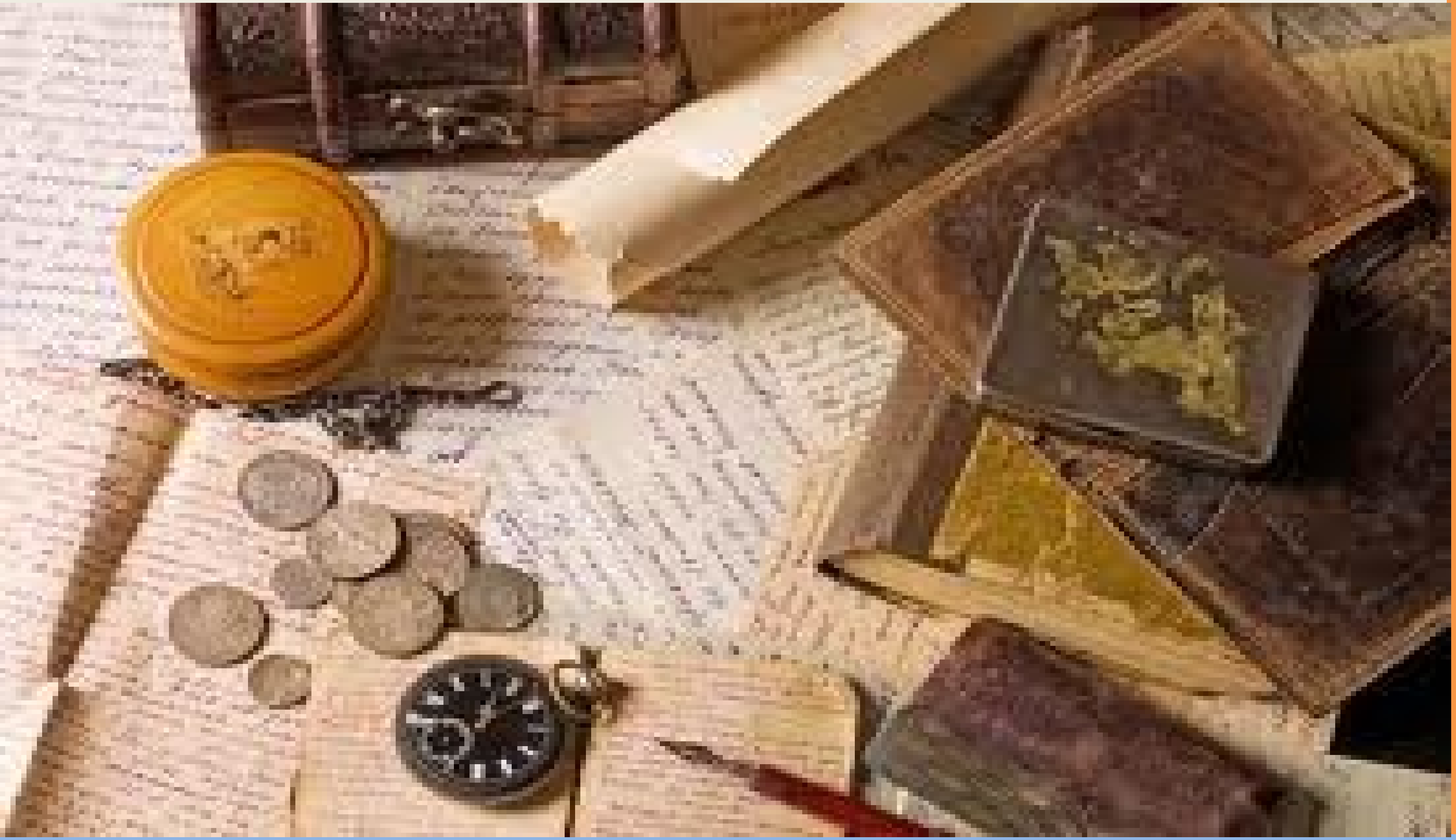
Tax Accounting Standards (TAS)

CA Kusai Goawala Feb 2013

History and Background



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History and Background

- Finance Act 1995 empowered Central Government to notify Accounting Standards.
- Standards to apply only to the following heads of income :
  - Profits and Gains from Business and Profession
  - Income from other sources

History and Background

- In 1996, two Accounting Standards notified u/s 145(2) of the Income tax Act (Act) :
  - Disclosure of accounting policies and
  - Disclosure of prior period and extraordinary items and changes in accounting policies
- A high level committee was set up in December 2010.

Why TAS?

Why TAS?

- Reasons for a need to introduce TAS :
  - There is flexibility in the standards issued by the ICAI)
  - This leads to avoidance of the payment of correct taxes by following a particular system.
  - There is an urgent need to standardize one or more of the alternatives in various standards
  - That income for tax purpose can be computed precisely and objectively

Committee Recommendation

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Committee Recommendation

- The Committee recommended as under :
  - 14 Accounting Standards modified and were called Tax Accounting Standards
  - Remaining 17 standards do not have any impact on income or expenditure and hence not considered.
  - 4 New TAS to be introduced.

Committee Recommendation

- No separate books of account required to be maintained
- Adjustments for deviation between AS and TAS to be made in the Computation of Income.
- Tax Auditor will have to report in 3CA and 3CD about compliance of TAS
- Income tax Act will prevail over Tax Standards.
- All entities are covered

Principles followed

Principles followed

- Objectives
  - Reduction of litigation
  - Minimization of alternatives
  - Giving ‘certainty to issues’.

Tax Accounting Standards

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Tax Accounting Standards

- The question is :

  Are they really

  Tax Accounting Standards

  Or

  Tax Computing Standards

  – Section 145(2) authorises Accounting Standards not just computing standards.

Tax Accounting Standards

- The date of implementation will be announced
- Impact of IFRS implementation on MAT provisions will be considered as and when implemented
- Disclosures required under TAS.

    To disclose where ?

    In the FS or Return ?

