & L A/c on accrual basis but allowed on actual payment.**
  - **Payments made without TDS, but disallowed for tax purposes u/s 40(a)(i) / (ia) and allowed when relevant tax is deducted & paid subsequently**
  - **Expenditure U/s 43B of Income Tax Act**
  - **Provision for Gratuity u/s 40A(7)**
  - **Provisions made in the P&L A/c in anticipation of liabilities – allowed when liabilities <u>crystallize</u>**

Timing Difference – Ex..

- Provision for doubtful debts / advance
- Provision for warranties
- Preliminary expenses written off fully when incurred (U/s 35D)
- Expenses amortized in books of Accounts over a period of years but a shorter or longer period is allowable for tax purposes
- Permanent Diminution in the Value of Investments (AS 13)

Permanent Difference – Ex...

- **Amortization of goodwill considered as disallowable expense**
- **Personal expenditure disallowed by tax authorities**
- **Penalty (Not being compensatory)**
- **Payments disallowed U/s 40(A)(3)**
- **Donations to the extent not allowed**
- **Remuneration to partners disallowed U/s 40(b)**
- **Scientific research expenditure.*(only weighted element)***
- **Exemptions u/s 10/10A/10B**
- **Deductions U/s 80IA / IB / IC**
- **Financial Lease – (Circular No. 2 dtd. 9th Feb 2001 – post AS 19 tax position)**
- **Additional Depreciation on Revaluation**

Recognition & Measurement

Computation of DT

STI
AI
+/- **PD**
+/- **TD**
TI

CT = IT on TI → (Applicable tax rates/laws)
DT = IT on (+\- TD)→ (Latest known tax rates/laws)
TE = CT +DT if a debit (otherwise it is a TS)

Case Study-1	Computer Pur. value (Rs. In Crores)	Depreciation Rate Co's Act	Depreciation Rate IT Act	Tax Rate
	50	40%	60%	30%

As as 31st March	1	2	3	4	5	6	7	8	9	10	
PBT - AI	100	100	100	100	100	100	100	100	100	100	1000
Add: Depreciation - A/c's	20	12	7	4	3	2	1	1	0	0	50
Less: Depreciation - IT	30	12	5	2	1	0	0	0	0	0	50
Total Income - TI	90	100	102	102	102	101	101	101	100	100	1000
TD-being Depn differential	-10	0	2	2	2	1	1	1	0	0	0
CT -30% of IT	27	30	31	31	31	30	30	30	30	30	300
DT-30% of TD	-3	0	1	1	1	0	0	0	0	0	0
Tax Exp.(CT-DT)	30	30	30	30	30	30	30	30	30	30	300
TE=IT on (AI+/-PD)	30	30	30	30	30	30	30	30	30	30	300

Case Study -2		(Rs. In Crores)			Co's Act		IT Act				
		50			40%		60%		30%		
As as 31st March	1	2	3	4	5	6	7	8	9	10	
PBT - AI	100	100	-50	100	100	100	100	100	100	100	850
Add: Depreciation - A/c's	20	12	7	4	3	2	1	1	0	0	50
43B disallowance	5	0	7	0	0	0	9	0	0	0	21
40A(3) disallowance	10	11	12	13	14	15	16	17	18	19	145
Less: Depreciation - IT	30	12	5	2	1	0	0	0	0	0	50
43B disallowance	0	5	0	0	7	0	0	0	9	0	21
CF LOSS				29							
Sec.10 exemption	20	20		20	20	20	20	20	20	20	180
Total Income - TI	85	86	-29	66	89	96	106	98	89	99	815
TD	-5	-5	9	2	-5	1	10	1	-9	0	0
CT -IT on TI	26	26		20	27	29	32	29	27	30	244
DT-30% of TD	-2	-2	3	1	-2	0	3	0	-3	0	0
DT-30% of CF LOSS			9	-9							
Tax Exp./(Saving)(CT-DT	27	27	-11	28	28	29	29	29	29	30	245

Case Study #3

Fixed Assets & Depreciation

	Co. Act	I T Act
Opening WDV -1/4/2004	1000	600
Additions during the year	400	400
	1400	1000
Depreciation for the year	200	300
Closing WDV - 31.3.2005	**1200**	**700**

