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Chapter six Implication of accounting standards issued by ICAI in tax audit u/s 44AB of Income Tax Act 1961

6-1- Introduction:-

In the Chapter Five the researcher learnt all details about tax audit u/s AB of Income Tax Act of 1961. In this chapter we will study the implication of accounting standards issued by ICAI in tax audit u/s 44 AB. This chapter has particular importance because the researcher in this chapter is trying to research about acceptance or reject the third hypothesis “there are Implication of accounting standards on tax audit u/s 44AB of Income Tax Act 1961” this is third hypothesis of our study, so we will search ASs implication on tax audit and the researcher will study the convergences and divergence between income tax Act 1961, and ASs issued by ICAI.

Tax audit under section 44 AB Income tax Act 1961, will not be away from implication of accounting standards issue by ICAI, but we should make sure how this implication, the implication is generally or specifically.

Tax audit is specialization audit. When there are disagreements between accounting standards issued by ICAI and Income Tax Act 1961, provisions, in this case absolutely the provisions of Income Tax will be prevalent on Accounting Standards.

Indian Central government and the Institute of Chartered Accounting of India are main players in the tax audit under section 44AB Income Tax Act 1961.

In this section the researcher well try to highlight on the role of two parties (central government and ICAI) on tax audit, because those two parties have formed tax audit procedures.

Indian central government enacted compulsory tax audit u/s 44AB and declared persons are required to get their accounts compulsorily audited by a chartered accountant according to u/s 44AB income tax Act, 1961, as well as central government issued through CBDT two Income Tax accounting standards. They are applying when conducted tax audit, and central board of direct tax is issuing once and again notifications pertaining tax audit.

On the other hand the Institute of Chartered Accounting of India, has issued Accounting Standards, Audit and Assurance standards, Guidance note on tax audit u/s 44AB of income tax Act, 1961 and supplementary guidance note on tax audit, guidance note on audit of fringe benefits under the income- tax Act, 1961, and also ICAI continues in issue
notifications to its members explaining some declaration for procedures of tax audit. So central
government and ICAI have complete relationship with tax audit u/s44AB. That means central
government enacted provisions or issues annual amendment in the income tax Act, then ICAI also issues the interpretation and procedures for that amendment. Due to tax audit aims to compute the taxable income according to the law and for maintaining transparency in the financial statement, it is also as a tool in the hands of tax authority to curb noncompliance of income tax law. That means government unique has benefits from tax audit, so the government absolutely has share in the arrangement of tax audit, therefore Indian central government has issued two accounting standards. Indian government has enacted section 44AB, in the fact both sides Indian government as official part and ICAI as domestic part has been subscribed in the arrangement tax audit. Central government enacted the finance Act, section 145, 1995, and also it has issued notification No.S.O.69(E), deted 25th January,1996, for exercise of the power by section 145(2).

The mandatory AS issued by ICAI also applies respect of financial statement audited under section 44AB of the income tax Act,1961. Accordingly, member should examine compliance with the mandatory accounting standards when conducting such audit (advance auditing, volume.1,IACI, jenury,2006,p13.9)

Conclusion:- Indian central Government enacted section44AB for tax audit and CBDT issued two accounting standard are applying when conducted tax audit and income tax Act 1961, provisions should apply when discharging tax audit and Institute of Chartered Accounting of India, has issued Accounting Standards, Audit and Assurance standards, Guidance note on tax audit u/s 44AB of income tax Act, 1961 and supplementary guidance note on tax audit, guidance note on audit of fringe benefits under the income- tax Act, 1961, and also ICAI continues in issue notifications to its members explaining some declaration for procedures of tax audit.

**6-2- The section deals with method of accounting:-**
The section in Income Tax Act, 19612, “145, (1) Income chargeable under the head “Profits and gains of business or profession” or “Income from other sources” shall, subject to the provisions of sub-section” (2) be computed in accordance with either cash or mercantile system of accounting regularly employed by the assessee.
(2) The Central Government may notify in the Official Gazette from time to time accounting standards to be followed by any class of assesses or in respect of any class of income. (Income tax Act, 1961, 1.657, 2007)

6-3- Role of Accounting Standards:-
Standards are formulated in general with a view to harmonize varying accounting policies and treatment across a section of businesses. The objective is to reduce the accounting alternatives in the preparation of financial statements within the bounds of rationality, thereby ensuring comparability of financial statements of different enterprises to give a true and fair view of financial position and working results.

While Accounting Standards (AS) issued by ICAI are expected to be complied with as a mandatory requirement for Company law purposes, the Income-tax Act also requires the income to be computed on the basis of a regular method of accounting (Sec 145), Further, both standards prescribed under the Income-tax Act and the company law would require prudence and conservatism to be followed in recognition of income. This has to be understood in the context of wide powers (including power to frame a best judgment assessment) given to the tax officer to reject a taxpayer's books of accounts and/or disallow a legitimate business claim, should proper and consistent accounting principles not be followed. (Business standards Mukesh Butani / New Delhi May 04, 2009)

6-4- Accounting standards issued by central government:-
With the biggest significance for tax revenue, taxation is representative main source of Indian government and also for getting the right tax due. Indian central government enacted section number 44AB in the year 1984. It also enacted a new section 145 in financial act, 1995, and central government issued notification No.S.O.69(E), relating to accounting standards that should be follow by assessee when tax audit is conducted.

Two different sets of Accounting Standards may cause confusion for taxpayers and other stakeholders. Accordingly, the Accounting Standards notified under the Act should be termed as "Tax Accounting Standards" (TAS) to distinguish them from the Accounting Standards issued by the ICAI/notified under the Companies Act, 1956. This Tax Accounting Standard is applicable for computation of income chargeable under the head "Profits and
gains of business or profession" or "Income from other sources" and not for the purpose of maintenance of books of account.

In the case of conflict between the provisions of the Income-tax Act, 1961 (‘the Act’) and this Tax Accounting Standard, the provisions of the Act shall prevail to that extent. In exercise of the powers conferred by section 145(2), the central government has by notification No.S.O.69(E), dated 25th January, 1996 notified two AS(IT). This notification came into force with effect from 1st day of April, 1996, and is accordingly application from assessment year 1997-98 and subsequent assessment years." (Guidance note on tacaudit, 2005, 33, 34) pursuant to the provisions of sec.145(2) the CBDT has notified two accounting standards for the purpose of the Income Tax Act. The first accounting standard is corresponding to the requirements of AS-1 of ICAI. The second accounting standard is corresponding to the requirements of AS-5 of ICAI.

Accounting standards to be followed by all assessss following mercantile system of accounting as per clause 11(d) of the from 3CD, the tax auditor has to report about the details of deviation, if any, in the method of accountancy employed in the previous year from accounting standards u/s 145 and effect thereof on the profit and loss.

A. Accounting standard I relating to disclosure of accounting policies
B. Accounting standard II relating to disclosure of prior period and extraordinary items and changes in accounting policies

6-4-1-AS-I- Disclosure of accounting policies:-
This standard requires disclosure of all significant accounting policies adopted in the preparation and presentation of financial statements. at one place. There are different accounting policies following different enterprises, for examples, method of depreciation, depletion, amortization, treatment of expenditure during construction, conversion of foreign currency items, valuation of investment, treatment of goodwill, valuation of inventories, valuation of fixed assets, treatment of contingent liabilities….etc.

The fundamental accounting assumption, like accrual, going concern and consistency are followed in financial statement. Specific disclosure of such assumption is not required, but if not followed, such facts should be disclosed. (C.A.T.H Gupta, and C.A.H.C.Gupta, 2007, 58)

These AS(IT) are given below:
Accounting Standards to be followed by all assessees following mercantile system of accounting

A. Accounting Standard I relating to disclosure of accounting policies

1. All significant accounting policies adopted in the preparation and presentation of financial statements shall be disclosed.

2. The disclosure of the significant accounting policies shall form part of the financial statements and the significant accounting policies shall normally be disclosed in one place.

3. Any change in an accounting policy which has a material effect in the previous year or in the years subsequent to the previous years shall be disclosed. The impact of, and the adjustments resulting from such change, if material, shall be shown in the financial statements of the period in which such change is made to reflect the effect of such change. Where the effect of such change is not ascertainable, wholly or in part, the fact shall be indicated. If a change is made in the accounting policies which has no material effect on the financial statements for the previous year but which is reasonably expected to have a material effect in any year subsequent to the previous year, the fact of such change shall be appropriately disclosed in the previous year in which the change is adopted.

4. Accounting policies adopted by an assessee should be such so as to represent a true and fair view of the state of affairs of the business, profession or vocation in the financial statements prepared and presented on the basis of such accounting policies. For this purpose, the major considerations governing the selection and application of accounting policies are the following, namely:

   (i) Prudence - Provisions should be made for all known liabilities and losses even though the amount cannot be determined with certainty and represents only a best estimate in the light of available information; ii) Substance over form - The accounting treatment and presentation in financial statements of transactions and events should be governed by their substance and not merely by the legal form;
   (iii) Materiality - Financial statements should disclose all material items, the knowledge of which might influence the decisions of the user of the financial statements.