Tax Accounting Standards

- Following standards not modified although it may have substantial impact on tax :
  - AS14 Amalgamations :
    - issues relating to deductibility of cost in purchase method.
    - Depreciation on Goodwill
  - AS 15 : Employee Benefits not covered :
    - Keyman Insurance
    - Leave Encashment
    - ESOP accounting and compensation

Tax Accounting Standards

- AS 18 -Related Party not covered –
  - 40A2(b) and AS18 needs to be synchronised

- AS 30/31/32 Financial Instruments –
  - Hedge and Derivatives – Mark to Market losses will not be allowed unless realised – When FI standard will be notified – These will be covered in TAS.

The TAX Standards harmonised based on the existing Accounting Standards

Sr. No.	Disclosure of Accounting Policies	Corresponding to AS
1	Disclosure of Accounting Policies #	(Corresponding to AS-1)
2	Valuation of Inventories#	(Corresponding to AS- 2)
3	Events Occurring After the Previous Year	(Corresponding to AS-4)
4	Prior Period Expense	(Corresponding to AS- 5)

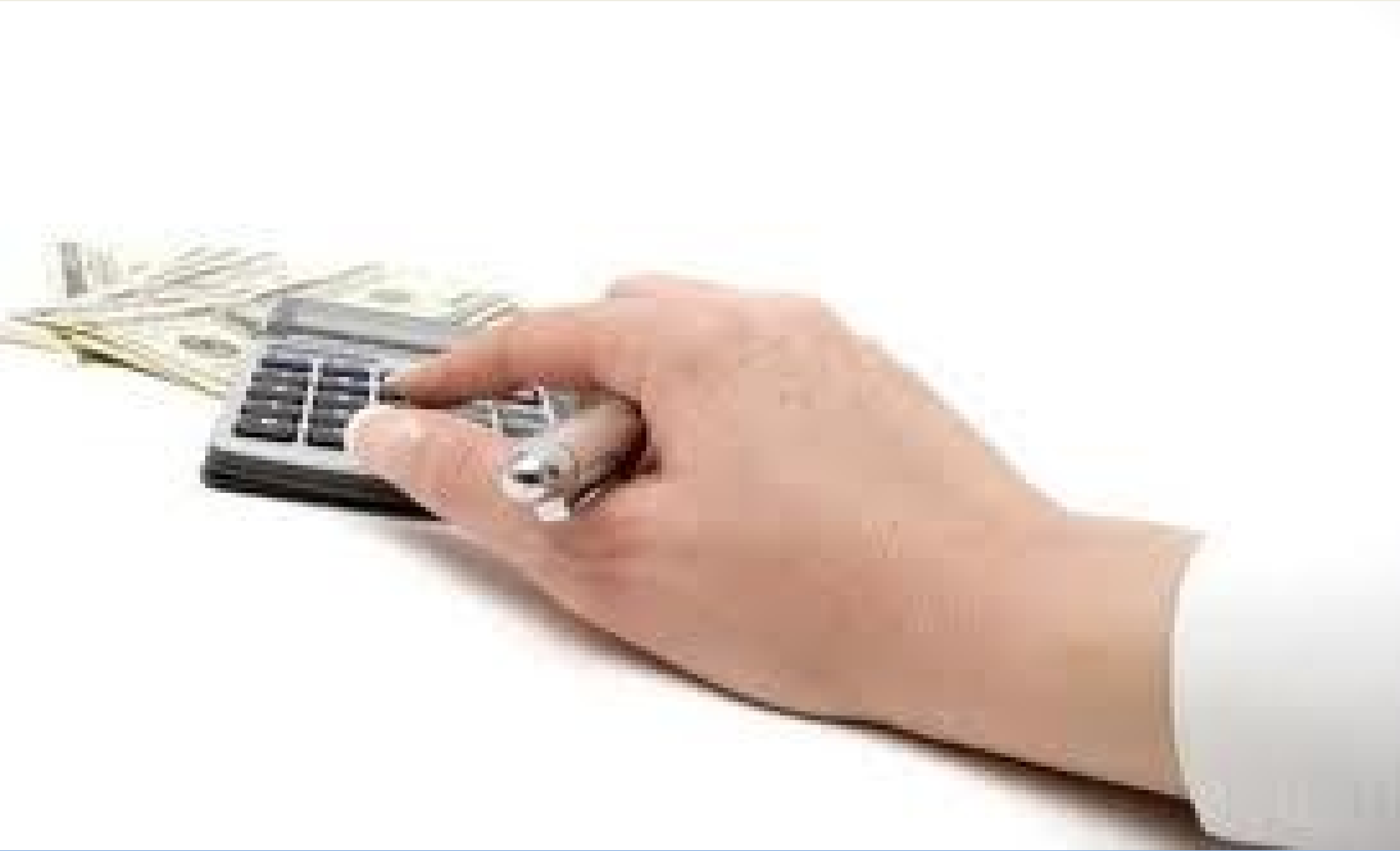
Sr. No.	Disclosure of Accounting Policies	Corresponding to AS
5	Construction Contracts*	(Corresponding to AS- 7)
6	Revenue Recognition#	(Corresponding to AS- 9)
7	Accounting for Tangible Fixed Assets#	(Corresponding to AS- 10)
8	The Effects of Changes in Foreign Exchange Rates	(Corresponding to AS-11)
9	Government Grants*	(Corresponding to AS-12)
10	Securities	(Corresponding to AS-13)
11	Borrowing Costs #	(Corresponding to AS-16)
12	Leases	(Corresponding to AS-19)

Sr. No.	Disclosure of Accounting Policies	Corresponding to AS
13	Intangible Assets*	(Corresponding to AS- 26)
14	Provisions, Contingent Liabilities and Contingent Assets#	(Corresponding to AS- 29)

Tax Accounting Standards

- The following new TAS will be issued :
  - Share based payment
  - Revenue recognition by real estate developers
  - Service concession arrangements (example, Built Operate Transfer agreements)
  - Exploration for and evaluation of mineral resources.

