



Global Business Tax Alert Sharp Insights

CBDT issues clarifications on Income Computation and Disclosure Standards ('ICDS')

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Background

- After notification of ICDS, the stakeholders brought to the notice of the Central Board of Direct Taxes ('CBDT') that certain provisions of ICDS may require amendment/clarification for proper implementation. The matter was then referred to an expert committee. The Committee recommended a two-fold approach for the smooth implementation of ICDS i.e. amendment to the provisions of ICDS in respect of certain issues and issuance of clarifications by way of FAQs for the rest of issues. Accordingly, the CBDT issued amended ICDS effective from AY 2017-18.
- The issues which require further clarifications have been considered by the CBDT and vide Circular No. 10/ 2017 dated 23 March 2017, further FAQs has been issued. The same has been discussed below.

Clarifications issued by the CBDT

A synopsis of the clarifications issued by CBDT are given below:

1. Interplay between ICDS I and maintenance of books of accounts

It has been clarified that the ICDS are not meant for maintenance of books of account or preparing financial statements. The accounting policies mentioned in ICDS I, being fundamental in nature, shall be applicable for computation of income under the head 'Profits and gains of business / profession' or 'Income from other sources'.

2. Inconsistency between judicial precedents and ICDS

It has been clarified that the ICDS have been notified after due deliberation and examination of judicial views for bringing certainty on issues covered by it. As the CBDT has now provided certainty by notifying ICDS, the provisions of ICDS shall be applicable to the transactional issues dealt therein from AY 2017-18 and onwards.

3. Applicability of ICDS in certain cases

The clarifications have been issued by the CBDT on the applicability of ICDS to persons covered under presumptive taxation scheme, companies following Ind-AS, computation under Minimum Alternate Tax ('MAT') and Alternate Minimum Tax ('AMT'), banks, etc. as under:

Persons covered by presumptive scheme of taxation (eg. Sec 44AD, 44AE, 44ADA, 44B, 44BB, 44BBA of the Income-tax Act, 1961).

It has been clarified that ICDS is applicable to persons having income chargeable under the head 'Profits or gains of business or profession' or 'Income from other sources'. Therefore the relevant ICDS shall also apply to persons computing income under the relevant presumptive taxation scheme.

Applicability to companies which adopted Ind-AS

ICDS is applicable for computation of taxable income under the Income-tax Act, 1961 ('Act') irrespective of the accounting standards adopted by the companies i.e., either Accounting standards or IND-AS.

Whether applicable to computation under MAT and AMT

As the provisions of ICDS are applicable for computation of income under the regular provisions of the Act, the provisions of ICDS shall not apply for computation of book profit under section 115JB of the Act.

However, as AMT is computed on adjusted total income derived by making specified adjustment to total income computed under regular provisions of the Act, the provisions of ICDS will apply for computation of AMT.

Applicability to Banks, Non-banking financial institutions, Insurance companies, Power sector etc.

The general provisions of ICDS shall apply to all persons unless there are sector specific provisions contained in the ICDS or the Act. (Example: ICDS VIII contains specific provisions for Banks or certain financial institutions and Schedule I of the Act contains specific provisions for Insurance business).

Applicability of ICDS III and IV by real estate developers and Build-Operate-Transfer ('BOT') projects and applicability of ICDS for leases

As currently there is no specific ICDS notified for real estate developers, BOT projects and leases, the relevant provisions of the Act and ICDS shall apply to these transactions as may be applicable.

Applicability of ICDS to income liable to tax on gross basis

The provisions of ICDS shall also be applicable for computation of income on gross basis (e.g. interest, royalty, fees for technical services under section 115A of the Act) for arriving at the amount chargeable to tax.

4. Conflict between the provisions of ICDS and Income Tax Rules, 1962 ('Rules')

As ICDS provides for general principles for computation of income, in case of conflict between the provisions of the Rules and ICDS, the provisions of Rules which deal with specific circumstances, shall prevail (e.g. 9A, 9B etc.).

5. Applicability of provisions of ICDS for recognising Mark To Market ('MTM') gains or expected income

The principles contained in ICDS I relating to recognizing MTM losses or an expected loss provides that the MTM loss or an expected loss, shall not be recognized unless the same is in accordance with the provisions of other ICDS. It has been clarified that the same principles as contained in ICDS I shall apply *mutatis mutandis* to MTM gains or an expected profit.