5. If the fundamental accounting assumptions relating to going concern, Consistency and Accrual are followed in financial statements, specific disclosure in respect of such assumptions is not required. If a fundamental accounting assumption is not followed, such fact shall be disclosed.
6. For the purposes of paragraphs (1) to (5), the expressions, - (a) "Accounting policies" means the specific accounting principles and the methods of applying those principles adopted by the assessee in the preparation and presentation of financial statements;
(b) "Accrual" refers to the assumption that revenues and costs are accrued, that is, recognised as they are earned or incurred (and not as money is received or paid) and recorded in the financial statements of the periods to which they relate;
(c) "Consistency" refers to the assumption that accounting policies are consistent from one period to another;
(d) "Financial statements" means any statement to provide information about the financial position, performance and changes in the financial position of an assessee and includes balance sheet, profit and loss account and other statements and explanatory notes forming part thereof;
(e) "Going concern" refers to the assumption that the assessee has neither the intention nor the necessity of liquidation or of curtailing materially the scale of the business, profession or vocation and intends to continue his business, profession or vocation for the foreseeable future ( Guidance note on tax audit under section 44AB,P,34,35,2005)

6-4-2-AS-II- Prior period and extraordinary items and changes in accounting policies:-
That means prior period items shall be separately disclosed in P&L a/c, Extra ordinary items shall be disclosed in P&L a/c as part of taxable income.
Accounting Standard II relating to disclosure of prior period and extraordinary items and changes in accounting policies: Prior period items shall be separately disclosed in the profit and loss account in the previous year together with their nature and amount in a manner so that their impact on profit or loss in the previous year can be perceived.
8. Extraordinary items of the enterprise during the previous year shall be disclosed in the profit and loss account as part of income. The nature and amount of each such item shall be separately disclosed in a manner so that their relative significance and effect on the operating results of the previous year can be perceived.
9. A change in an accounting policy shall be made only if the adoption of a different accounting policy is required by statute or if it is considered that the change would result in a more appropriate preparation or presentation of the financial statements by an assessee.
10. Any change in an accounting policy which has a material effect shall be disclosed. The impact of, and the adjustments resulting from such change, if material, shall be shown in the financial statements of the period in which such change is made to reflect the effect of such change. Where the effect of such change is not ascertainable, wholly or in part, the fact shall be indicated. If a change is made in the accounting policies which has no material effect on the financial statements for the previous year but which is reasonably expected to have a material effect in years subsequent to the previous years, the fact of such change shall be appropriately disclosed in the previous year in which the change is adopted.

11. A change in an accounting estimate that has a material effect in the previous year shall be disclosed and quantified. Any change in an accounting estimate which is reasonably expected to have a material effect in years subsequent to the previous year shall also be disclosed.

12. If a question arises as to whether a change is a change in accounting policy or a change in an accounting estimate, such a question shall be referred to the Board for decision.

13. For the purposes of paragraphs (7) to (12), the expressions:

(a) "Accounting estimate" means an estimate made for the purpose of preparation of financial statements which is based on the circumstances existing at the time when the financial statements are prepared;

(b) "Accounting policies" means the specific accounting principles and the method of applying those principles adopted by the assessee in the preparation and presentation of financial statements;

(c) "Extraordinary items" means gains or losses which arise from events or transactions which are distinct from the ordinary activities of the business and which are both material and expected not to recur frequently or regularly. Extraordinary items include material adjustments necessitated by circumstances which, though related to the years preceding the previous years are determined in the previous year: Provided that income or expenses arising from the ordinary activities of the business or profession or vocation of an assessee, though abnormal in amount or infrequent in occurrence, shall not qualify as extraordinary items;

(d) "Financial statements" means any statement to provide information about the financial position, performance and changes in the financial position of an assessee and includes
balance sheet, profit and loss account and other statements and explanatory notes forming part thereof;

(e) "Prior period items" means material charges or credits which arise in the previous year as a result of errors or omissions in the preparation of the financial statements of one or more previous years: Provided that the charge or credit arising on the outcome of a contingency, which at the time of occurrence could not be estimated accurately shall not constitute the correction of an error but a change in estimate and such an item shall not be treated as a prior period item (Guidance note on tax audit under section 44AB, P.36, 35, 2005)

As mentioned before AS-I- and -II-, it appears that the method of accounting referred here, refers to accounting policies. Therefore the auditor should ensure that, if there is any deviation in the accounting policy, or its disclosure from the Accounting standard prescribed u/s 145 of the income tax Act, these are to be reported here. Change in accounting policy, which has a material effect along with effect of such change, is not ascertainable, wholly or in part, the fact shall be indicated. Deviation, if any, from the Accounting standard issued by the CBDT has to be reported.

6-5-Accounting standards and Income Tax Act 1961 Convergence and Divergence:-

The Institute of Chartered Accountants of India (ICAI) has prescribed 32 Accounting Standards (ASs) so as to ensure that there is uniformity in the accounting practices followed in the Country. Accounting Standards relate to the codification of generally accepted accounting principles.

These are the norms of accounting policies and practices by way of codes or guidelines to direct as to how the items which go to make up the financial statements should be dealt with in accounts and presented in the annual accounts.

The main purpose of standards is to provide information to the users as to the basis on which the accounts have been prepared. Disclosure of accounting policies enables the users to interpret the reported information. Standards may consist of detailed rules to be adopted for accounting treatment of various items before the presentation of financial statements, these AS are generally applicable to all entities, who prepare their financial statements for various purposes.
Accounting Standards have received statutory recognition in terms of Sec. 211(3B) of Companies Act, 1956, there is statutory support for the accounting standards issued by the institute u/s 227(3)(d) of the companies Act, 1965, as well, which provide that the auditor's report shall also state whether, in his opinion, the profit and loss account and balance sheet comply with the accounting standards referred to in sub-section(3C) of section 211. (C.A.T.H. GUPTA,2007.P290)

Accounting is the language of business and accounting standards the grammar of the language. The question that arises for consideration is whether requirement of mandatory compliance of other accounting standards will apply to tax audit or non-corporate entities?

“The institute has issued a notification in January, 1994 issue of CA Journal (p-639), which state that in respect of the accounting years 1993-94 and onwards the mandatory accounting standards will apply in respect of general purpose financial statement, where such statement are statutorily required to be under the law. The institute has clarified, that Accounting Standards are applicable to undertaking having only commercial, industrial or business activities” (Guidance note on tax audit,2005, p.30)

ASs apply in respect of financial statement audited under section 44AB of the income mandatory accounting standards when conducting such audit. , (Guidance note on tax audit,2005, p.31)

"While discharging their attest function, it will be the duty of the members of the Institute to ensure that the Accounting Standards are implemented in the presentation of financial statements covered by their audit reports. In the event of any deviation from the standards, it will be also their duty to make adequate disclosures in their reports so that the users of such statements may be aware of such deviations.” (Guidance note on tax audit, 2005,p.32)

Financial statements are prepared as these are required to be submitted to the concerned government authorities. The Government of India collects Income-tax on the income earned on the basis and at the rates prescribed under the Income tax Act, 1961 (ITA). The Department of Income-tax assesses the income and levies tax on the basis of assessed income after taking into consideration the provisions contained in the ITA. For assessing the income of the assessee, the Income-tax Department relies upon the books of accounts maintained by the assessee.
The Income-tax Department is one of the major beneficiaries of the standardization of the accounts maintained by various assesses. This standardization is due to the various accounting standards issued by the ICAI.

Mandatory accounting standards are also applicable in respect of financial statements audited under Section 44 AB of the Income-tax Act, 1961. The ICAI has issued various accounting standards to harmonize the diverse accounting policies and practices in consonance with the International Accounting policies and statements. The corporate and non-corporate entities are subject to these mandatory regulations.

It is well accepted that accounting standards and taxation of income are two independent subjects operating in their own spheres. However, given the fact that eventually both seek to prescribe methodologies for quantification of economic performance and have distinct philosophy and methodology of determining the quantum of “income” some overlap is inevitable. Ideally, overlap should not result in any divergence between the two approaches. But that is the ideal situation which in reality is not always achieved. As a result there are areas where the principles of taxation and the accounting standards supplement and support each other, areas where the two deal with subjects which do not directly affect each other and some areas which affect certain common subjects but one sees divergent approaches between the two.

The objectives of determination of income by revenue officials are different from those entrusted with the task of preparation and attestation of accounts. Accounting Standards are intended to lay down consistent methodologies of treatment of certain items and the ultimate objective is to enable a reflection of true and fair view. The intention of the tax authorities is to determine `income' as is understood under the Income-tax Act. This may not necessarily be the real income. While the income as computed for the purpose of the tax laws is not entirely divorced from the concept of "true and fair, the Courts have increasingly started relying on the Accounting pronouncements issued by the ICAI for drawing certain conclusions,( Jayant Gokhale, August 2010,p 3)

"But as presented by the ICAI, other mandatory accounting standards also apply in respect of financial statement audited u/s 44AB of the income tax –tax Act, 1961. Accordingly, the auditor should examine compliance with the mandatory accounting standards when conducting such audit." (Gupta,2007,p.291)
As mentioned earlier, it is clear that, all opinions are in the need for compliance with accounting standards when tax auditor discharge tax audit to the assessee. It is pertinent to note that a few provisions of Income Tax Act seek to bring about a synthesis with accounting, while a few others expressly deviate from accounting. It is also to be noted that although the tax audit is done basically for facilitating income tax assessment, still they are to be regarded as General Purpose Financial Statements and the Accounting Standards are applicable.

Researcher will try prescribed brief each accounting standard, its relation into provisions of income tax Act, 1961, and if there are positive Implication of accounting standards on tax audit u/s 44AB of income tax Act, 1961, in order to prove second hypothesis in our Ph.D Research, and also to achieve one of the study's objectives.

Accounting standards may be broadly classified into two categories:

1. Standards which affect the scheme of accounting entries in the book of accounting and quantification of these entries. Such accounting standards would have a direct bearing on the quantum of reported income and also on valuation of assets and liabilities. Therefore, these accounting standards have a direct bearing on the tax liability of the assessee.

2. Standards which do not affect the accounting entries but require disclosure of additional information, these may be called reporting standards. These standards may not affect the reported income directly. Such information can be used by the tax Administration for determination of taxable income.

6-5. 1. Recognition of accounting principle by judicial forums while setting tax disputes.

Various judicial authorities in the country, including the Supreme Court of India, have recognized the accounting principles and accounting standards laid down by the ICAI while deciding the tax disputes. There have also been instances when courts have purposefully synchronized the statement/Guidance Note/Accounting Standards issued by the ICAI while deciding about certain issues from the taxation point of view.