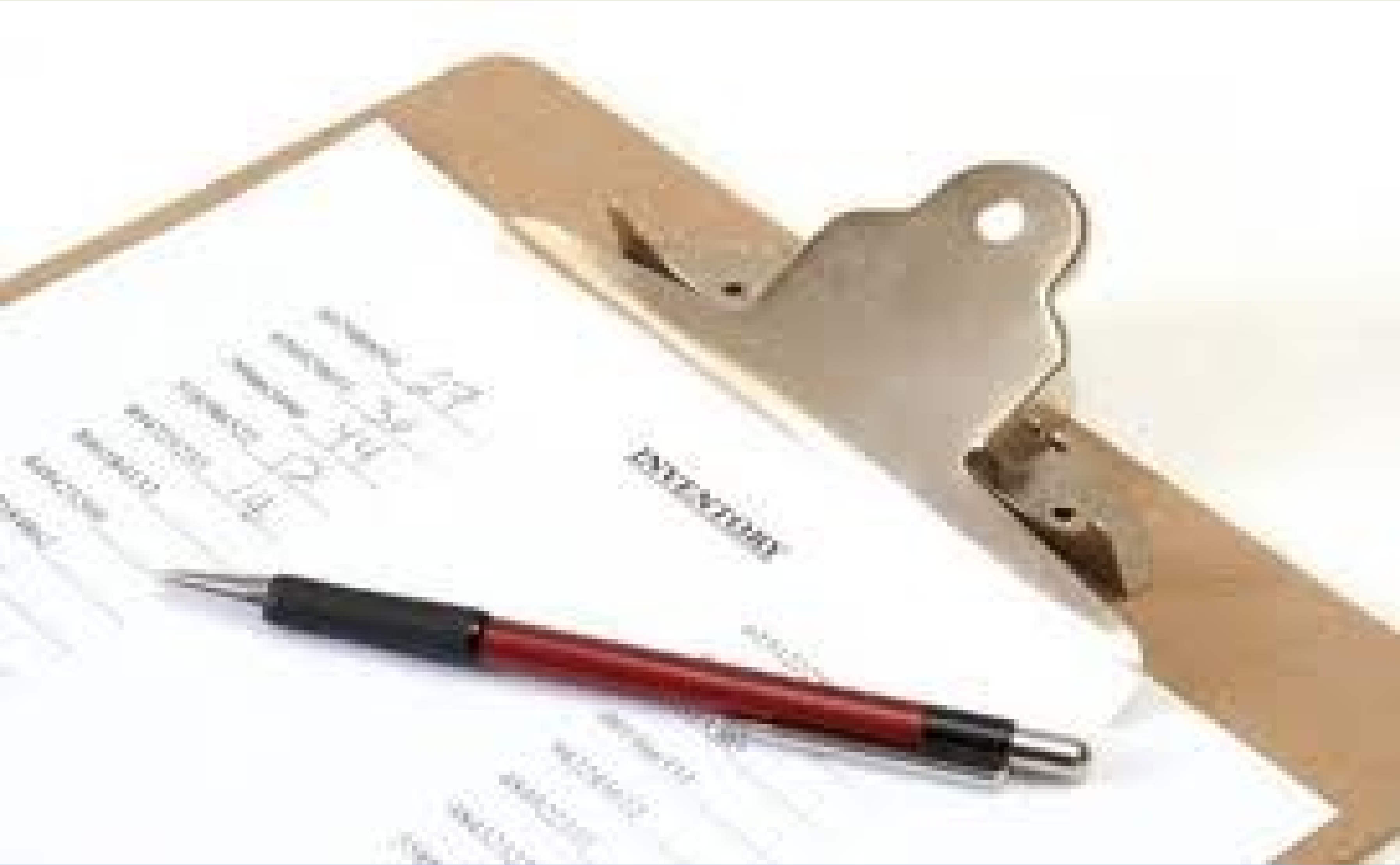
TAS (AS) = AS-1



TAS (AS) = AS-1

- **Tax AS for Accounting Policies**
  - Expected losses or mark-to-market losses shall not be recognized unless permitted by any other Tax AS.
  - Concept of materiality for selection of accounting policies is not to be considered for TAS.
  - Accounting policies shall not be changed without a "reasonable" cause. – What is reasonable cause – not defined.

