NEWSLETTER

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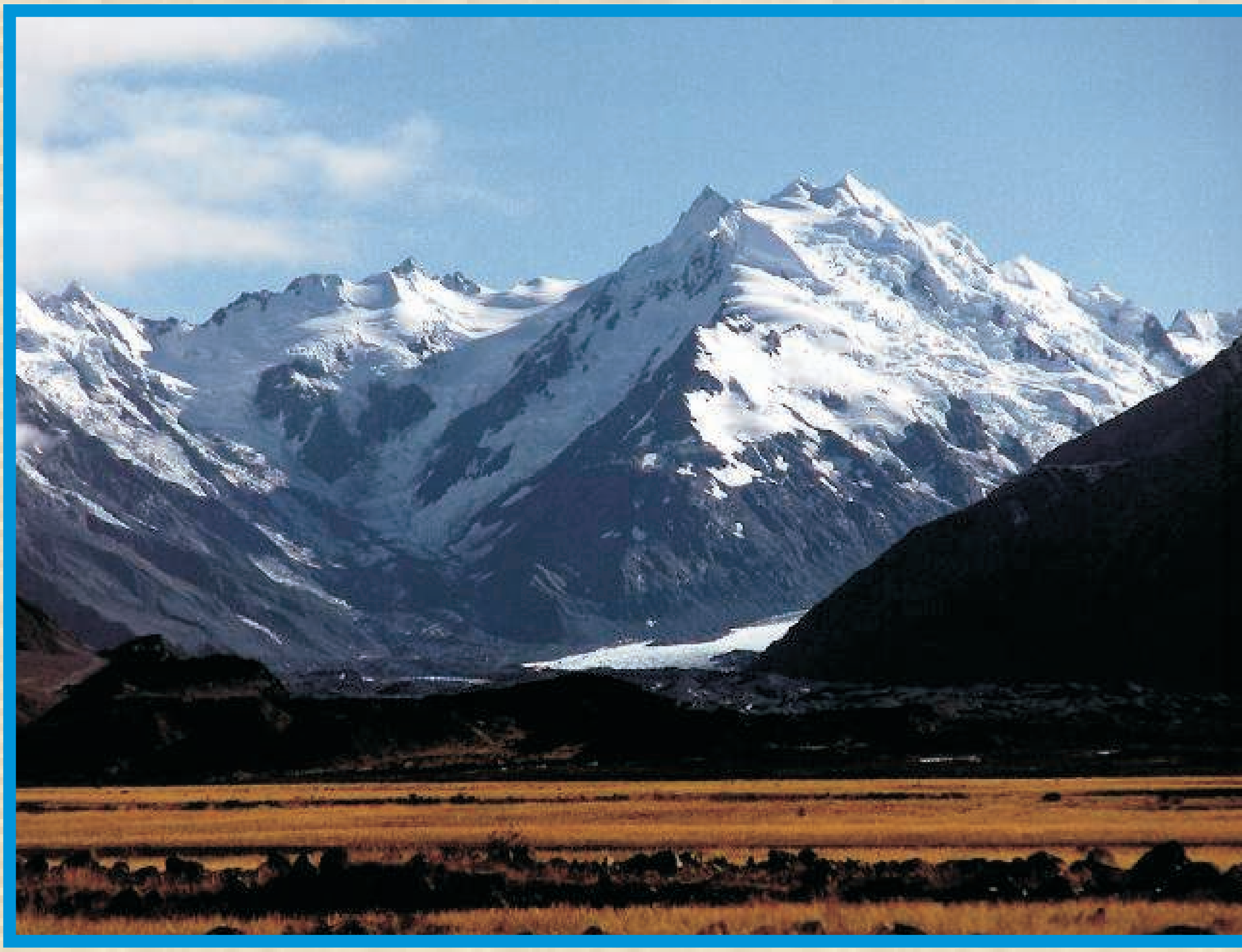

ASSURANCE & AUDIT

Tax Accounting Standard - Update

1.Brief:

Though the provisions of the Income Tax Act, 1961 ('the Act') govern the computation of taxable profits, the Act currently does not comprehensively specify accounting standards that should be followed for this purpose.

Even though the Finance Act, 1995 empowered the Central Government to notify such accounting standards, only two accounting standards on disclosure of accounting policies; and disclosure of prior period and extraordinary items and changes in accounting policies have been notified till date.

In the absence of such notified accounting standards under the Act, companies generally compute their taxable income following the same accounting principles and policies followed for the preparation of financial statements, subject to specific provisions of the Act and after considering various judicial pronouncements.

Over the last several years, the Institute of Chartered Accountants of India (ICAI) has issued several accounting standards and pronouncements, many of which have been notified by the Ministry of Corporate Affairs (MCA). Additionally, as a part of the convergence with International Financial Reporting Standards (IFRS), the MCA has placed thirty five converged standards (Ind AS).

