Accounting Standards 15, 22 and 29

Young Members Empowerment Committee of the ICAI

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AS 15– Employee Benefits

AS 15– Briefly Explained

- **EMPLOYEE BENEFITS**
  - During Service
    - $\leq$ 12 Months(Short Term) : Accrual Basis and No Discounting
    - > 12 Months(Long Term) : Actuarial Valuation- Projected Unit Credit Method
  - Post Employment
    - On / After Retirement
      - Defined Contribution Plan
      - Defined Benefit Plan
    - Termination Benefits

Employee Benefits

- Include all forms of consideration to employees in exchange of services rendered payable under
  - Legislative requirements
  - Formal plans / agreements
  - Industry arrangements
  - Informal practices giving rise to an obligation
- Employees include
  - Full Time/part time
  - Permanent/casual
  - Whole time directors
  - Temporary workers

Short Term employee benefits …

- Accounting treatment
  - Benefits other than short term compensated absences and profit sharing to be expensed , unless capitalisation permitted by AS-10
  - No discounting to be used.
- Short term compensated absences classified as :
  - Accumulating- Do not lapse if not used; can be carried forward in future periods
  - Non-accumulating-lapse if not used
  - Different manner for accounting of both

Post employment benefits

Comprise of

- Retirement benefits:
  - Gratuity, pension
- Other benefits:
  - Life Insurance
  - Medical care
- Arrangements to provide post employment benefits are post employment benefit plans
- Classified as:
  - Defined contribution plans- Obligation limited to agreed contribution
  - Defined benefit plans- Obligation to provide agreed benefits.

Multi Employer plans

- Enterprise may classify a MEP as
  - Defined contribution plan or
  - Defined benefit plan
- Proportionate share of defined obligation to be recognised if it is a defined benefit plan.
- If information is not sufficient to classify as a defined benefit plan , it should recognise cost as a defined contribution plan and disclose reasons for the same.

Post Employment benefits

- Defined Contribution plan:
  - Amount of contribution payable to be recognised as an expense. No actuarial assumptions
  - Liability to be created for net amount after deducting contributions paid.
  - If excess contribution paid, such excess to be shown as prepaid.
  - If expense falls due after 12 months from balance sheet date- discounting to be used.

Post Employment benefits …

- Defined benefit plan:
  - Measurement is complex as they may be settled many years after employees render service
- Responsibility of measurement of obligation lies with the enterprise, but services of a qualified actuary may be used.
- Obligation arising from informal practices also to be recognised in the financials.

Post Employment Benefits …

- Accounting of defined benefit plans involve following steps :
  - Actuarial Techniques to identify benefit amount
  - Discounting using Projected Unit Credit method to arrive at the Present value of defined benefit obligation
  - Fair value of plan assets
  - Total amount of actuarial gains and losses
  - Determination of past service cost
  - Gain or loss on curtailment/settlement

Post Employment Benefits Defined Benefit …

- PROFIT AND LOSS:
- Following amounts to be included in expense calculation
  - Current Service cost
  - Interest Cost
  - Expected return on any plan assets
  - Actuarial gains and losses
  - Past service cost
  - Effect of any curtailments

Termination Benefits

- Benefits payable when:
  - Enterprise terminates employment before retirement date
  - Employee voluntarily accepts redundancy in exchange for such benefits
  - Certain benefits payable on employee departure
    - Amount is certain, timing uncertain
    - To be treated as post employment benefits
- Enterprise should recognize termination benefits only if:
  - Present obligation exists due to past events
  - Probability of resource outflow
  - Can be reliably estimated.

Termination Benefits …

- Termination benefits are recognised immediately
- Benefits falling due more than 12 months after balance sheet date are discounted using appropriate discounting rate.
- If there is uncertainty about no. of employees willing to accept offer of termination benefits, amount to be disclosed as a contingent liability

Case Studies…

- **Question :**
  - Measurement of accumulating compensated leaves where vesting occures and there will be cash payment for unused leave entitlement, on leaving.
- **Solution :**
  - W.r.t paragraph 11,14 and 16
    - Expense should be recognized when the service is rendered which increases entitlement to future compensated absences
    - Bases the additional amount that the enterprise expects to pay as a result of accumulation of unused entitlement, and not the maximum amount it could be obliged to pay

EAC Query w.r.t AS 15

- Facts of the case:
  - How to value and disclose liability towards Exempt Provident Fund Trust where interest portion is a defined benefit and contribution made is having the characteristic of defined contribution plan
- Opinion:
  - Exempt Provident Fund Scheme is a defined benefit plan in terms of paragraph 7.6 of AS 15, the accounting for which has to be done on an actuarial basis.
  - Since it is a defined benefit obligation, the enterprise is required to make the disclosures in terms of paragraph 120 of AS 15.
  - The plan assets held by the Trust should be valued at fair value as per the principles of AS 15.