TAS (VI) = AS-2



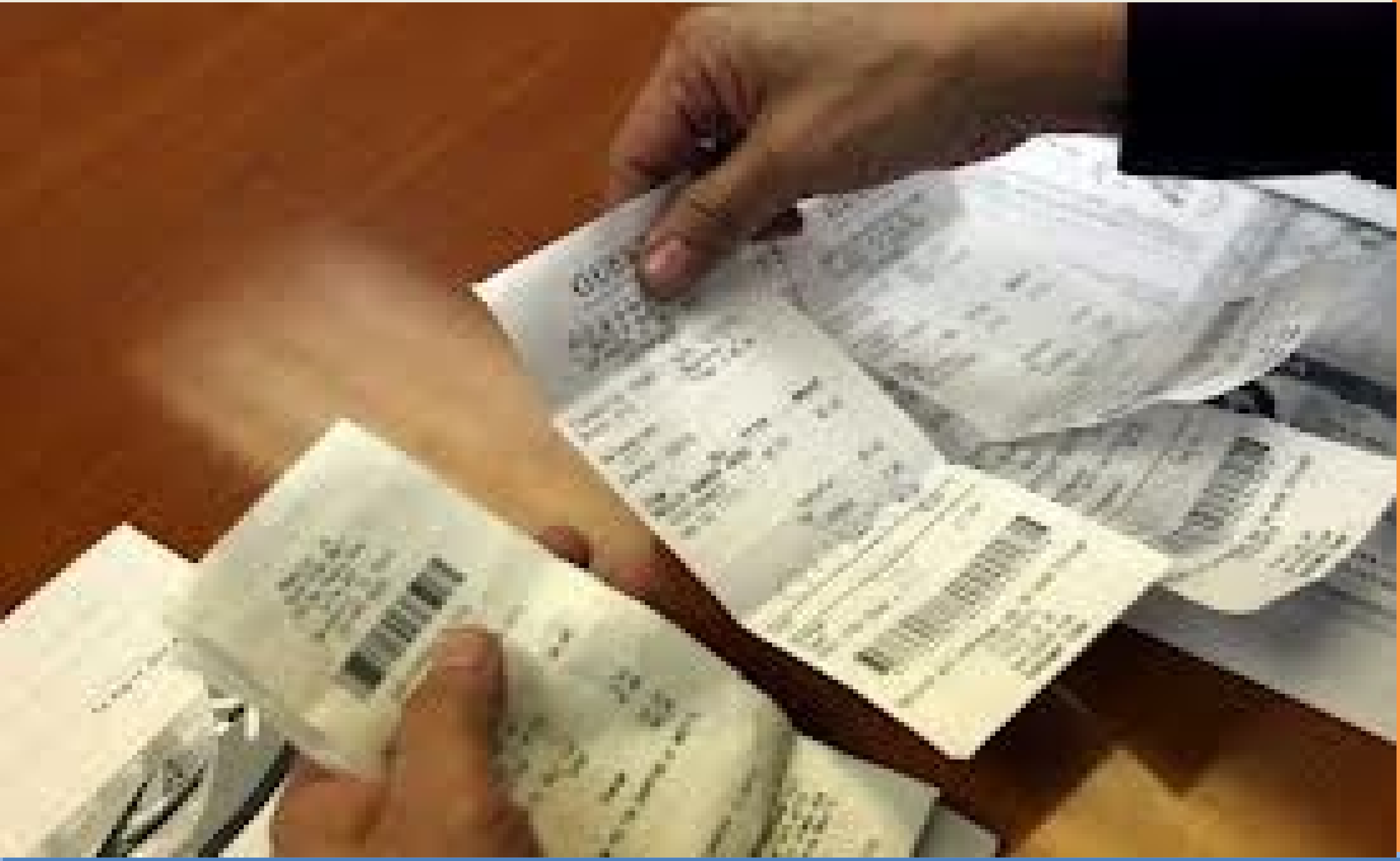
TAS (VI) = AS-2

- **Tax AS for Valuation of Inventories**
  - Inventory for Services.
  - Cost of inventory of such services = Labour plus other cost of personnel directly engaged in providing services including supervisory personnel and attributable Overheads.
  - Service Inventory to be valued only at Cost – NRV not to be considered.
  - Conflict with AS9.
  - Use of standard cost method as a technique for measurement of cost is not recommended. Hence to use Retail Method.
  - TAS provides that where it is impracticable to use FIFO or Weighted Average Method, then apply Retail Method – Cost Formula conflicts with Techniques of Measurement.

TAS (VI) = AS-2

– Under AS – Individual item by item comparison for calculating NRV.
– Under TAS – comparison on aggregate basis for NRV.
– The value of inventory of a business as on the beginning of a tax year shall be the same as the value of inventory at the end of the immediately preceding tax year.
– Method of valuation once adopted shall not be changed without a reasonable cause.
– Inventory on the date of dissolution of a Firm, AOP, BOI shall be valued at net realizable value. (Similar provision for a capital asset exists in Section 45(6))

TAS (EA) AS-4



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TAS (EA) AS-4

- **Tax AS for Events occurring after the End of Tax Year**
  - Disclosures relating to events occurring after the end of the tax year do not directly impact the computation of income. Hence, these provisions have been removed in Tax AS.
  - What happens to the adjusting events under AS4 and its impact on taxation.
  - **Disclosure :**
    - (a) Brief disclosure of item of income, expenses, asset or liability recognised on account of events occurring after the balance sheet date.
    - (b) Amount recognised.

TAS (PP) AS-5

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TAS (PP) AS-5

- **Tax AS for Prior Period Expense**

  – The ITL does not distinguish extraordinary items from ordinary items. Hence, provisions relating to separate disclosure of extraordinary items are not included in Tax AS.
  – Prior Period Expense shall not be considered as an allowable deduction in the tax year in which it is recorded unless the taxpayer proves that such expense accrued during the said tax year.
  – If it had accrued during that year – it would not have been classified as Prior Period Expenses in first place.
  – **Disclosures :**
    - Prior Period Expenses, whether considered allowable deduction or not, shall be disclosed with reference to its nature and amount seperately.

TAS (CC) AS-7

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TAS (CC) AS-7

- **Tax AS on Construction Contracts**
  - Retention money shall be recognized for computing revenue based on percentage of completion method.
  - Reversal of revenue already recognized as income on account of uncertainty arising on realizability of contract revenue, the sum shall be written off in the books of account in line with the provisions of the ITL relating to bad debts.

TAS (CC) AS-7

– Pre-construction income in the nature of interest, dividend and capital gains shall not be reduced from the cost of construction but shall be taxed as income in accordance with the applicable provisions of the ITL.

– Contract costs relating to future activity shall be recognized as an asset and if such costs are not realizable then the same may be allowed under the provisions of the ITL.

– Option in AS for recognising cost as revenue if revenue and cost cannot be reliably estimated has been deleted.

TAS (CC) AS-7

- Contract Revenue to be recognized even if it is not possible to reliably measure the outcome of the Contract.
- Losses incurred on a contract shall be allowed only in proportion to the stage of completion.
- Future or anticipated losses shall not be allowed unless such losses are actually incurred.
- Once a contract crosses 25% of the completion stage, the revenue in respect of such contract shall be required to be recognized.

TAS (RR) AS-9

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TAS (RR) AS-9

- **Tax AS for Revenue Recognition**
  - Revenue from service transactions shall be recognised by following only "percentage completion method".
  - The postponement of revenue recognition due to uncertainty in ultimate collection shall be restricted to claims for price escalation and export incentives.
  - In case of non recovery – write off as Bad Debts.