From the very rigid position earlier, the Courts have come around in to the view that the manner of accounting entries passed though not conclusive may have persuasive value in deciding the correct income (CA. C.N. Vaze, p3, April 10, 2010)

“Finally the Courts have increasingly started relying on the Accounting pronouncements issued by the ICAI for drawing certain conclusions. It would thus appear that the law is thus
evolving in the manner giving increasing weight age to the standards and guidance provided by the ICAI” (Jayant Gokhale, F.C.A. p4, Program on Direct Taxes hosted by EIRC Aug 2010)

However, there have also been occasions when appellate and judicial forums have not followed the accounting principles and accounting standards in the context of determining certain issues under the tax law. This is for the reason that courts having recognized. Authenticity of accounting principles and accounting standards, have felt that in the matter of computation of income, effect should be given to the specific provisions of the tax laws.

6-5-2-Accounting standards and income tax law convergence and divergence:-
Are accounting principles and accounting standards recognized under taxation law? Apparently this question seems to be very simple. However, when you delve into the depth of the question, you may find that there are conflicting answers, Yes or No. The answer may be Yes or No depending on the specific issue in taxation in respect of which the question is raised.

It is well accepted that accounting standards and taxation of income are two independent subjects operating in their own spheres. However, given the fact that eventually both seek to prescribe methodologies for quantification of economic performance and have distinct philosophy and methodology of determining the quantum of “income” some overlap is inevitable. Ideally, overlap should not result in any divergence between the two approaches. But that is the ideal situation which in reality is not always achieved.

As a result from our discussion in this chapter we found that (we will see in coming pages), there are areas where the principles of taxation and the accounting standards supplement and support each other, areas where the two deal with subjects which do not directly affect each other and some areas which affect certain common subjects but one sees divergent approaches between the two. The areas where there is some divergence between the taxation of income and accounting for Income arises due to some conceptual differences.

Even this is theoretically acceptable because it has to be recognized that accounting is not an exact science but rather a process of scientific approximation. In the long run these deviations would cancel out and therefore "in the long run" the net result by either method would be the same. This is where the conceptual mismatch arises because for accounting theory.
The prime objective for financial statements and balance sheet is to present a true & fair view. The presentation of the state of affairs as at a particular cut-off date is emphasized rather than determination of income. Income is determined on a conservative basis. As against the above; the objectives of determination of income by revenue officials are different from those entrusted with the task of preparation and attestation of accounts, AS are intended to lay down consistent methodologies of treatment of certain items and the ultimate objective is to enable a reflection of true and fair view. The intention of the tax authorities is to determine `income' as is understood under the Income-tax Act. This may not necessarily be the real income, while the income as computed for the purpose of the tax laws is not entirely divorced from the concept of "true and fair".

After globalization, there is one more dimension and challenge of synchronizing or reconciling different laws, practices, customs and accounting standards prevailing in different countries. Some degree of uniformity is sought to be achieved by the proposed implementation of international financial reporting standards IFRS (CA. C.N. Vaze, April 10, 2010)

In any case, we have to bear with the dichotomy or lack of harmony between accounting standards and the provisions of revenue laws – like Income Tax Act. Therefore, there is a need to study the Impact of accounting standards on tax audit u/s44AB of income tax Act1961.

Income tax Act 1961, has recognized and prescribed only two AS in terms of Sec. 145. They call it as NAS – 1 and NAS – 2, which correspond to AS 1 (Disclosure of Accounting Policies) and AS 5 – Prior period adjustments. Nevertheless, all other AS are applicable either under Company Law; or in any case under the regulations for CAs, Naturally the AS applicable to a particular entity will affect its taxation.

It is pertinent to note that a few provisions of Income Tax Act seek to bring about a synthesis with accounting, while a few others expressly deviate from accounting. E.g.: Sec. 115JB: – gives lot of weight age to the book profit. So also, proviso to Sec. 36 (1) (iii) tries to adopt the principles mentioned in AS 16 (accounting for borrowing costs). On the other hand, Sec. 32 is a major deviation from accounting, particularly by virtue of ‘block of assets’ concept.

Further, Sec. 43B deviates clearly from the tenets of accrual method of accounting.
2.3 It is also to be noted that although the tax audit is done basically for facilitating income tax assessment, still they are to be regarded as General Purpose Financial Statements (GPFS) and the AS are applicable.

Strictly speaking, till date, IT has recognized and prescribed only two AS in terms of Sec. 145. They call it as NAS – 1 and NAS – 2, which correspond to our AS 1 (Disclosure of Accounting Policies) and AS 5 – Prior period adjustments.

Nevertheless, all other AS are applicable either under Company Law; or in any case, under the regulations for CAs Naturally the AS applicable to a particular entity will affect its taxation. It is pertinent to note that a few provisions of Income Tax Act seek to bring about a synthesis with accounting, while a few others expressly deviate from accounting. E.g.: Sec. 115JB: – gives lot of weight age to the book profit. So also, proviso to Sec. 36 (1) (iii) tries to adopt the principles mentioned in AS 16 (accounting for borrowing costs).

On the other hand, Sec. 32 is a major deviation from accounting, particularly by virtue of ‘block of assets’ concept. Further, Sec. 43B deviates clearly from the tenets of accrual method of accounting.

Now, we shall study the points of similarity and differences between the principles laid down under the Accounting Standards and income-tax Act, 1961.

(1) Disclosure of accounting policies – AS1 and AS-1 in income tax Act:-

This Accounting Standard deals with the disclosure of significant accounting policies followed in preparing and presenting the financial statements. The purpose of this statement is to promote better understanding of financial statements.

The CBDT has notified TAS-1 on Disclosure on accounting policies, AS-1 issued by CBDT is more or less in line with AS-1 issued by the ICAI.

Compliance with standards is mandatory for assessees following mercantile of accounting. Further, it may be noted that in the case of corporate assesses, the profit and loss account prepared for section 115 JB(2) of the income-tax Act and annual accounts including profit and loss account prepared and placed before the Annual General Meeting has to be based on the same accounting policies. This is required even if the company adopts a financial year which is different from the previous year under the Income –tax Act.
The differences between I.T. AS-I and AS-1 of ICAI,
a- AS issue under (IT) apply only to those assesses who follow the mercantile system of accounting only, but AS issue by (ICAI) apply to both system cash, mercantile as well.
b- Concept of prudence, AS notified by the government does not contain this concept; AS1 issue by (ICAI) mentioned this concept.
c- AS issue by government include fund flow statement, AS issue by (ICAI) include cash flow statement.
d- The requirement of AS 5 regarding separate disclosure of certain item of income and expenditure from ordinary activities due to their, size or incidence does not specifically appear in the corresponding standard notified by the government. (Kamak Gupta, 2005, p 917)
e- “Under I.T AS 1 change in accounting policy shall be made only if (i) the adoption of a different accounting policy is required by statute or (ii) it is considered that the change would result in a more appropriate preparation or presentation of the financial statements of the assessee. Under AS 1 a third situation contemplated is for compliance with an accounting standard”. (Arvind H. Dalal, June, 2001, p18)

The above differences in the two standards appear to more changes of form rather than substance and if so, accounts in compliance with Accounting standard -1 can equally be considered as complying with income tax accounting standard -1 for purposes of income tax and, if any of the policies is not acceptable to the IT, it may invite enquiry.

Conclusion:- There is no doubt that the preparation of accounts according to accounting standards will be leading to uniformity and comparison of the results of the various enterprises both under the companies Act as well as for tax purposes. However there are cases of variance between the accounting standards and the tax principles in some cases.

(2) Valuation of inventories –AS 2:-

Policy in respect of valuation of inventory is required to be disclosed as per accounting standard-1 and particulars are to be given as per clause 12: valuation of stock of form No.3CD. The divergence between the methods of valuation of inventory as prescribed under AS-2 and the valuation prescribed by Section 145A is well known. Sec. 43B and Sec. 145A are good examples of deviation from AS 2 and other accounting principles

“23.11 It may be pointed out that the "inclusive method" is not permitted by AS2 which is made mandatory from accounting year beginning on or after 01.04.1999. Further, in the Guidance Note on Accounting for MODVAT the second method (inclusive method) has been withdrawn with effect from accounting year commencing from 1.4.1999. In view of the above, the adjustments under section 145A will have to be made in all cases where 'exclusive method' is followed”. (Guidance note on tax audit under section 44AB, P63, 2005)

There is a view that irrespective of whether one follows the inclusive or the exclusive method the same are tax neutral

“Although this proposition may hold true in the long run; I believe that on a year to year basis this mismatch can result in needless divergence between the income computed by the two methods and can result in avoidable litigation.” ( Jayant Gokhale, Programme on Direct Taxes hosted by EIRC, Aug 2010)

As per this standard, Inventory has to be valued at lower cost and net realizable value. This method is also recognized for income-tax purposes in case of a going concern. Only in a case where the fundamental accounting assumption of going concern no longer holds goods, the closing stock has to be valued at market price.

The Supreme Court, in ALA firm v. CIT (1991) 189 ITR 285, held that when a firm is dissolved and the business is discontinued, closing stock taken over by the partner has be valued at market value and not at cost.

The principle involved in this case is that the fundamental accounting assumption of going concern cannot be applied valuing stock-in-trade at the time of dissolution. Section 145A requires the assessee to follow the Inclusive method which results in higher profits. However if a higher value of closing stock is shown in a particular year, the same will be the opening stock in the next year. Therefore, the increase in profits in one year would be compensation by a reduction in profits in the subsequent year. The effect of adopting the inclusive method under section 145A would be to pre-open the booking of profits to the preceding year. A reasonable portion of the overheads has to be included. This decision is in accordance with the principle enunciated in AS-2

In Hela Holding Pvt. Ltd. V. CIT. (2003) 263 ITR 0129, the Calcutta Court has held that where the change in the method of valuation of stock effected by the assessee is in
accordance with the Accounting Standard and the new method has been followed consistently in the subsequent years, such a change in method would be valid and proper. Conclusion:- for the purpose of tax filings and tax audit forms. The inclusive method should be used as per section 145A of the Income-tax Act, whereas for purposes of general purpose financial statements, the exclusive method under AS-2 should be followed.