Examples of Qualified Opinion

- In the financials as on March’13, the Auditor’s Report of Steel Authority of India gave a qualified opinion in respect of AS-15 as under :
  - In view of the assumptions provided by the Company relating to the salary escalation rates, auditors were unable to comment on the adequacy of provision for retirement employee benefits based on actuarial valuation as per Accounting Standard -15 : "Employee Benefits" issued by the Ministry of Corporate Affairs

Examples of Qualified Opinion

- In the financials as on March'14, the Auditor's Report of Oriental Bank of Commerce gave a qualified opinion in respect of AS-15 as under :
  - The plan assets of the pension fund and gratuity fund includes an amount of Rs.117.51 crore and Rs.59.20 crore respectively invested by the trust in the Bank's own Bonds / Deposits which is not in accordance with Accounting Standard – 15 "Employee's Benefits" issued by the Institute of Chartered Accountant of India.

AS 22 – Accounting for Taxes on Income

Scope

- Determines and accounts for expenses and savings pertaining to taxes on Income (both domestic and foreign) in respect to an accounting period
- Tax Expenses should include current tax and deferred tax
- Except in the situations stated in paragraph 17, deferred tax assets should be recognised and carried forward only to the extent that there is a reasonable certainty that sufficient future taxable income will be available against which such deferred tax assets can be realised.
- Where an enterprise has unabsorbed depreciation or carry forward of losses under tax laws, deferred tax assets should be recognised only to the extent that there is virtual certainty supported by convincing evidence that sufficient future taxable income will be available against which such deferred tax assets can be realised.

Scope …

MATCHING PRINCIPLE	• Taxes on income should be accrued in the same period as the revenue and expenses to which they relate.
DIFFERENCE BETWEEN ACCOUNTING PROFIT & TAXABLE PROFIT	• Differences between **ITEMS and AMOUNTS** of revenue and expenses in statement of Profit & Loss and those for tax purposes
DEFERRED TAX	• Tax effect of timing differences • Tax on income earned/accrued but not taxed as per the taxation laws of the country • Tax on income not earned/accrued but taxed as per the taxation laws of the country

Illustrations

- Can DTA/DTL in Balance sheet be considered for goodwill or share valuation?
- DTA/DTL being fictitious assets cannot be considered for goodwill or share valuation.

Illustrations…

- On company becoming subsidiary, while calculating goodwill/capital reserve, can deferred tax be provided on accrual basis?
- Deferred tax cannot be provided on accrual basis because tax is not notional income of the group.
- However, for foreign subsidiaries under integral operation, the translation effect is taken into Parent's Profit & Loss Account; requiring deferred tax to be taken into account.

EAC Query on AS 22

Subject	• Treatment of income tax paid for earlier years against the uncontested demand received during the current period
Facts	• A private sector listed company is engaged in providing global fluid management solutions • The Co. had a survey under section 133A of the Income tax Act, 1961 during the financial year 2012-13. • After the survey, the Income-tax authorities sent a notice of demand disallowing certain expenses claimed by the company as allowable for earlier financial years for which assessments are pending.
Management view	• Adjust/debit these tax expenses for earlier years directly to general reserve instead of debiting it to the statement of profit and loss for the current period. • Debiting earlier year's tax expenses to the current year's statement of profit and loss will give a distorted figure of the current year's profit
Query	• Whether income tax paid for earlier years against the uncontested demand raised by the Income-tax authorities during the current period can be directly debited to general reserve of the Co.

Opinion Given by EAC

- Income tax paid for earlier years against the uncontested demand raised by the Income-tax authorities against the Co. during the current year should not be directly adjusted against the general reserve of the Co. based on:

Para 9 of AS 22

- Tax expense for the period, comprising current tax and deferred tax, should be included in the determination of the net profit or loss for the period.

Para 5 of AS 5

- All expenses and incomes recognised during the period should be included in the determination of profit or loss

Committee View

- Although tax is estimated on profits, for accounting purposes, it is an expense which is to be included in the determination of profit/loss

Example of Qualified Opinion - BSNL

- In the financials as on March'13, the Auditor's Report of BSNL gave a qualified opinion in respect of AS-22 as under :
  - The Company has not accounted for the amount of deferred tax asset as on 31st March, 2013 in accordance with Accounting Standard 22 on accounting for taxes on income notified by Companies Accounting Standard Rules, 2006. the consequential impact of adjustment, if any, on the financial statements is currently not ascertainable.