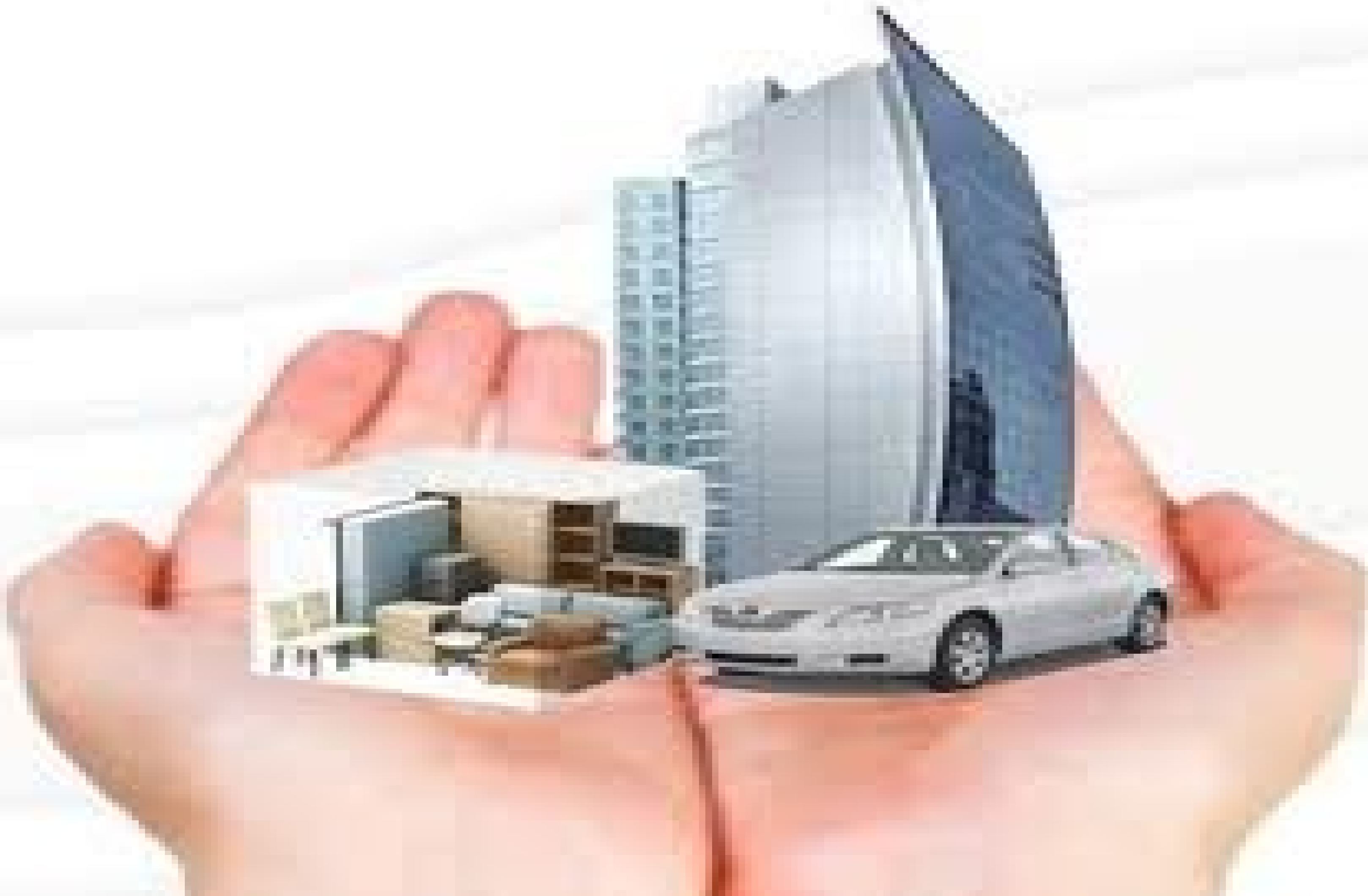
TAS (RR) AS-9

- **Disclosures**
  - (a) In a transaction involving sale of good, total amount of claim raised for escalation of price and export incentives but not recognised as revenue during the previous year along with nature of uncertainty about such claims.
  - (b) the amount of revenue from service transactions recognised as revenue during the previous year ; and
  - (c) the methods used to determine the stage of completion of service transactions in progress.

for service transactions in progress at the end of previous year:

- (i)amount of costs incurred and recognized profits (less recognized losses) upto end of previous year;
- (ii)the amount of advances received; and
- (iii)the amount of retentions.

TAS (FA) = AS-10



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TAS (FA) = AS-10

- **Tax AS for Tangible Fixed Assets**
  - Cost in case of acquisition of an asset in exchange for another asset :
    - lower of the fair value of
      - the asset/securities given up or
      - the asset acquired.
  - Presently, assessee had a choice of any of the above value to be taken as Cost.

TAS (FA) = AS-10

- Revaluation of assets deleted as Income tax Act does not recognize Revaluation.
- Cost to be adjusted with Exchange fluctuations
- The Act contains specific provisions relating to retirement and disposal of tangible fixed assets. Hence, same are not incorporated in Tax AS.
- Tangible Fixed Asset Register to be maintained :
  - Description of the asset
  - Location
  - Actual cost
  - Date on which first put to use

TAS (FA) = AS-10

- **Disclosures**
  - (a) Description of asset/block of assets.
  - (b) Rate of depreciation.
  - (c) Actual cost or written down value, as the case may be.
  - (d) Additions/deductions during the year with dates; in the case of any addition of an asset, date put to use; including adjustments on account of-
    - (i) Modified Value Added Tax credit claimed and allowed under the Central Excise Rules, 1944, in respect of assets acquired on or after 1st March, 1994,
    - (ii) change in rate of exchange of currency, and
    - (iii) subsidy or grant or reimbursement, by whatever name called.
  - (e)Depreciation Allowable.
  - (f) Written down value at the end of year.