(3) Cash flow statement AS-3:-
This is a reporting standard. However, it is very relevant from the tax law point of view while justifying claims for items such as interest, which is expended for the purpose of business. This statement explains cash flow of incoming and outgoing cash and assesses the ability of the enterprise to generate cash and to utilize the cash.
This standard provide for the accounting treatment of income- tax expense. As per this standard, cash flow on account of income –tax has to be shown as operating activity unless it can be specifically identified with an investing or financing activity. If income-tax paid is segregated between these activities, then total tax paid should also be disclosed. Income-tax paid should be shown net of TDS.

4- Contingencies and events occurring after the balance sheet date AS-4 :-
As per accounting principles, contingent gains should not be accounted in the financial statement since their recognition may result in revenue which may not be realized. This treatment is in accordance with the fundamental concept of ‘prudence’
A contingent loss is one that may arise depending upon whether an event occurs at some point in the future. If firms can reasonably estimate the amount of the contingent loss and it is probable that the loss will occur, then you should record the loss in the accounting records. If the loss event is only reasonably possible, then do not record the loss in the accounting records; instead, describe the situation in the notes accompanying the financial statements. If the probability of the loss event occurring is remote, then it is not necessary to record or describe the event.
So according to AS-4 requires an enterprise to make provision for the contingent losses by charging to profit and loss account.
Under the Income-tax Act, expenditure is allowed provided it is laid out or expended for the purposes of business. It is allowed when it is incurred and not necessarily paid. It is allowed
only when it is accrued. Again, it is allowed only in the year in which an expenditure is incurred and liability is accrued. (Pradip N. Kapasi, p38)

Further, it may be pertinent to note that as per clause (c) of Explanation (1) to Sec. 115JB, the provisions made for meeting unascertained liabilities are to be added back. The provisions made under AS 4 are, generally, unascertained liabilities and hence are to be added back for the purpose of computing book profits. (J. S. Lodha Auditorium, p4). So the Income tax Act also recognizes the distinction between a present liability and future liability. However, under the tax laws, provisions for contingencies are not allowable as deduction.

"However, there is a possibility that the said expenses may be disallowed as deduction while computing taxable income. It has been held by the Hon’ble Apex Court in the case of Molasis Co. Pvt. Ltd. v. CIT [37 ITR 66 (SC)] that the expenditure dependant upon the future events is not allowable as deduction. Further, in the case of Shree Sajjan Mills Ltd. v. CIT [156 ITR 585 (SC)], it was observed that the said expenses will be allowed in the year in which such events take place.

“In a recent decision by the Hon’ble Supreme Court in the case of Southern Technologies Ltd vs. JCIT (Civil Appeal No 1337/2003) It was held that provisions for Non Performing Asset (NPA) as per RBI Norms by NBFCs is not deductible. The Hon’ble Supreme Court further held that the prudential norms or disclosure norms have nothing to do with the computation or taxability of the provisions for NPA under the IT Act. A provision for NPA is only a notional expense” (CA. C.N. Vaze, P4, April 10, 2010)

Events occurring after the balance sheet date are those significant events both favourable and unfavourable, that occur between the balance sheet date and the date on which the financial statement are approved. (T.H.Gupta and H.C.Gupta, 2007, p297)

Despite previous divergence between AS-4 and Income tax Act 1961 in the issue of events occurring after balance sheet but there is convergence between AS-4 and Income tax Act 1961. As per AS-4, events occurring after balance sheet date require adjustment in accounts if they confirm condition as at balance sheet date or call into question the assumption of going concern or such adjustments are statutory required. Further, even if events do not relate to conditions existing at the balance sheet date, adjustments to assets and liabilities will be required if they call into question the assumption of going concern. For Income-tax purpose also, the valuation of stock at lower cost or market value is permitted only if the fundamental assumption of going concern is satisfied. If this assumption fails, the stock has
to be valued only at net realizable value. Therefore, the question of whether the assumption of going concern holds good is relevant for income-tax purposes also.

It is therefore clear that an expenditure or loss is allowed under the Income tax Act only where the enterprise is able to establish that the same pertained to the year under consideration, that it is related to an event which had balance sheet date. Accordingly events occurring after the balance sheet date shall not have any effect on allowance or otherwise of expenditure or a loss for a year which was completed. The event necessarily has to take place within the year unless;

1- The Act specifically allows it in another year, for example, an expenditure specified in section 43B of the Act.
2- The theory of relating back applies or is invoked to allow such expenditure in an earlier year on the basis of the matching principle.
3- Subsequent event provides a finality to an otherwise certain event and enables the exact quantification. (Pradip N.Kapasi, 2001,p 40)

Conclusion:- According to AS-4 the contingent loss should be provided for on the basis of the nature of probability of occurrence and possibility of reasonable estimate. However, under the tax laws, provisions for contingencies are not allowable as deduction.

5- Net Profit or loss for the period. Prior period Items and Changes in accounting policies AS-5:-

The accounting standards definition on prior period items cover errors or omission in preparation of accounts and requires these items to be disclosed separately along with the heads of item. For such disclosure concept of materiality should be kept in mind.

TAS-II Disclosure of prior period and extradinary items and change in accounting policies notified by central government, which is in line with AS-5 Issued by the ICAI, has to be followed by assessees following mercantile system of accounting for income-tax purpose.

“They said standard, as it originally stood, was one of the two standards notified u/s 145 of the Income Tax Act. The notified standard was almost identical to AS-5 and therefore the position in tax and accounting in this regard would be expected to coincide. However, after Income Tax department issued Notification No. S.O. 69(E) dt. 25th January, 1996, the Institute has revised AS5. Similar revision in the notified standard under S. 145 not having been made there arises a slight divergence. Slight divergence like the requirement of AS-5
regarding separate disclosure of certain items of income and expenditure from ordinary activities due to their nature, size or incidence does not specifically appear in the corresponding standard notified by the government. Second divergence, There is a difference in the definition of the term ‘extraordinary Items’ while the standard notified by the central government includes within extraordinary Items ”material adjustments necessitated by circumstances which, though related to the years preceding the previous year are determined in the previous year.” Such items are not a part of ‘extraordinary Items’ as per AS 5, though they would still be required to be separately disclosed under AS 5.(Kamal .Gupta, 2004,p 917)

I may only mention that the standard notified under the Act significantly omits the phrase. In view of the uncertainty attached to future events, profits are not anticipated, but recognised only when realized, though not necessarily in cash. This statement which embodies the very core of what would be considered to be a prudent approach reflects the mismatch caused by the eagerness of the tax authorities to include in the taxable income what may not be considered to have accrued under the accounting standards and accounting concepts.

Conclusion:- TAS-II Notified by the central government, which in line with AS-5 is issued by the ICAI with slight divergence, has to be followed by all assesses following mercantile system of accounting for income-tax purposes.

6- Depreciation Accounting AS-6:-
In the original, Accounting standard-6 and Income Tax Act 1961, agree that, account depreciation for tangible and intangible assets and charging it into profit and loss account. The accounting standard requires depreciation to be provided on all assets which have been capitalized. Schedule XIV of the companies Act, 1956 lays down the rate of depreciation. Similarly, the Income-tax Rules provide for depreciation rates in Appendix-I-A. Depreciation between AS-6 issued by ICAI and section 32 of income tax Act 1961 is divergence more than convergence, therefore tax auditor recalculates each asset depreciation according to schedule VIX of the companies Act, 1956.

From within the convergence between AS-6 and section 32 of income tax Act, 1961 the original cost of the asset was the same for accounting as well as taxation purposes.
Now we have to enumerate some divergence between AS-5 issued by ICAI and section 32 of income tax Act, 1961.
1- The basis for provision of depreciation as per this accounting standard (Depreciation Accounting) is the estimated useful life of an asset. However, under the Income-tax Act, the useful life of an asset is not relevant.

2- The accounting standard provides for allowance of depreciation on revalued amount in the case of revaluation. Under Income-tax Act, depreciation is allowed only on the written down value of block of asset. Revaluation is not recognized for income-tax purposes.

3- For the purpose of claiming depreciation under section 32, the asset, in respect of which the depreciation is claimed, must have been used for the purpose of business or profession. However, use of asset is not a pre-condition for provision of depreciation under AS-6.

4- Method of Depreciation As per Income Tax Act, 1961 (the Act) WDV (From A.Y. 1998-99, power sector units have an option to follow (SLM). As per Accounting Standard SLM / WDV for Companies. No restriction for non-corporate. (J. S. Lodha Auditorium, p 7)

5- Rates of Depreciation As per Income Tax Act, 1961 (the Act) I.T. Rules No specific provision for writing-off of small value assets, As per Accounting Standard Schedule XIV of Companies Act (Minimum rates). For others, as per statutes governing them, otherwise no restriction. Assets having actual cost less than Rs. 5,000/- to be written off fully subject to specific conditions in proviso

6- Concept of block of Assets I.T Defined in Sec. 2(11) but AS-6 Each asset is depreciated separately. There is no block concept.

7- Change in method according to I.T not allowed but according to AS-6 Allowed

8- Exchange of assets in I.T Net amount paid / received is adjusted to WDV and Depreciation is calculated on adjusted WDV. According to AS-6 New asset acquired is recognized at fair value or at net book value of asset exchanged and depreciation is charged on that value.

9- Asset retired from active use I.T Depreciation on WDV of the asset (in the block) allowed, AS-6 Depreciation is not allowed on such asset. It should be shown as Current Asset. It has to be stated at lower of their net book value and net realizable value. Any expected loss is recognized immediately in profit and loss account. (J. S. Lodha Auditorium, p 7)

10- Depreciation in the year of sale according to income tax Act, 1961 The sale proceeds will reduce the balance in block of assets. Hence, no depreciation is admissible. According to accounting standard No-6 Charged till date of sale.