In the absence of notification of accounting standards under the Act, in practice, uncertainty and litigation continues on various accounting related issues where the views of the tax authorities are not consistent with the provisions of the accounting standards and pronouncements of the ICAI or the MCA.

Further, in the absence of clarity around the tax impact of the transition to Ind AS, the MCA is yet to notify the final implementation dates for adoption of Ind AS.

2.Accounting Standards Committee constituted by the CBDT:

With the above background, in December 2010, the CBDT constituted an Accounting Standard Committee (the Committee) comprising of officers from the Income Tax department and other professionals. The terms of reference of this Committee are as follows:

- to study the harmonization of Accounting Standards issued by the ICAI with the direct tax laws in India, and suggest Accounting Standards which

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need to be adopted under section 145(2) of the Act along with the relevant modifications;

- to suggest method for determination of tax base (book profit) for the purpose of Minimum Alternate Tax (MAT) in case of companies migrating to IFRS (Ind AS) in the initial year of adoption and thereafter; and
- to suggest appropriate amendments to the Act in view of transition to IFRS (Ind AS) regime.

On 17 October 2011, based on the recommendation of the Committee, the Ministry of Finance issued a discussion paper on Tax Accounting Standards.

3. Key recommendations of the committee:

- The Accounting Standards issued by the ICAI cannot be notified without modifications as the requirements prescribed by these standards are not necessarily consistent with other specific provisions of the Act. The accounting standards to be notified under the Act should provide specific rules, which would enable computation of income with certainty and clarity. Further, such notified accounting standards should eliminate alternatives to ensure horizontal equity and uniformity. Accordingly, separate accounting standards should be notified under Section 145(2) of the Act. These separate accounting standards should be termed as 'Tax Accounting Standards (TAS)' to distinguish them from accounting standards issued by the ICAI or notified by the MCA;
- TAS should be made applicable only to the computation of taxable income and a taxpayer should not be required to maintain separate books of account on the basis of TAS;
- A reconciliation between the income as per the financial statements and the income as computed per the TAS should be required;
- Since the TAS are based on the mercantile system of accounting, the TAS should be applicable to only taxpayers who follow the mercantile system for tax purposes; and
- Since the TAS is intended to be in harmony with the provisions of the Act, it should be expressly provided in the TAS, that in case of conflict, the provisions of the Act shall prevail over the TAS.

If the recommendations in the discussion paper are eventually accepted and incorporated into the Act, taxable income would be computed based on provisions of the TAS irrespective of the accounting standards followed for the preparation of the financial statements.

This would partially address the issue relating to the impact of transition of Ind AS on taxation, as taxes payable (other than MAT) would be computed based on TAS irrespective of whether a company follows the currently applicable accounting standards or Ind AS.

Further, though taxpayers will not be required to maintain separate books of account per the TAS, they would need to maintain and present a reconciliation between the profits per the financial statements and per the provisions of TAS.

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4.Draft Tax Accounting Standards:

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 this 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.

A. TAS on Construction Contracts:

Significant differences between TAS on Construction Contracts and Construction Contracts (AS 7), are as follows:

1. The TAS mandates the use of the percentage of completion method for revenue recognition on construction contracts. Accordingly, use of completed contract method may no longer be permitted for tax purposes;

2. Even though the TAS permits non-recognition of margins during the early stages of a contract, it prohibits such deferral if the stage of completion exceeds twenty five percent;

3. Unlike AS 7, the TAS does not provide for recognition of expected losses on onerous construction contracts; and

4. The TAS precludes any incidental income in the nature of interest, dividend or capital gains from being reduced from the contract cost. However, incidental income, other than interest, dividend or capital gains can be reduced from the costs, if such income is not a part of the contract revenue.

Further, as the TAS is based on AS 7, the new concepts in Ind AS that may impact accounting for construction contracts (for example, discounting of retention receivables) have not been incorporated into the TAS. Accordingly, companies that transition to Ind AS may need to make certain additional adjustments to comply with the TAS.

B. TAS on Government Grants:

Significant differences between TAS on Government Grants and Accounting for Government Grants (AS 12), are as follows:

- The TAS does not permit the capital approach for recording government grants. Accordingly, the current practice of recording grants in the nature of promoters' contribution or grants related to non-depreciable assets, directly in shareholders' funds as a capital reserve will not be permitted under the TAS;

- Under the TAS, all grants will either be reduced from the cost of the asset; or recorded over a period as income; or recorded as income immediately; depending on the nature of the grant; and

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- Unlike AS 12, the TAS provides that the initial recognition of the grant cannot be postponed beyond the date of actual receipt. AS 12 specifically provides that mere receipt of a grant is not necessarily a conclusive evidence that conditions related to the grant will be fulfilled.