6. Meaning of the term 'Reasonable cause' under ICDS I

The term 'reasonable cause' is an existing concept and has evolved well over a period of time and confers desired flexibility to the tax payer in deserving cases.

7. Which ICDS to govern derivative instruments

ICDS VI (subject to para 3 of ICDS VIII on Securities) provides guidance on accounting of derivatives contracts. Therefore, in respect of derivatives, not covered within the scope of ICDS VI, the provisions of ICDS I shall apply.

8. Recognition of retention money

The retention money (being part of overall contract revenue) shall be recognised as revenue, subject to reasonable certainty of its ultimate collection condition as provided in ICDS III on construction contracts.

9. Accounting of interest, royalty and dividend when collection is uncertain

The subsequent non-recovery in aforesaid cases can be claimed as a deduction under the provisions of the Act. Further, the provisions of the Act (e.g. special provisions in case of income of public financial institutions, etc.) shall prevail over ICDS provisions.

10. Treatment for expenditure incurred after test runs and experimental production but before commencement of commercial production

It has been clarified that the expenditure incurred till the plant has begun commercial production (i.e. production intended for sale or captive consumption) shall be treated as capital expenditure as per ICDS V on Tangible Fixed Assets.

11. Taxability of opening balance of Foreign Currency Translation Reserve ('FCTR') as on 1 April 2016 relating to non-integral operation as per AS-11:

The FCTR balance as on 1 April 2016 on monetary items for non-integral operations, shall be recognised in AY 2017-18 to the extent not recognized in the income computation in the past.

12. Recognition of subsidy received prior to 1 April 2016

In case of a government grant which meets the recognition criteria on or after 1 April 2016 shall be recognised in accordance with ICDS VII.

However, if the grant or subsidy is already received prior to 1 April 2016, then said subsidy or grant shall continue to be recognised as per the law prevailing prior to 1 April 2016, even if some of the related conditions are met on or after 1 April 2016.

13. Clarification on ICDS VIII on Securities

Deduction in respect of interest already taxed but not received, while computing the capital gain

The amount already taxed as interest income on accrual basis to be taken into account for computation of capital gains arising from such sale, although interest may not have been received prior to the sale.

Valuation of securities held as stock in trade

Securities held as stock-in-trade shall be first aggregated category-wise. The aggregate cost and Net Realisable Value of each category of security are to be compared and the lower of the two is to be taken as carrying value as per ICDS VIII.

14. Clarifications relating to ICDS IX on Borrowing costs

Whether borrowing cost to be capitalised if portion of the borrowing cost is disallowed

As the specific provisions of the Act override the provisions of the ICDS, the borrowing costs disallowed under the specific provisions of the Act [e.g. section 14A, 43B, 40(a)(i) etc. of the Act] to be excluded from borrowing costs considered for capitalization under ICDS IX.

Whether Bill discounting and other similar charges fall under the definition of borrowing cost

As the definition of borrowing cost is inclusive, the aforesaid charges would be covered as borrowing cost.

Allocation of general borrowing cost to different qualifying assets

The capitalization of general borrowing cost under ICDS IX shall be done on an "asset-by-asset" basis.

15. Clarifications relating to ICDS X – Provisions, Contingent liabilities and contingent assets

Transitional Provisions

The provisions or assets and related income to be recognized for the previous year commencing on or after 1 April 2016, in accordance with the provisions of ICDS X after taking into account the amount recognized, if any, for the same for any previous year ending on or before 31 March 2016.

It has been clarified that the intent of the same is that there is neither 'double taxation' of income nor should there be exemption of any income due to application of ICDS from a particular date.

Provision for employee benefits

The provisions for employee benefits, which are otherwise covered by AS 15 shall continue to be covered by specific provisions of the Act and will not be dealt with by ICDS X.

16. Reporting of disclosures specified in ICDS

The Disclosures required under the ICDS shall be made in the tax audit report in Form 3CD. However, no separate disclosures are required for persons not liable to tax audit.

Further, the net effect on the income due to application of ICDS is to be disclosed in the return of income.

¹ Notification No. 87/2016 dated 29 September 2016

Conclusion

Based on the concerns raised by the stakeholders on certain aspects of ICDS, the CBDT has issued the Circular seeking to resolve ambiguities. The clarifications also seek to provide a roadmap on the applicability of ICDS.

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