TAS (FE) = AS-11

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TAS (FE) = AS-11

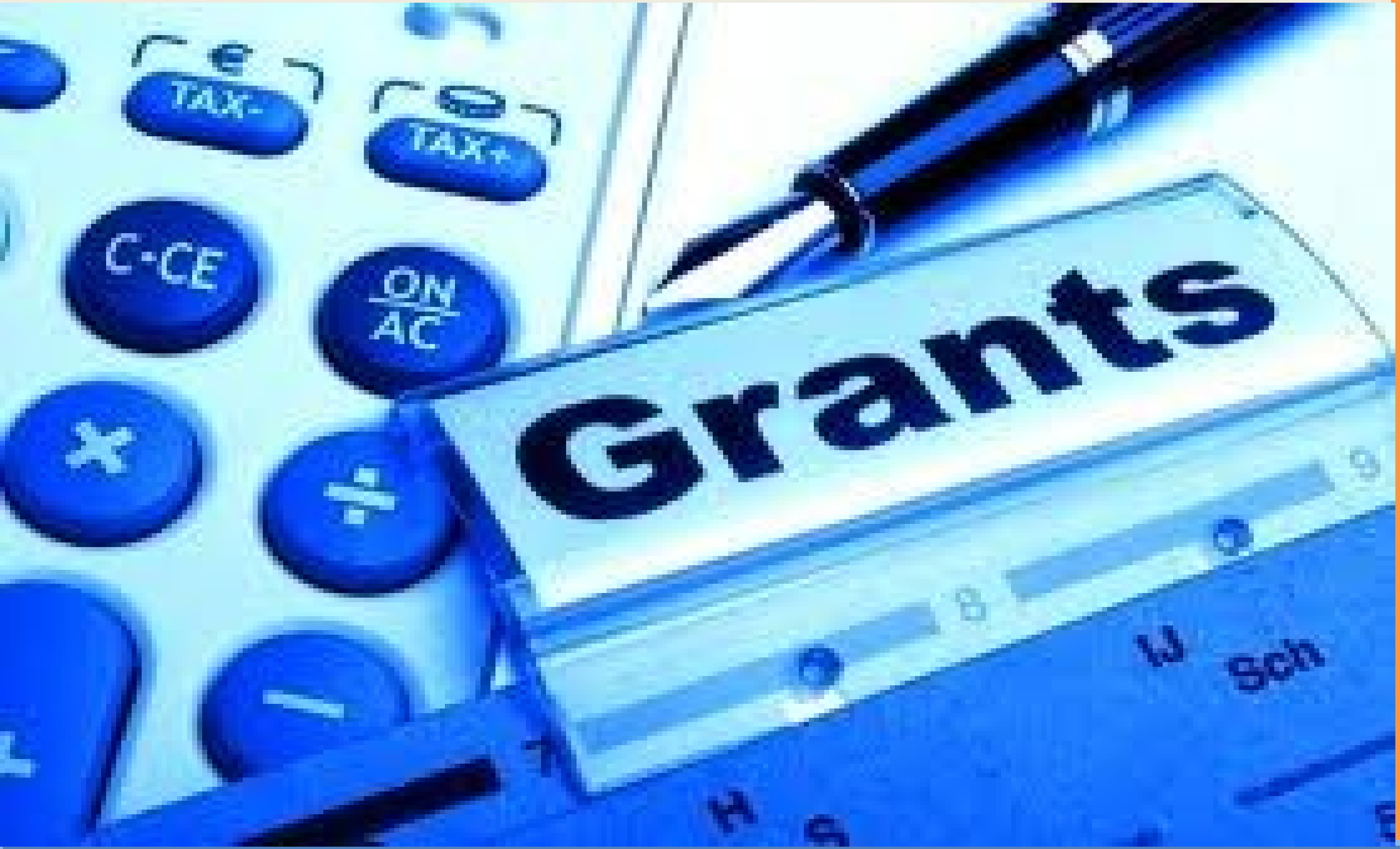
- **Tax AS for Effects of Changes in Foreign Exchange Rates**
  - AS-11 provides that exchanges differences arising on translation of the financial statements of non-integral foreign operations should be accumulated in a foreign currency translation reserve in the balance sheet.
  - Since the Act does not provide for a distinction between integral and non-integral foreign operations, the TAS (FE) provides that such exchange differences shall be taken as Income or Expenditure for the purpose of computation of income.

TAS (FE) = AS-11

- AS-11 provides that forward exchange or similar contracts entered into for trading or speculation purposes should be mark-to-market at each balance sheet date and the resultant exchange differences should be recorded in profit or loss.

- Since such mark-to-market gains or losses are unrealized in nature, the TAS (FE) provides that all gains or losses on such contracts shall be recognized on settlement.

TAS(GG) = AS-12



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TAS(GG) = AS-12

- **Tax AS for Government Grants**
  - Government grants should either be treated as revenue receipt or should be reduced from the cost of fixed assets based on the purpose for which such grant or subsidy is given.
  - Recognition of Government grants shall not be postponed beyond the date of actual receipt.
  - Compliance of conditions should not be a reason for postponement

TAS(GG) = AS-12

- **Disclosures:**
  - Nature and extent of Government grants recognised during the previous year by way of deduction from the actual cost *of the asset or assets or from the written down value of block of assets during the previous year.*
  - Nature and extent of Government grants recognised during the previous year as income.
  - Nature and extent of Government grants not recognised during the previous year by way of deduction from the actual cost *of the asset or assets or from the written down value of block of assets and* reasons thereof.
  - Nature and extent of Government grants not recognised during the previous year as income and reasons thereof.

TAS (SC) = AS-13

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TAS (SC) = AS-13

- **TAX AS FOR SECURITIES**
  - Tax AS only deals with securities held as stock-in-trade.
  - Securities should be valued at lower of cost or net realizable value (NRV). Comparison of cost and NRV shall be done category-wise (and not for each individual security) for which securities shall be classified into the following categories:
    - (a) Shares
    - (b) Debt securities
    - (c) Convertible securities
    - (d) Any other securities not covered above.

TAS (SC) = AS-13

- Unlisted or thinly traded securities shall be valued at cost.
- Cost which cannot be ascertained by specific identification shall be determined on the basis of first-in-first out (FIFO) method.

TAS (BC) = AS-16

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TAS (BC) = AS-16

- **Tax AS for Borrowing Costs**
  - Borrowing cost will not include exchange differences arising from foreign currency borrowings
  - As against the criterion of substantial period of time for classifying an asset as qualifying asset under ICAI AS-16, QA includes all Fixed Assets.
  - Substantial period of time test is applicable only in case of inventories.

TAS (BC) = AS-16

- Specific formula is provided for capitalizing borrowing costs relating to general borrowings.