Example of Qualified Opinion - BSNL …

- The deferred tax has been dealt with in accordance with the contention of the Company before the tax authorities.
- The Company contends that the capital reserve arising out of the capital structure at the time of incorporation of the company is not in the nature of financial relief and hence not to be reduced from the value of fixed assets.
- According to the company's contention, the depreciation provided in the book on the value of assets without deducting the amount involved in capital reserve is admissible in income tax.
- On this basis, the Company is recognizing the deferred tax assets/liabilities.

Example of Qualified Opinion

Southern Power Distribution Co of Andhra Pradesh Ltd.

- In the financials as on March'11, the Auditor's Report of Southern Power Distribution Co of Andhra Pradesh Ltd. gave a qualified opinion in respect of AS-22 as under :
  - Deferred Tax asset / liability has not been recognized in the accounts as required under AS-22 "Accounting for Taxes on Income".

AS 29 – Provisions ,Contingent Liabilities and Contingent Assets

AS 29 : PROVISIONS, CONTINGENT LIABILITIES and CONTINGENT ASSET

PROVISIONS	Present obligation from past events	Outflow is Probable	Ability to measure	No alternative settlement
CONTINGENT LIABILITIES	Possible Obligation from past events	Dependent upon a contingent event	Future event not within control	
CONTINGENT ASSET	Possible asset from past event	Dependent upon a contingent event	Future event not within control	

Decision Table - Position Summarized

Situation 1	Situation 2	Situation 2
There is a present obligation that probably requires an outflow of resources and a reliable estimate can be made of the amount of obligation.	There is a possible obligation or a present obligation that may, but probably will not, require an outflow of resources.	There is a possible obligation or a present obligation where the likelihood of an outflow of resources is remote.
Action 1	**Action 2**	**Action 3**
A provision is recognised (para 14). Disclosures are required for the provision (paras 66 and 67)	No provision is recognised (para 26). Disclosures are required for the contingent liability (para 68).	No provision is recognised (para 26). No disclosure is required (para 68).

As per Para 26 of AS 29 an enterprise should not recognise a contingent liability

- TATA STEEL Annual report for 2012-13:
  - Disclosed Potential liability of Rs:3,006.46 crores (Approximate)
- Facts of the case:
  - The State Government of Odisha introduced "Orissa Rural Infrastructure and Socio Economic Development Act 2004" with effect from February 2005 levying tax on mineral bearing land computed on the basis of value of minerals produced from the mineral bearing land. The Company had filed a Writ Petition in the High Court of Odisha, challenging the validity of the Act. Odisha High Court held in November 2005 that State does not have authority to levy tax on minerals. The State Government of Odisha moved the Supreme Court against the order of Odisha High Court and the case is pending with Supreme Court.

As per Para 26 of AS 29 an enterprise should not recognise a contingent liability …

- ACC LTD Annual report for year ended December 12, 2013:
  - The Competition Commission of India issued an Order dated 20th June, 2012, imposing penalty on certain cement manufacturers, including the Company, concerning alleged contravention of the provisions of the Competition Act, 2002, and imposed a penalty of ` 1,147.59 Crore on the Company. The Company had filed an appeal against the said Order before the Competition Appellate Tribunal(COMPAT).
  - Pending final disposal of the appeal, the COMPAT has stayed the penalty with a condition to deposit 10% of the penalty amount, which has been deposited in the form of short term bank fixed deposit with lien in favour of COMPAT. The fixed deposit has been renewed on maturity along with interest of ` 4.30 Crore. Based on the advice of external legal counsel, the Company believes that it has good grounds for a successful appeal.
  - Accordingly, no provision is considered necessary.
  - Suitable Disclsoures have been given

Example of Qualified Opinion - BSNL

- In the financials as on March'13, the Auditor's Report of BSNL gave a qualified opinion in respect of AS-29 as under :
  - The provisions and the disclosures with regard to the matters under litigations have been made based upon the management estimates. Based upon the report of auditors reports for certain circles, sufficient and appropriate audit evidence for examining and verifying the quantum of contingent liabilities disclosed in note 42.1 to the financial statements has not been obtained. In the absence of the required details and documents at some of the circles and pending the responses to our confirmation requests in respect of the litigations at Company level, the impact of adjustment, if any, on the financial statements is currently not ascertainable.

Open House

Thank you

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