Conclusion:- From aforesaid Depreciation between AS-6 issued by ICAI and section 32 of income tax Act 1961 is divergence more than convergence. Depreciation allowable in AS-6
and income-tax Act, the original cost of the asset was the same for accounting as well as taxation purposes, income-tax is following Schedule XIV of the companies Act, 1956 and Appendix-I-A of Income-tax Rules provide for depreciation rates, but according to depreciation AS-6 issued by ICAI, each company is free to follow the depreciation.

7- Accounting for construction contracts AS-7:-
This Accounting standard will be applicable to these assessees who are in the business of construction contract. AS-7 requires adoption of percentage completion method; and does not allow completed contract method. On the other hand, in IT, completed contract method is not prohibited, although in practice they insist on declaration of profit on percentage (progress) only. (J. S. Lodha Auditorium, April 10, 2010, p 9)
The method followed by the taxpayer cannot be called as an unreasonable method and any change in the method is revenue neutral. Further, the tax department cannot change the method of accounting which was accepted by it over the years.
The Tribunal observed that the Bangalore Tribunal in the case of Prestige Estate Projects (P) Ltd. held that the Government has not specified AS 7 in Section 145 of the Act and the taxpayer developer had been regularly, under a bonafide belief, employing Project Completion Method which is an accepted method of accounting. Accordingly, the AO cannot reject the accounts of the taxpayer under Section 145(3) of the Act.

- The Tribunal relied on the decision of the Mumbai Tribunal in the case of Champion Construction Co. and held that it would be appropriate to offer income tax in the year in which 80% of the construction was completed. Since the taxpayer admittedly completed only 53.95 percent of the construction it cannot be said that the taxpayer has substantially completed the project so as to recognize income under the Project Completion Method of accounting.

- The Tribunal also relied on the decision of the Bombay High Court in the case of CIT v. Tata Iron & Steel Co. Ltd. where it was held that the method of accounting followed by the taxpayer company cannot be said to be unreasonable, and that in such a case, even if a better method could be visualized, the method consistently followed should be accepted.
• Accordingly, the Tribunal allowed the taxpayer’s contention to follow Project Completion Method and recognize the revenue accordingly in the year of project completion. The Tribunal refrained from deciding as to whether any revenue has to be recognized in the relevant assessment year based on the Guidance Note issued by ICAI considering the agreement to sale entered into by the taxpayer. (http://taxguru.in/income-tax-case)

Completed contract method, it is highly debatable whether one can adopt cash basis of IT and accrual basis for other purposes. For corporate; Sec. 115JB comes in the way as it considers accounts as laid before the AGM of a company. In respect of retention money also, the AS 7 and IT are at a variance.

“Contract costs comprise, inter alia, of costs that are attributable to the contract activity in general and are allocated to the particular contract. The permissible cost which can be included in this category is borrowing costs, the Madras High Court, in CIT v. s.i property Development (p) ltd. (2004) 135 taxman 235 has applied AS-7 for including interest in project cost for tax purpose. Further, it appears that the percentage of completion method required to be adopted as per AS-7 will be adequate for tax purposes also” ( inter-relationship between AS and taxation, p5, without name)

Conclusion:- AS-7 requires adoption of percentage completion method; and does not allow completed contract method. On the other hand, in IT, completed contract method is not prohibited, although in practice they insist on declaration of profit on percentage (progress) only.

8- Accounting for Research and Development AS-8:-
This Accounting standard has been withdrawn w.e.f 1-412004

9- Revenue Recognition AS-9:-
This Accounting standard deals with the recognition of revenue arising in the course of the ordinary activities of the enterprise from the sale of goods or by way of rendering of services and by source like interest, royalty and dividends. This standard provides that revenue recognition should be postponed if there is significant uncertainly regarding collectability.

Various judicial authorities in the country, including the Supreme Court of India, have recognized the accounting principles laid down by the ICAI while deciding various disputes, particularly tax disputes and reiterated that the Institute is the authoritative body in the matter of laying down accountancy standards and accounting principles.(P.N.Shah,p 72)
This principle has been recognized for tax purpose also by the Supreme Court in the case of UCO Bank v.CIT237 ITR 889, where it was held decision of the Allahabad High court in CIT v. U.P. Financial corporation (2005) 143 taxman 47 that interest accrual should be postponed where suits for recovery of interest-bearing loans are pending. This is also in consonance with this principle enunciated in AS-9. Presently dividend income is exempt, hence this may not have any practical implication. Section 145 of the Income-tax Act provides that the income of an assessee under the head” profits and gains of business or profession” shall be computed in accordance with the assessee. However, in case of Kedarnath Jute Mfg.co.ltd .CIT (82 ITR 363) Supreme Court has held that the entries in the books of account will not determine the issue whether a particular expenditure is allowable or not. Similarly, if income is earned but not credited to tax in the year in which it is earned. (P.N.Shah, p 72) The year of accrual is important for determination of income, both under the true and fair view concept as well as for arriving at taxable income. The accounting standard based on concepts of prudence exclude from income certain items not certain of realization.

“Further in a recent and interesting case of CIT vs, Elgi Finance Ltd (2007) 293 ITR 357, the Hon’ble Madras High Court dealt with recognition of interest on “non performing assets” (NPA). It was held that the assessee had not recognized any income from the non performing asset and this treatment was in consonance with the Notification of RBI and AS 9 issued by the ICAI. Therefore the assessee was justified in not recognizing the interest from NPA. Hence, while deciding the issue the Court had very well taken AS – 9 into consideration.”(CA. C.N. Vaze, p 9, April 10, 2010)

Conclusion:-The accounting standard-9 based on concepts of prudence exclude from income certain items not certain of realization. This standard provides that revenue recognition should be postponed if there is significant uncertainly regarding collectability. This AS-9 has been recognized in many cases in front of the judge that means Income-tax Act 1961, has been recognized Accounting standard (Revenue Recognition-9)

10- Accounting for fixed assets AS-10:-

The Account standard requires capitalization of all assets, which are ready for their intended use. The income-tax Act, 1961 permits depreciation on assets used. The Accounting standard permits revaluation of assets. The Income- Tax Act, 1961 does not recognise revaluation.
Profits on sale of assets as reflected in the books in compliance with Accounting standard are significantly at variance with the profit as computed as per the provisions of Section 46 and Section 50 of the income tax Act (Jayant Gokhale, aug 2010, p11)

As per this standard, profit/loss on sale of fixed assets carried at historical cost has to be credited/charged to profit and loss account. As per the Income-tax Act, in respect of sale capital assets, capital gains/loss arises. In case the capital asset is a long term capital asset, benefit of indexation is available and the indexed cost is reduced from the net set consideration to arrive at the capital gains.

In respect of sale of depreciable assets, the entire sale proceeds have to be reduced to arrive at the written down value, where the block continues to exist. In case the block ceases to exist, the resultant figure would be a short-term capital gains/loss. Therefore, under the income-tax Act, profit/loss on sale of capital assets is not considered as business income/business loss.

Conclusion:– The Accounting standard-10 permits revaluation of assets. The Income- Tax Act, 1961 does not recognise revaluation. As per AS-10, profit/loss on sale of fixed assets carried at historical cost has to be credited/charged to profit and loss account. As per the Income-tax Act, in respect of sale capital assets, capital gains/loss arises.

11 – The effect of changes in foreign exchange rate AS-11 :-

An exchange rate based on the date of the transaction is used for this computation and the procedure prescribed under AS 11 is entirely different from rule prescribed under the Income Tax Act.

AS- 11 does not permit capitalization of exchange differences. However, Sec. 43A of IT is different. If due to devaluation, the liability in respect of moneys borrowed for purchase of machinery goes up, it should add to the cost of fixed assets.

As per AS-11, exchange differences relating to a liability incurred for the purpose of acquiring fixed assets, which are carried in terms of historical cost, cannot be adjusted in the carting amount of the respective fixed assets. The exchange difference has to be charged to profit and loss account. However, section 43A of income-tax requires such exchange differences to be adjusted against the actual cost of the asset. Such adjustment has to be made in the year in which the actual payment is made irrespective of the method of accounting followed by the assesssee.
“Accounting Standard 11 issued by the Institute of Chartered Accountants of India on accounting for exchange rate differences as well as the corresponding international accounting standard, require that there should be any increase or decrease in the liability on the balance-sheet date in terms of the reporting currency in respect of a loan taken for purchasing a fixed asset or in respect of supplier's credit for that purpose. Such liability must, as the case may be, revised upwards or downwards. Any increase in such liability, according to the standards, must be matched by increasing the actual cost of the fixed asset and any decrease in such liability must be matched by a reduction in the actual cost of the fixed asset. Even the AS-11 does not call upon businesses to make immediate adjustments to actual cost; it only calls for year-end adjustments. AS-11's mandate in this regard is unexceptionable. The rupee liability in respect of transactions entered into in other currencies must reflect the value of the rupee on the balance-sheet date. But Section 43A is not concerned with the disclosure aspects of accounting. Its focus instead is on ensuring accurate recording of the actual cost of fixed assets so that depreciation is charged appropriately and capital gains are computed correctly” (M. Sathya Kumar, p1, 18 Feb 2008).

Ditto in the Bombay High Court verdict in Padamjee Pulp & Paper Mills Ltd vs CIT (1994 210 ITR 97) as well as in the Calcutta High Court verdict in Bestobell (India) Ltd vs CIT (1979 117 ITR 789). All these verdicts for good measure set store by the fact that the assessee maintained their accounts on mercantile basis in terms of which a liability or right must be recorded immediately on its happening.

Conclusion: - Foreign exchange rate according to AS -11 is entirely different from Rule prescribed under the Income Tax Act. AS-11 does not call upon businesses to make immediate adjustments to actual cost; it only calls for year-end adjustments, section 43A of income-tax requires such exchange differences to be adjusted against the actual cost of the asset. Such adjustment has to be made in the year in which the actual payment is made irrespective of the method of accounting followed by the assessee.