Further, as the TAS is derived from AS 12, the new concepts in Ind AS that impact accounting for government grants (for example, recognition of non-monetary grants at fair value) have not been incorporated into the TAS. Accordingly, companies that transition to Ind AS may need to make certain additional adjustments to comply with the TAS.

Compiled by: Mr. Bharat Jain

INFORMATION TECHNOLOGY

Cloud Computing - A Silver Lining or A Storm Ahead

Cloud Computing is a technology that uses the internet and central remote servers to maintain data and applications. Cloud Computing allows consumers and businesses to use applications without installation and access their personal files at any computer with internet access. This technology allows for much more efficient computing by centralizing storage, memory, processing and bandwidth.

It could be a lifeline for small businesses to keep costs down. Perhaps the most confusing thing about cloud computing is that you are very likely already doing it. For instance, if you have a web-based email account through Gmail, Yahoomail or Hotmail, you are a cloud computing veteran. If you have uploaded photos on Picasa, created a Google Doc or posted something on Facebook, you're a cloud computing pioneer.

A cloud can be private or public. A public cloud sells services to anyone on the Internet. (Currently, Amazon Web Services (AWS) is the largest public cloud provider.) A private cloud is a proprietary network or a data center that supplies hosted services to a limited number of people. When a service provider uses public cloud resources to create their private cloud, the result is called a virtual private cloud. Private or public, the goal of cloud computing is to provide easy, scalable access to computing resources and IT services.

CLOUD SERVICE MODELS

Cloud Service Models simply mean what type of services can be provided to customers. Different models cater to different kinds of requirements, and can achieve different business objectives. There are in all 3 different types of service models at present:

- SaaS (Software as a Service)
- PaaS (Platform as a Service)
- IaaS (Infrastructure as a Service)

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SAAS I PAAS I IAAS - LOOK BEYOND THE JARGON

	SaaS	PaaS	IaaS
Meaning	In SaaS, the vendor supplies the hardware infrastructure, the software product and interacts with the user through a front-end portal. Services can be anything from Web-based email to inventory control and database processing. Because the service provider hosts both the application and the data, the end user is free to use the service from anywhere. The Service Provider has very high administrative control on the application & is responsible for update, deployment, maintenance & security.	PaaS is a platform where software can be developed, tested and deployed, meaning the entire life cycle of software can be operated on a PaaS. This service provides everything you need to develop a cloud SaaS application. PaaS provider may use APIs (Application Programing Interfaces), websiteportals orateway software installed on customer's computer.	This model of service typically includes the core IT infrastructure services such as operating systems, data storage, web servers and edge caching services. The primary difference between this approach and traditional outsourcing is that with cloud computing, access to infrastructure is through the public or private networks and payment for resources is based on usage.
Subscribers	Individuals, Enterprises and Organisations	Independent Software Vendors, IT service providers or even individual developers who want to develop SaaS.	System Administrators
When / Why should you opt for	When you want to focus on your business rather than wasting time in replacing faulty hardware, managing IT infrastructure, hiring or retaining your IT staff etc.	When you focus only on developing the application, everything else will be taken care of by the platform.	Very useful for startup companies who don't know how successful their newly launched application / website will be.

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Cloud Computing & Chartered Accountants

With cloud computing, a Chartered Accountant can come with new ways of providing service to their clients. This can be evident from the fact that IT has become important on account of compliance services which requires use of IT and client data on which assurance has to be provided. With Cloud, everything becomes a service thus enabling enterprises to create new initiatives without huge investment in IT. It offers new business benefits which are expected to change the way businesses collaborate, compete, operate and deliver services.

This is where Chartered Accountants can provide assurance and consulting services for clients who are on cloud by leveraging their knowledge of compliances, accounting and assurance. For this, we are required to have a good working knowledge of how cloud computing operates, what are the risk, security concerns and the kind of control it offers so that we can be a step ahead of our clients and in a position to serve them better. It will help reduce the costs will save ample amount of time and increase the productivity of employees. This will enable to keep our focus on the service rather than invest our time in maintaining and securing data servers.

Implementing cloud computing has immense rewards but as with any IT implementation, it has certain inherent risks too:

1. Cloud Computing has risks primarily on account of dependence on the Internet and data being and transmitted on the cloud.

2. Risk of loss of data at data centers due to reasons like fire, data corruption, hacking of data, power failure etc.

3. Risk may also be due to vulnerabilities of hardware devices and the increased reliance on independent assurance processes.

Conclusion

All in all, cloud computing is not such a revolutionary idea- most of us have already been using it for years. Google & other cloud capitalists envision a future where your device is essentially a low- cost, thin- client interface, while all your data, programs and work is stored securely and safely in the cloud. Computer broken or stolen? Pick up a new one, log in and find all your stuff waiting there. Whether we'll give up the idea of keeping our data "safe at home" in a hard drive is an open question, but cloud computing's indisputable advantages are also winning over a lot of fans.

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