  A x B/C

  A = BC – Specific BC

  B = Avg cost of QA – QA directly funded

  C = Avg Total Assets – Avg Assets directly funded.

- AS 16 and conflict with Section 36(1)(iii)

- Income on temporary investments of borrowed funds cannot be reduced from borrowing costs eligible for capitalization.

- Condition of suspension of capitalization during interruption of active development is removed in Tax AS.

TAS (BC) = AS-16

- Commencement of Capitalisation :
  - For Specific Borrowings – from the date the funds were borrowed
  - For General Borrowings – from the date the funds were utilised.
- Cessation of Capitalisation :
  - For FA
    - As per AS – when ready for intended use
    - As per TAS – when first put to use.
  - For inventory – as per AS16
- No suspension provision hence continue capitalisation.
- Disclosures :
  - Accounting policy
  - Amount of BC capitalised

TAS (LS) = AS-19

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TAS (LS) = AS-19

- **Tax AS for Leases**
  - For classification of a lease as operating lease or finance lease by both lessor and lessee, a joint confirmation from both required.
  - Where the lessor is a manufacturer/dealer, AS-19 proposes adjustment in the sale price only in the cases of artificially low rate of interest.
  - TAS (LS) provides for adjustment in case of artificially high rate of interest as well.

TAS (LS) = AS-19

- AS-19 provides for adjustment in the recognition of income/expense on account of changes in estimates of the residual value. To provide certainty, the TAS (LS) provides that adjustments in the residual shall be carried out only at the end of the lease term.

- AS-19 contains provisions relating to sale and lease back transactions. As the Act contains specific provisions for treatment of such transactions, the same has been removed in the TAS (LS).

- In case of no joint declaration by lessor and lessee in respect of type of lease, no depreciation will be allowed to the lessee in case of Finance lease and to lessor in case of Operating lease.

TAS (IA) = AS-26

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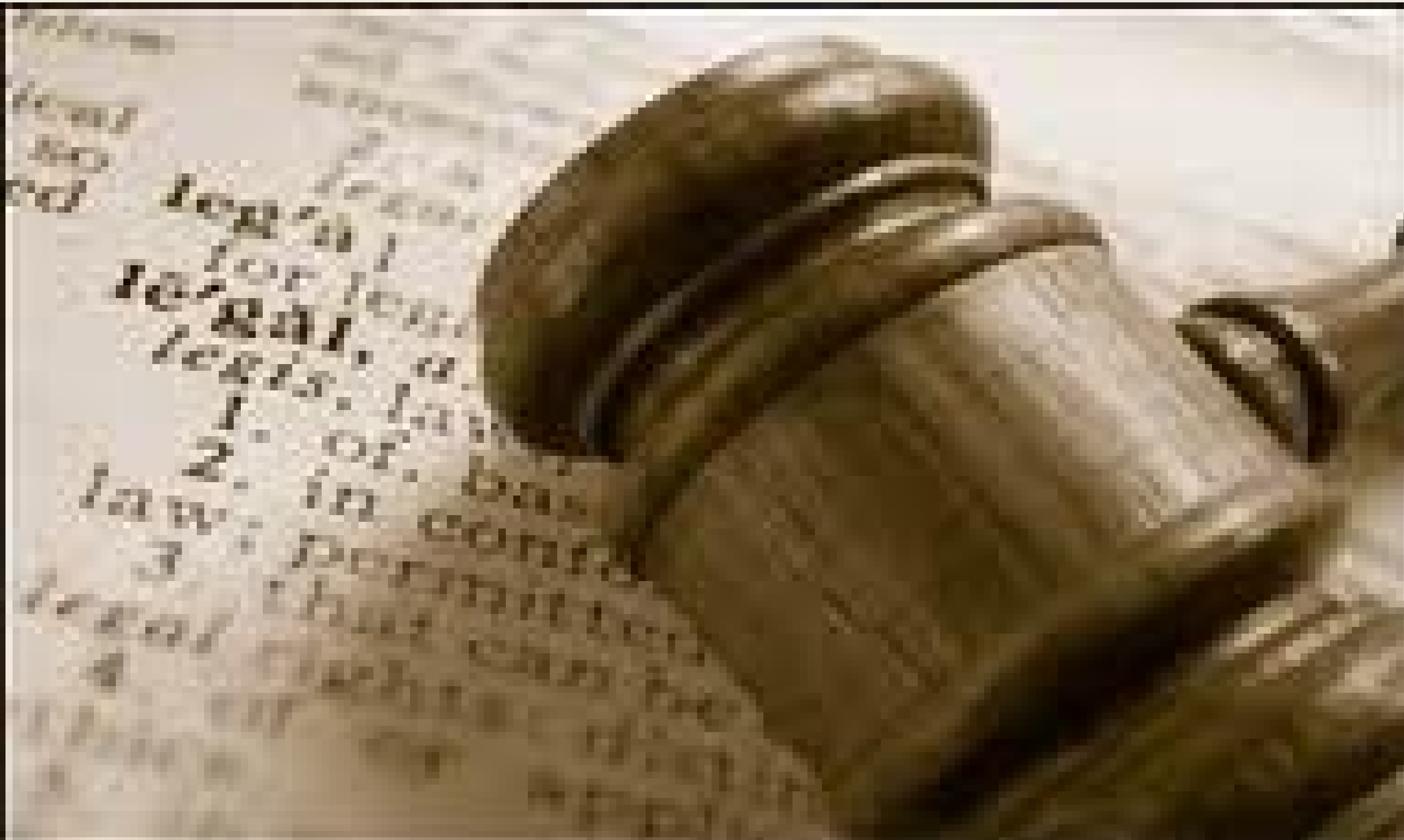
TAS (IA) = AS-26

- **Tax AS on Intangible Assets**
  - Cost in case of acquisition of an asset in exchange for another asset :
    - lower of the fair value of
    - the asset/securities given up or
    - the asset acquired.
  - Presently, assessee had a choice of any of the above value to be taken as Cost.
  - As the ITL contains specific provisions relating to amortization, retirement and disposal of intangible assets (including those acquired on amalgamation), same are not incorporated in Tax AS.