12- The Accounting for Government Grants AS-12:-

The accounting standard requires that if the Government Grant relates to specific fixed assets it should be reduced from the gross block alternatively. It can be treated as deferred income in the P&L a/c on rational basis over the useful life of the depreciable asset.
Grant related to non-depreciable asset should be generally credited to capital reserve unless it stipulates fulfillment of certain obligation. In the later case, the grant should be credited to the P&L a/c cover for a reasonable period.

“The deferred income balance is to be shown separately in the balance sheet. If it is related to revenue, it must be recognized systematically in the P&L a/c. The tax departments also have the similar view and this accounting standard by far is the simplest and least controversial” (Gupta, May2007, p 302)

This standard provides that the accounting treatment would depend on the nature and purpose of the grant. The Madhya Pradesh high court, in shreejee chitra Mandir v. CIT (2004) 275 ITR 055, Observed that question of whether a particular subsidy is a capital receipt or a revenue receipt for income-tax purposes has to be decided keeping in view the nature of subsidy received by the assessee, and the scheme pursuant to which the same has been received. In other words, it is obligatory upon the taxing authorities examine the nature of subsidy and the object of the scheme pursuant to which it has been received by the assessee, before they record a finding one way or the other. This decision is in consonance with AS-12 (Inter-relationship between accounting and taxation, p 12.6) (2000) 245 ITR 9 CIT vs. Chhindware Fuels(Cal.) of 18-4-2000. The assessee received government subsidy in the form of sales tax refund after production commenced and hence not a capital receipt, not exempt from tax following.

If condition attached subsidy cannot be fully reduced from the cost as per accounting standard -12, it is to be reduced from Cost of asset for income tax depreciation computation (Chinnsamy Ganesan, A study on the application of Relevant Accounting Standards, 21.08.2010)

Conclusion:- If the Government Grant relates to specific fixed assets it should be reduced from the gross block alternatively, it can be treated as deferred income in the P&L a/c on rational basis over the useful life of the depreciable asset. The tax departments also have the similar view and this accounting standard by far is the simplest and least controversial

13- Accounting for investmwntAS-13 :-

This Accounting standards deals with accounting for investment in the financial statement of enterprise and related disclosure requirement, there is divergence between AS-13 and income tax provisions Act, 1961, While AS have gone by concepts of prudence and
conservatism, the treatment under the Income Tax Act takes into account only crystallized losses.

As per this standard, long-term investments should be carried at cost, provision should be made to recognize a decline other than temporary in the value of long-term investment. Such reduction should be determined and made for each investment individually. However, under the Income-tax Act, there is no provision to recognize a decline in the value of investment. Only if the investments are disposed off, the profit/loss on account of the same is recognized. In Kerala Small Industries Development Corporation Ltd .v. CIT (2004) 270 ITR 0452, the assessee had written off Rs.80 lakhs, representing investment in shares of co-operative societies, in its profit and loss account considering the fact that said co-operative societies were either defunct or under liquidation. The High Court observed that any loss on shares representing investment of the assessee cannot be termed as trading/revenue loss.

This accounting standard requires that, whenever investments are purchased cum dividend or cum interest and the dividend or interest is subsequently received, the same should be reduced from the cost of investment.

The absence of an exactly similar provision in the income tax Act, 1961 used to result in what is called as “dividend stripping”. AS provides that carrying cost of a part of holding of investment shall be calculated on the basis of average carrying amount of total holding but income-tax Act,1961 does not permit such averaging, while calculating capital gain tax. It takes cost based on specific identification.

AS requires investment to be stated at cost or market value whichever is lower. However, the provision for fall in value is not an allowable seduction under the income-tax Act,1961 and where such investment are held as stock-in-trade, capital loss is allowed only when realized.(Gupta. P303.2007)

Conclusion:- The divergence between AS-13 and income tax provisions Act, 1961 are much While AS have gone by concepts of prudence and conservatism, the treatment under the Income Tax Act takes into account only crystallized losses and income tax Act 1961, doesn’t recognize previson for fall in value of investments.
Accounting for Amalgamation AS-14:-

Accounting Standard-14 recognises the amalgamation to be in the nature of merger accounting for under pooling of interest method or in the nature of purchase accounting for under purchase method.

The following conditions have to be satisfied to classify a transaction as an 'amalgamation' under the Act. Section 47(vi) and 47(vii) of the Income-tax Act, 1961 and Section 2(1B) of the Income-tax Act, 1961.

Income-tax Act, 1961 vide section2(1B), defines amalgamation as the merger of one or more companies with another company or the merger of two or more companies to form a new company. The Income-tax Act, 1961 is tax neutral in the case of such amalgamation.

As per this standard, amalgamation expenses incurred by the transferee company should be debited to profit and loss account where the amalgamation is in the nature of merger and to Goodwill/Capital reserve account where the amalgamation is in the nature of purchase.

Under section 35DD of the income-tax Act, deduction of one-fifth of such expenditure is allowed for five successive previous years, beginning with the previous year in which amalgamation takes place. Further, the Income-tax Act does not distinguish between amalgamation in the nature of merger and amalgamation in the nature of purchase. (Inter-relationship between accounting and taxation.)

Accounting standard requires 90% of the shareholders of the transferor company must become shareholders in the transferee company where as under Income-tax Act, 1961 the filter is restricted at 75% only. The Accounting standard requires that the business must be continued and the transaction must be recorded at book value. The Income-tax Act does not have such requirements.

Conclusion: Point of view of accounting standard -6 is different from of view point of income tax Act 1961, in Amalgamation between companies, from that one angle. According to AS-14 expenses for amalgamation should be debited to profit and loss account, but under section 35DD of Income-tax Act, deduction of one-fifth of such expenditure is allowed for five successive previous years, second AS-14 requires 90% of shareholders of the transferor company must become shareholders in the transferee company, whereas under Income-tax Act, 1961 the filter is restricted at 75% only.
15- Accounting for retirement Benefits AS-15:-

The following are the retirement benefits as per accounting standard-15.

(a)- Provident fund
(b)- Superannuation/pension
(c)- Gratuity
(d)- Leave Encashment benefit on retirement
(e)- Other Retirement Benefits

In respect of the above retirement benefits, the requirement of clause 16: employee oriented items, clause17 (i): provision for payment of gratuity not allowable under section 40A (7) and Clause 21: taxes and other dues of form No. 3CD is to be examined and reported. The standard (AS 15) treats such items as revenue expenditure. (Gupta,p304)

AS-15 treats such items as revenue expenditure. The related cost is based on actuarial valuation. Every variation in the estimated liability as on cutoff date is required to be charged as a revenue expenditure of the respective year in which such liability is determined

The accrual basis of accounting is prescribed under this accounting standard for accounting of retirement benefits like provident fund and gratuity. However, as per section 43B of the Income-tax Act, deduction is allowable only on the basis of actual payment in respect of employer's contribution to any provident fund or superannuation fund or gratuity fund or any other fund for the welfare of employees.

The assessee should have actually paid these amounts on or before the due date for furnishing the return of income section 130(1) to claim the deduction during the previous year of accrual.

Thus, the following provisions of the Income tax Act,1961 would govern the allowance of some of the items of expenditure in relation to retirement benefits incurred by employers:

Section 36(1)(iv) this section deals with the allowance of contributions to a recognized provident fund or an approved superannuation fund. As per this section “any sum paid” by way of contribution is allowable.

Section36(1)(v): this section provides for an allowance for any sum paid by way of contribution to an approved gratuity find.

Section 40A(7): As per this section, provisions made in the accounts for payment of gratuity are not allowable except in two specific cases, namely:

a- Provision made for contribution to an approved gratuity fund
b- Provision made for payment of gratuity that has become payable during the relevant previous year. Section 43B provides that sums payable towards contribution to an approved gratuity fund would be allowable only on actually payment basis. (Yogesh Thar, June 2001, p 99)

Accounting standard-15 requires gratuity liability and leave encashment to be provided in the accounts on a year to year, whereas section 40A(7) of the income-tax Act specifically provides that such liability shall not be an admissible deduction, unless gratuity paid and section 43B permits deduction for leave encashment only when actually paid and not otherwise.

As per Para 2(d) of AS-15 “leave encashment benefit on retirement” thus, an employer is obliged to make a provision in its accounts in respect of accrued liability towards leave encashment of its employees based on an actuarial valuation of such liability. There is no specific provision in the Act to deal with the allowance or disallowance of such a provision.

Conclusion:- There is divergence between AS-15 Accounting for retirement Benefits and income-tax Act, 1961, whereas AS-15 treats items as revenue expenditure, but according to Income-tax Act, 1961, as per section 43B of the Income-tax Act, deduction is allowable only on the basis of actual payment in respect of employer's contribution to any provided fund or superannuation fund or gratuity fund or any other fund for the welfare of employee.

16- Borrowing cost AS-16:-
The related issues that arise in the treatment of borrowing cost especially when it relates to acquisition of assets which take substantial time to complete or acquire. The intention in introducing the Proviso in Section 36 (1) (iii) seems to be two fold:

a) To limit the allowance of expenditure in regard to borrowings for acquisition of assets only from the date that such assets are put to use.

b) To prevent situations where interest was capitalised in the books, but claimed as revenue expenditure for computation of income.

As per this standard, borrowing costs that are directly attributable to the acquisition, construction or production of a qualifying asset should be capitalized as of the cost of that asset.

Qualifying asset is an asset that necessarily takes a substantial period of time to get ready for its intended use or sale e.g. manufacturing plants, power generation facilities. Other
borrowing costs should be recognized as an expense in the period in which they are incurred and charged off to profit and loss account.

Under the Income-tax Act, interest in respect of capital borrowed for acquisition of a new asset for expansion of existing business or profession for any period from the date of borrowed to the date on which the asset was first put to use should be capitalized. Explanation 8 to section 43 (1) clarifies that interest relatable to a period after the asset is first put to use cannot be capitalized. Such interest would be allowed as deduction under section 36(1), if the capital is borrowed for the purposes of business or profession.