Accounting Income for the FY 2004-05	5000
Deferred Tax Liability as at 01.04.2004	140
Tax Rate for FY 2003-04 (Excluding Surcharge & Cess)	35%
Tax Rate for FY 2004-05 (Excluding Surcharge & Cess)	30%

	Co. Act	I T Act	Diff.
Opening WDV -1/4/2004	1000	600	400
Additions during the year	400	400	
	1400	1000	
Depreciation for the year	200	300	(100)
Closing WDV -31.3.2005	**1200**	**700**	**500**

Deferred Tax Liability	***35%***		***30%***
	31.3.2004	**2004-05**	**31.3.2005**
Deferral Method (Timing Difference)	140	*30* **(100*30%)**	170
Liability Method (Temporary Difference)	140	*10*	150 **(500*30%)**
		20	20

Reconciliaition **400 x (35% - 30%)**

400 x (5) = 20

Measurement in Special Cases

- Entity paying tax u/s 115 JB:
  - Payment of tax u/s 115 JB is a current tax for the period.
  - Deferred tax Assets and Liabilities are measured using the regular tax rates and not the rates u/s 115 JB.
  - (AS-22 under CSR,2006 is silent on treatment of MAT Credit. ***ASI 6:*** **Accounting for Taxes on Income in the context of *S. 115JB* of the Income-tax Act, 1961 requires that** MAT Credit should be shown under the heading "Loans and Advances" with **"MAT Credit Entitlement"** subject to convincing evidence *(GN on Accounting for MAT Credit)*)

Measurement in Special Cases

- Defered Taxes in situation of *Tax Holiday U/S 10A and 10B / 80 IA etc* of the Income-tax Act,1961
  - Deferred tax is not recognised to the extent the timing differences reverse during the holiday period.
  - Deferred tax which reverse after the holiday period are recognised in the year in which the timing differences originate
  - For the above purposes the timing differences which originate first are expected to reverse first.
  - Recognition of DTA is subject to consideration of prudence.

Case S… No. 4

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Year	Depreciation		TD		CT	Deferred	Accumulated	Tax		
	Books	IT			@ 30%	Tax	DTL/DTA	Expense		
(a)	(b)	(c)	(d)=(c-b)		(e)	f)=(d*30%	(g)	(h)=(e+f)		
1	100	375	275	(O)	0	14	14	14		
2	100	281	181	(O)	0	54	68	54		
3	100	211	111	(O)	0	33	102	33		
4	100	158	58	(O)	0	17	119	17		
5	100	119	19	(O)	0	6	125	6		
6	100	89	(11)	(R)	0	0	125	0	-3	
7	100	67	(33)	(R)	0	0	125	0	-10	
8	100	50	(50)	(R)	0	0	125	0	-15	
9	100	38	(62)	(R)	0	0	125	0	-19	
10	100	28	(72)	(R)	0	0	125	0	-22	-69
11	100	21	(79)	(R)	294	(24)	101	270		
12	100	16	(84)	(R)	295	(25)	76	270		
13	100	12	(88)	(R)	296	(26)	49	270		
14	100	9	(91)	(R)	297	(27)	22	270		
15	100	7	(93)	(R)	298	(28)	(6)	270		
	1500	1480								

Note: Deferred Tax, for the first year, is calculated after considering the reversal within 10 years.

I.e	275	(229)	46	@ 30% =	14	
		-69				

Conditions for recognition of Deferred Tax Asset

Recognition of Deferred Tax Asset

Consideration of PRUDENCE is a must while recognizing DTA

DTA Arising due to	Basis of Recognition
Unabsorbed Business & Depreciation Loss	Virtual Certainty (Judgment) & Convincing Evidence (Fact)
Other than above	Reasonable Certainty

Re-Assessment v/s Review

Re-Assessment (Right)

Relates to DTA *Previously unrecognized*

Review (Duty)

Relates to DTA *Previously recognized*

- ***Not a prior period item as per AS-5 unless it was a mistake***
- **AS 22 does not mention review or re-assessment of DTL**