TAS (IA) = AS-26

- Disclosures
  - (a) Description of asset/block of assets
  - (b) Rate of depreciation
  - (c) Actual cost or written down value, as the case maybe
  - (d) Additions/deductions during the year with dates; incase of any addition of an asset, date put to use including adjustments on account of :
    - (i) Modified value added tax credit claimed and allowed under the central exercise rules, 1944, in respect of assets acquired on or after 1 March 1994
    - (ii) Change in rate of exchange of currency, and
    - (iii) Subsidy or grant or reimbursement by whatever name called
  - (e) Depreciation allowable
  - (f) Written down value at the end of year

TAS (PC) = AS-29



TAS (PC) = AS-29

- **Tax AS for Provisions, Contingent Liabilities and Contingent Assets**
  - AS-29 inter-alia stipulates recognition of a provision when it is probable that an outflow of economic resources will be required to settle an obligation.
  - To provide certainty and to align with the principles for recognition of revenue, the TAS (PC) replaces the condition of “probable” with “reasonably certain” for recognising a provision.

TAS (PC) = AS-29

- AS-29 provides for recognition of a contingent asset when the realisation of related income is virtually certain.
- In order to remove the differential treatment between recognition of income and expenses, the TAS (PC) replaces the condition of “virtually certain” with “reasonably certain” for recognition of income and the related asset.
- As there are specific provisions in the Act for restructuring expenses, the provisions of AS-29 relating to restructuring costs is not incorporated in the TAS (PC).

TAS (PC) = AS-29

– No provision to be made for cost that is needed to be incurred to operate in future – example – warranty cost.

– Reimbursements to be recognised only when :

- Under AS – virtually certain
- Under TAS – reasonably certain

TAS (PC) = AS-29

- Disclosures
  - (a) a brief description of the nature of the obligation;
  - (b) the carrying amount at the beginning and end of the previous year;
  - (c) additional provisions made during the previous year, including increases to existing provisions;
  - (d) amounts used (i.e. incurred and charged against the provision) during the previous year;
  - (e) unused amounts reversed during the previous year; and

Transitional Provisions

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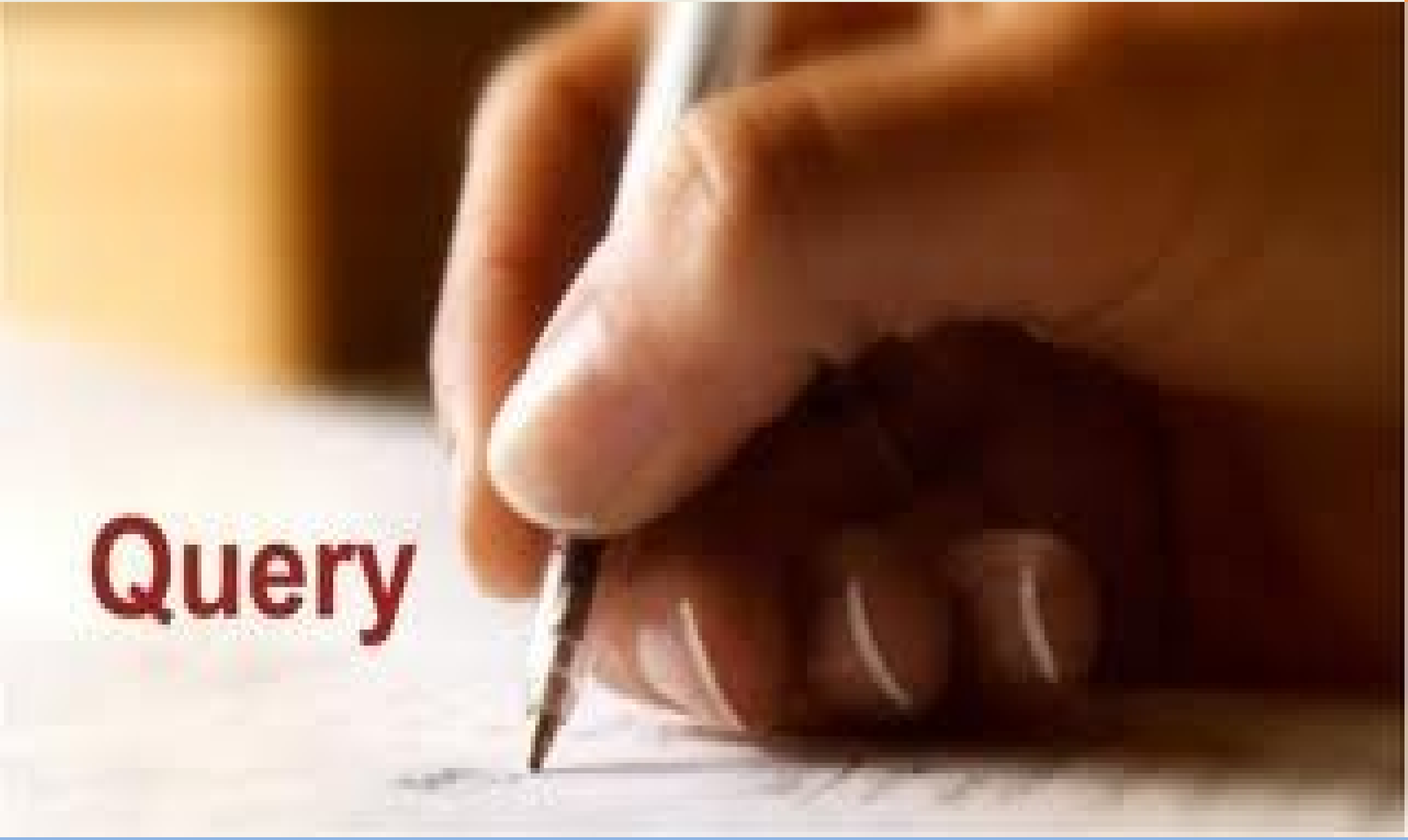
Transitional Provisions

- Suitable provisions will be made to ensure that the same income is not taxed twice

  Or
- An Expenses does not get disallowed twice.

Any Query?



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