The accounting standard requires that, income on the temporary investment of the borrowed funds be deducted from the borrowing cost. The Income-tax Act, 1961, however, levies tax on income earned during this intervening, period. In such case if the income is disclosed u/s 56 as income from other sources, then attributable interest expenses for that period can be claimed u/s 57(iii)(Gupta,p304)

Although the intention seems to be to bring the tax treatment of interest in line with the principles prescribed in AS 16 divergence arises because of the following reasons.

1- Literal reading of the Act would indicate that the proviso applies irrespective of whether an asset takes significant time to acquire or construct. As such, the concept of “qualifying asset” as referred to AS 16 is not recognised under the Income Tax Act

2- The cut offs for the period up to which capitalisation is to take place are different under AS and Income Tax Act. While AS recognises the possibility of suspending capitalisation during the periods when development of the assets is interrupted; there is no such provision in the Income Tax Act.

3- Every standard is always subject to the concept materiality and therefore, such capitalisation in regard to non-material items cannot be invoked under the Standard. However capitalisation would automatically apply under the Income Tax Act resulting in computational difficulties

4- The Proviso introduced in the Act refers to assets being part of “extension of existing business or profession”. AS 16 however, does not put such precondition. As a result there could be differences in application especially when projects are put up in phases where the issue of distinction between extension and integration could become relevant. (Jayant Gokhale, P12, Programme on Direct Taxes hosted by EIRC, Aug 2010)
Amount of borrowing has to be reported under clause 23: hundi loans and clause 24: loans and deposits accepted/ repaid during the previous year u/s 269SS and 269T of the form No.3CD.

Conclusion: According to AS-16 there are two types of borrowing, first borrowing costs that are directly attributable to the acquisition, construction or production of a qualifying asset should be capitalized as of the cost of that asset. Qualifying asset is an asset that necessarily takes a substantial period of time to get ready for its intended use or sale e.g. manufacturing plants, power generation facilities. Second borrowing costs should be recognized as an expense in the period in which they are incurred and charged off to profit and loss account. But Under the Income-tax Act, interest in respect of capital borrowed for acquisition of a new asset for expansion of existing business or profession for any period from the date of borrowed to the date on which the asset was first put to use should be capitalized. Explanation 8 to section 43 (1) clarifies that interest relatable to a period after the asset is first put to use cannot be capitalized. Such interest would be allowed as deduction under section 36(1), if the capital is borrowed for the purposes of business or profession. In the end there are similarities between AS-16 and income tax act in borrowing cost.

17- Segment report AS-17:-
This is merely a reporting standard. This standard established principle for reporting financial information, about different types of products and services an enterprise produces and the different geographical areas in which it operates. The Accounting standard also provides that interest on overdraft may not be allocated to any specific segment. Under the Income-tax Act, tax is payable for an assessee on the "total income" as defined in section 2(45) read with section 5 of the Act and not on the basis of segment. . (Gupta. P305.2007)

18- Related party disclosure AS-18
The objective of this standard is to establish requirement for disclosure related party relationship and transaction between a reporting enterprise and its related parties.
This standard prescribed disclosure of related party relationship and transactions between a reporting enterprise and its related parties. It does not prescribe any accounting requirement. However, under Income-tax Act, a specific disallowance has been provided Under section 40A(2), Where the assessee incurs any expenditure in respect of which a payment has been
or is to be made to a relative or associate concern, so much of the expenditure as is considered to be excessive or unreasonable shall be disallowed by the assessing officer.

The AS focuses on control and ability to exercise significant influence. The income-tax Act, 1961 has in place its own section 40A(2)(b), which dealt with payments for expenditure to parties where there is substantial interests and the assessing officer has been given powers to disallow payments which in his opinion are more than the reasonable rates. The above fact should be kept in mind while reporting for clause 18: payment to specified person u/s 40A(2) of form No.3CD.

Conclusion: - AS does not prescribe any accounting requirement but under section 40A(2) of Income Tax Act 1961, Where the assessee incurs any expenditure in respect of which a payment has been or is to be made to a relative or associate concern, so much of the expenditure as is considered to be excessive or unreasonable shall be disallowed by the assessing officer. The provision of the Accounting standard covers more parties and transactions in their ambit as compared to income tax Act, 1961.

19- Accounting for leases AS-19 :-

The leases are classified into finance leases and operating leases as per standard. A finance lease is a lease that transfers substantially all risks and rewards incident to ownership of an asset, in operating lease, only the right to use the asset is transferred.

Depreciation on leased asset is allowed as per AS-6 in the hands of the lessee in case of a finance lease. However, this Accounting standard will have no implication on the allowance of depreciation on assets under the provision of the income-tax Act. The owner of asset is entitled to depreciation under section 32 of the Income-tax Act, if the asset is used in this business.

The income-tax Act, 1961 does not recognize the right of the lessee in financial leases to claim ownership of the asset and correspondingly claim depreciation thereof. This has been clarified by CBDT circular No.2 dated 9.2.2001. Lease rentals from finance lease are apportioned between finance income and reduction of lease receivable to the profit and loss account whereas the full rental is treated as income for tax purposes. Similarly, in the books of the lessee, lease rental is apportioned between finance charges and reduction of liability. Only the finance charges are debited to the profit and loss account whereas the full lease rental is deductible for tax purposes.
As per AS-19, lease income from operating leases should be recognized in the profit and loss account on a straight line basis over the lease term even if the receipts are on such basis. However, for income-tax purpose, such lease income is recognized on cash/mercantile basis, depending on the method of accounting regulator followed by the assessee.

Conclusion:- Depreciation on leased asset is allowed as per AS-6 in the hands of the lessee in case of a finance lease. The owner of asset is entitled to depreciation under section 32 of the Income-tax Act, if the asset is used in this business. The income-tax Act, 1961 does not recognize the right of the lessee in financial leases to claim ownership of the asset and correspondingly claim depreciation thereof. As per AS-19, lease income from operating leases should be recognized in the profit and loss account on a straight line for income-tax purpose, such lease income is recognized on cash/mercantile basis, depending on the method of accounting regulator followed by the assessee.

20- Earning per share AS-20:-
This is a reporting standard and has no tax implication. Earning per share is a financial ration that gives the information regarding earning available to each equity share. The standard prescribed principles for the determination and presentation of earning per share.
Conclusion: AS-20 has no tax implication

21- Consolidated Financial Statements AS-21:-
The consolidated financial statements are intended to present information about a parent and its subsidiary as a single economic entity. Tax under Income-tax Act, 1961 is still levied on the holding company and its subsidiary separately, since each is a separate taxable entity.
Conclusion: This standard also has no tax implication.

22- Accounting for Taxes on Income AS-22:-
Taxes on income are normally accrued in the same accounting period to which the revenue/expense is related in view of matching concept. In a number of cases, taxable income may be significantly different from the accounting income. The purpose of this standard is to match the taxes on the income as per books of account and as per the income tax law. For this purpose, deferred tax asset or deferred tax liability is provided in the accounts.
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“Accounting standard 22 on accounting for taxes on income is a standard which will normally impact profit for the year and earnings per share without there being any impact on actual tax liability which is governed by provisions like section 40, section 40A and section 43B of the Income tax Act, 1961. Hence, there is no tax implication while applying Accounting standard 22” (Jayesh Thakur, income tax review, p136)

On the first occasion taxes on income are accounted for in accordance with this standard, the opening balances of assets and liabilities for accounting purpose and for tax purpose are compared and the differences, if any, are determined. The tax effects of these differences, if any, should be recognized as deferred tax assets and liabilities, if these differences are timing differences.

A provision for deferred tax while reducing the distributable profit does not reduce the taxable profit (no concept of deferred tax under the IT Act). Even for the purpose of computing book profit u/s 115JB, deferred tax may need to be added back.(Gupta, p307)

Conclusion: there is no tax implication.

23- Accounting for investment in associates in consolidated financial statements AS-23:-

This accounting standard was formulated with the objective to set out the principle and procedure for recognizing the investment with association in the consolidated financial statements of the investor, so that the effect of investment in associates on the financial position of the group is indicated. There is no implication on income tax, since associate entities are separate taxable entities.

24- Discontinuing operation AS-24:-

Accounting standard -24 is a Reporting or a Disclosure standard. It does not affect the quantum of income or assets reported in the financial statements and tax thereon. For revenue authorities, this disclosure can be a source of enquiry, although it would not have any direct tax implication.

25- Interim financial Reporting (IFR) AS-25:-

Interim financial reports (IFR) are financial statement for an interim period that is shorter than a full financial year. This standard prescribes the minimum contents of an interim
financial report and prescribed the principle for recognition and measurement in a complete or condensed financial statement for an interim period. This also does not have any tax implication.

26- Intangible Assets AS-26:-
This standard prescribes the accounting treatment for intangible assets, without physical substance, held for use in the production or supply of goods or services for rental to others or for administrative purposes.
This standard requires an enterprise to recognize an intangible asset, if certain criteria are met. The statement also specifies how to measure the carrying amount of intangible assets and requires certain disclosures about intangible assets.
“Intangible assets like intellectual property rights are assuming greater and greater Importance. Income Tax Act also started allowing depreciation on such assets. However, the principles of capitalization stated in AS 26 are significantly different than those prevailing in IT” (J. S. Lodha. Auditorium, , April 10, 2010, p 10)
Income-tax Act, 1961 has recognized the existence and ownership of intangible assets such as knowhow, patents, copyrights, trade markets, business franchises or any other business or commercial rights of a similar nature [section 32(1)] and has provided for systematic claiming of depreciation thereon at 25%. The Accounting standard also recognizes intangible separately.
The Accounting standard has permitted amortization of expenditure incurred under VAS. The income-tax Act, 1961 also permits write off over 5 years ( section 35DDA-Amortisation of Expenditure under voluntary Retirement scheme)
Conclusion: There are similarities between AS-26 and income-tax Act, 1961. Income-tax Act, 1961 has recognized the existence and ownership of intangible assets and has provided for systematic claiming of depreciation thereon at 25% every year. The Accounting standard also recognizes intangible assets and has permitted amortization of expenditure incurred under VRS.
27- Financial reporting of interest in joint ventures AS-27:-

This standard sets out the principles and procedures for accounting for interest in joint venture and reporting of joint venture assets and liabilities, income and expenses in the financial statements of ventures and investors.