CASE STUDY 5		(Rs. In Crores)			Co's Act		IT Act				
		50			40%		60%		30%		
As as 31st March	1	2	3	4	5	6	7	8	9	10	
PBT - AI	-100	-75	-50		10	30	50		100	100	65
Add: Depreciation - A/c's	20	12	7	4	3	2	1	1	0	0	50
43B disallowance	5	10	20		0	0	9	0	0	0	44
40A(3) disallowance	10	11	12	13	14	15	16	17	18	19	145
Less: Depreciation - IT	30	12	5	2	1	0	0	0	0	0	50
43B disallowance	0	0	0	15	20	0	0	0	9	0	44
CF LOSS					6	46	76	18	29		
Sec.10 exemption							0	0	0	0	0
Total Income - TI	-95	-54	-16	0	0	0	0	0	80	119	210
TD	-5	10	22	-13	-18	1	10	1	-9	0	0
CT -IT on TI				0	0	0	0	0	24	36	60
DT-30% of TD	-2	3	7	-4	-5	0	3	0	-3	0	0
DT-30% of CF LOSS						37	-23	-5	-9		
Tax Exp./(Saving)(CT-DT	2	-3	-7	4	5	-37	20	5	35	36	60

Losses under the head Capital Gains

- DTA recognised subject to the condition of virtual certainty.
- Amount carried forward is based on the amount which can be carried forward and set off (including effect of indexation in the case of Long Term Capital Loss)

Case Study #6 Recognition of DTA

	(DTL)	DTA				<u>NET</u>
Situation	**Depreciation or <u>otherwise</u>**	**C/f Loss**	**C/f Depn.**	**Depn**	**43B exps.**	
		Virtual Certainty		*Reasonable Certainty*		
A	*(200)*	**Nil**	**170**	**Nil**	**Nil**	*(30)*
B	*(200)*	**Nil**	**250**	**Nil**	**Nil**	**0 / 50**
C	*(200)*	**Nil**	**60**	**Nil**	**170**	**0/ 30**
D	*(200)*	**240**	**40**	**Nil**	**60**	*(100)* / **140**
E	*(200)*	**140**	**30**	**Nil**	**20**	*(150)* / <u>*(10)*</u>
F	Nil	**Nil**	<u>**Nil**</u>	<u>**80**</u>	<u>**10**</u>	**Nil/90**
G	*(200)*	**300**	**Nil**	**Nil**	**Nil**	*(200)/100*

Presentation & Disclosure

Presentation of CT - Para 27

An Enterprise should offset assets and liabilities representing current tax if the enterprise:

a) has a legally enforceable right to set off the recognized amounts; and

b) intends to settle the asset and the liability on a net basis

Presentation of DT - Para 28

- **DTA and DTL to be set off if**
  - **permissible to set off assets against liabilities in respect of current tax**
  - **And the DTA and DTL relate to taxes on income governed by the same tax laws.**
- **Presentation of net DTL & DTA on the face of the Balance Sheet:**
  - **Net DTL to be disclosed after Unsecured Loans**
  - **Net DTA to be disclosed after Investments**

Disclosure

- **Break-up of major components of DTA / DTL to be disclosed.**

- **The nature of the Evidence supporting the recognition of DTA to be disclosed, if an enterprise has Unabsorbed Depreciation / Tax Losses to be carried forward.**

Transitional Provisions

- **Effect on transition:**
  - **Corporate - Revenue Reserve**
  - **Non Corporate – Capital account**

Summing Up

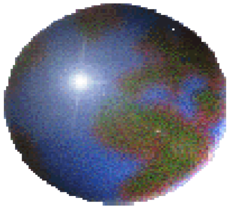
- Tax expense for a period comprising CT +DT should be considered while determining the net profit or loss for the period.
- Deferred tax should be recognised for all timing difference subject to the considerations of Prudence as set out in paragraphs 15-18
- In case of carry forward of unabsorbed depreciation or loss DTA should be recognised only if there is virtual certainty supported by convincing evidence that sufficient future taxable income will be available to absorb the loss.

Summing Up

- In the case of other DTA reasonable certainty of availability of future taxable income to realise the asset will suffice.
- Current tax should be measured at the amount expected to be paid to the tax authorities
- Deferred tax assets and liabilities should be measured using the tax rates enacted or substantively enacted as on the balance sheet date.

Summing Up

- At every Balance Sheet date DTA to the extent not recognised should be reassessed and DTA recognised should be reviewed.
- Net Deferred Tax Assets and Liabilities are presented separately from CTA and CTL and on the face of the Balance sheet.
- Disclosures should give the break up of the major components of net DTA and DTL and the evidence supporting recognition of DTA in case of unabsorbed depreciation and Carry forward loss.



Questions?