This standard is also reporting standard, with no tax implication.

28- Impairment of Assets AS-28:-

Almost all accounting done for financial reporting purposes is “Historical cost Accounting” the values of assets do not reflect their correct market values. To rectify this, accounting standard -28 provides that eligible assets are checked for any impairment in their reporting values and this impairment is provided for out of the earnings of the enterprise.

As per this standard, if the carrying amount of an asset exceeds its recoverable value, the excess is impairment loss. Such loss be provided for in the statement of profit and loss. It must be noted that impairment provision is in addition to the depreciation provided as per AS-6. However, there is no such provision for impairment loss under the income-tax law.

“AS 28 makes it mandatory to provide for impairment in the value of fixed assets. The Minimum Alternate Tax (MAT) provisions under Income Tax Act, 1961 provide for making certain adjustments to the profit as shown in Profit and Loss Account to arrive at the book profits. Earlier, it was held by the Supreme Court in the case of CIT V. HCL Comnet Systems and Services Ltd. 305 ITR 409 (SC) that diminution in the value of assets need not be added to the profits for the purpose of computing book profits. However, to overrule this decision, recently the Finance Act 2009 added an explanation to provide that even diminution in the value of assets should be added back to compute book profits. Consequently, in the present scenario, it is necessary to add back the provision made for impairment of assets” (CA. C.N. Vaze,PN10,11, April 10, 2010)

The Accounting standard requires recognition of losses from impairment of assets, but under Income-tax Act, 1061 these losses can be claimed only when realized.

For a company which is charged under MAT u/s 115JB, such debit to the account is not for the purpose of meeting any liability, hence should be deducted from book profit.

Conclusion: According to AS-28 if the carrying amount of an asset exceeds its recoverable value, the excess is impairment loss. Such loss be provided for in the statement of profit and loss. It must be noted that impairment provision is in addition to the depreciation provided as
per AS-6. This provision is not recognized in income tax Act, 1961 and should be added back to profit and loss account for being taxable.

29- Provision, contingent liabilities and contingent assets AS-29.

The objective of this statement is to ensure that appropriate recognition criteria and measurement bases are applied to provisions and contingent liabilities and that sufficient information is disclosed in the notes to the financial statements. The objective of this accounting standard is also to lay down appropriate accounting for contingent assets. Contingent liability and contingent asset will not have any direct effect on the income tax matters. Contingent liabilities are not recognized in the accounts only to be disclosed by way of a suitable note in the financial statements. Contingent assets are neither recognized nor required to be disclosed in the financial statements. Provision made, based on this accounting standards may not be allowed as deduction under Income-tax Act, 1961.

Conclusion: Provision made, based on this accounting standards may not be allowed as deduction under Income-tax Act, 1961

Conclusion:-

As mentioned in the beginning of this Chapter that, tax audit u/s 44 AB will not be away from implication of accounting standards issue by ICAI, also in the same time not all accounting standards implication in tax audit. We also found that, there are four areas, where the Income tax Act 1961, provisions and the accounting standards supplement and support each other, area where the two have some convergence ,area where the two deal with subjects which do not directly affect each other because some of accounting standards are not recognized under income tax Act 1961, and some area which affect certain common subjects but one sees divergent approaches between the two, In the end we find that Implication of accounting standards to tax audit u/s 44 AB may be broadly classified into four categories.

Category 1- First category is corresponding with slight divergence between income tax provision under section 145 and accounting issued by ICAI. IT has recognized and prescribed only two AS in terms of Sec. 145. There are two accounting standards similarities with income tax AS, first is: - AS (IT)-1 conformity with AS-1(disclosure of accounting
policy) issued by ICAI and second is: - AS (IT) -2 prior period and extraordinary items and changes in accounting policies with AS -5(net profit or loss for the period prior period items and change in accounting policies) issue by ICAI.

Category 2- Second category is convergence between income tax Act, 1961 provisions and AS issued by ICAI.

AS-9 This standard provides that revenue recognition should be postponed if there is significant, Revenue Recognition AS-9 uncertainly regarding collectability Various judicial authorities in the country, including the supreme court of India, have recognized the accounting principles laid down by the ICAI while deciding various disputes, particularly tax disputes.

The Accounting for Government Grants AS-12, Government Grant relates to specific fixed assets it should be reduced from the gross block alternatively, it can be treated as deferred income in the P&L a/c on rational basis over the useful life of the depreciable asset. The tax departments also have the similar view and this accounting standard by far is the simplest and least controversial. Borrowing cost AS-16 as per this standards (the AS-16) borrowing cost that is directly attributable to the acquisition, construction or production of a qualifying asset should be capitalized till the completion of substantial activities, the Income tax Act, has a similar provision u/s 36(1) (iii) acquisition interest on capital borrowing for extension of existing business to be capitolised till the asset is put to use and shall not be allowed as deduction. According to income tax Act, Interest relatable to a period after the asset is first put to use cannot be capitalized. Such interest would be allowed as deduction under section 36(1), if the capital is borrowed for the purposes of business or profession. Other borrowing cost should be recognized as expenses.

Accounting for leases AS-19 Depreciation on leased asset is allowed as per AS-6 in the hands of the lessee in case of a finance lease. The owner of asset is entitled to depreciation under section 32 of the Income-tax Act, if the asset is used in this business.

Intangible Assets AS-26 both this accounting standard and income tax Act are recognized by intangible assets amortization.

Third category divergence, AS-2(Valuation of Inventories) recognises exclusive method of inventory valuation whereas section 145A of the income- tax Act prescribes inclusive method of inventory valuation. Contingencies and events occurring after the balance sheet date AS-4, the contingent loss should be provided for on the basis of the nature of
probability of occurrence and possibility of reasonable estimate but Sec. 115JB, the provisions made for meeting unascertained liabilities are to be added back. Depreciation Accounting AS-6, - Change in method according to I.T not allowed but according to AS-6 Allowed, depreciation according to income-tax is following Schedule XIV of the companies Act, 1956 and Appendix-I-A of Income-tax rules, but depreciation according to AS-6 issued by ICAI, each company is free to follow the depreciation. Accounting for construction contracts AS-7, AS-7 requires adoption of percentage completion method; and does not allow completed contract method. On the other hand, in IT, completed contract method is not prohibited, although in practice they insist on declaration of profit on percentage (progress) only.

Accounting for fixed assets AS-10 The Accounting standard-10 permits revaluation of assets. The Income- Tax Act, 1961 does not recognize revaluation. As per AS-10, profit/loss on sale of fixed assets carried at historical cost has to be credited/charged to profit and loss account. As per the Income-tax Act, in respect of sale capital assets, capital gains/loss arises. The effect of changes in foreign exchange rate AS-11 according to AS -11 is entirely different from Rule Prescribed under the Income Tax Act. AS-11 does not call upon businesses to make immediate adjustments to actual cost; it only calls for year-end adjustments, section 43A of income-tax requires such exchange differences to be adjusted against the actual cost of the asset.

Accounting for investment AS-13 While AS have gone by concepts of prudence and conservatism, the treatment under the Income Tax Act don’t takes this principal, income tax Act takes into account only crystallized losses. As per this standard, long-term investments should be carried at cost provision should be made to recognize a decline other than temporary in the value of long-term investment. Such reduction should be determined and made for each investment individually. However, under the Income-tax Act, there is no provision to recognize a decline in the value of investment.

Accounting for Amalgamation AS-14 according to AS-14 expenses for amalgamation should be debited to profit and loss account, but under section 35DD of Income-tax Act, deduction of one-fifth of such expenditure is allowed for five successive previous years, second AS-14 requires 90% of shareholders of the transferor company must become shareholders in the transferee company, here as under Income-tax Act, 1961 the filter is restricted at 75% only.

Accounting for retirement Benefits AS-15, there is divergence between AS-15 Accounting for retirement Benefits and income-tax Act, 1961, whereas AS-15 treats items as revenue
expenditure, but according to Income-tax Act, 1961, as per section 43B of the Income-tax Act, deduction is allowable only on the basis of actual payment in respect of employer's contribution to any provided fund or superannuation fund or gratuity fund or any other fund for the welfare of employee.-

Related party disclosure AS-18   AS does not prescribe any accounting requirement but under section 40A(2), Where the assessee incurs any expenditure in respect of which a payment has been or is to be made to a relative or associate concern, so much of the expenditure as is considered to be excessive or unreasonable shall be disallowed by the assessing officer.

Accounting for leases AS-19   the income-tax Act, 1961 does not recognize the right of the lessee in financial leases to claim ownership of the asset and correspondingly claim depreciation thereof. This has been clarified by CBDT circular No.2 dated 9.2.2001.

Intangible Assets AS-26 according to income tax Act amortization at 25% every year whereas AS amortization under VRS

Impairment of Assets AS-28 when asset exceeds its recoverable value, the excess is impairment loss and  impairment provision is in additional o the depreciation provided this provision is not recognize in income tax Act, 1961 and should added back to profit and loss account for taxable.

Provision, contingent liabilities and contingent assets AS-29 Provision, contingent liabilities are not recognized and not be allowed as deduction under Income-tax Act, 1961 Fourth category Income tax Act 1961 provisions don’t recognize (a reporting standard) Accounting standards issue by ICAI, such as Cash flow statement AS-3 This is a reporting standard, Segment report AS-17 this section related in capital gains, Earning per share AS-20, This standard also has no tax implication, Consolidated Financial Statements AS-21, : This standard also has no tax implication, Accounting for Taxes on Income AS-22 there is no tax implication, Accounting for investment in associates in consolidated financial statements AS-23 There is not implication on income tax, Discontinuing operation AS-24 There is not implication on income tax, Interim financial Reporting (IFR) AS-25 This also does not have any tax implication, Financial reporting of interest in joint ventures AS-27, This standard is also reporting standard, with no tax implication