

Accounting Standards

AS - 9 & AS - 10

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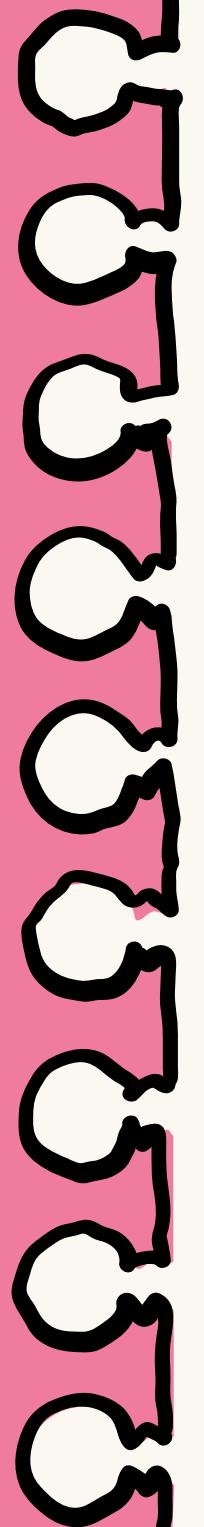
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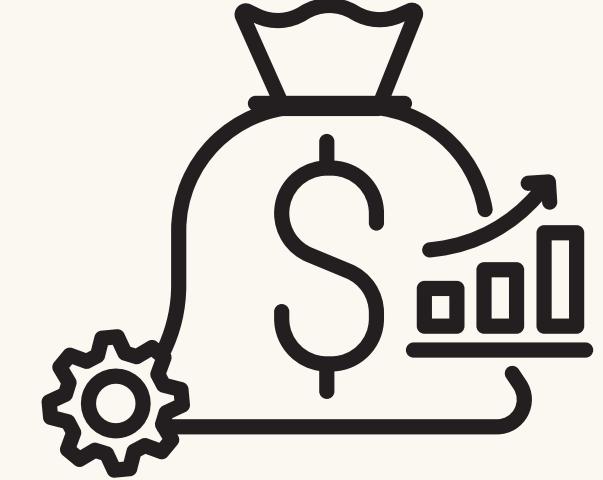
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AS - 9

Revenue Recognition



Understanding Revenue Recognition (AS 9)



In the world of business, revenue is more than just numbers—it's the lifeline of an enterprise, flowing from everyday activities like selling goods, rendering services, and leveraging resources.

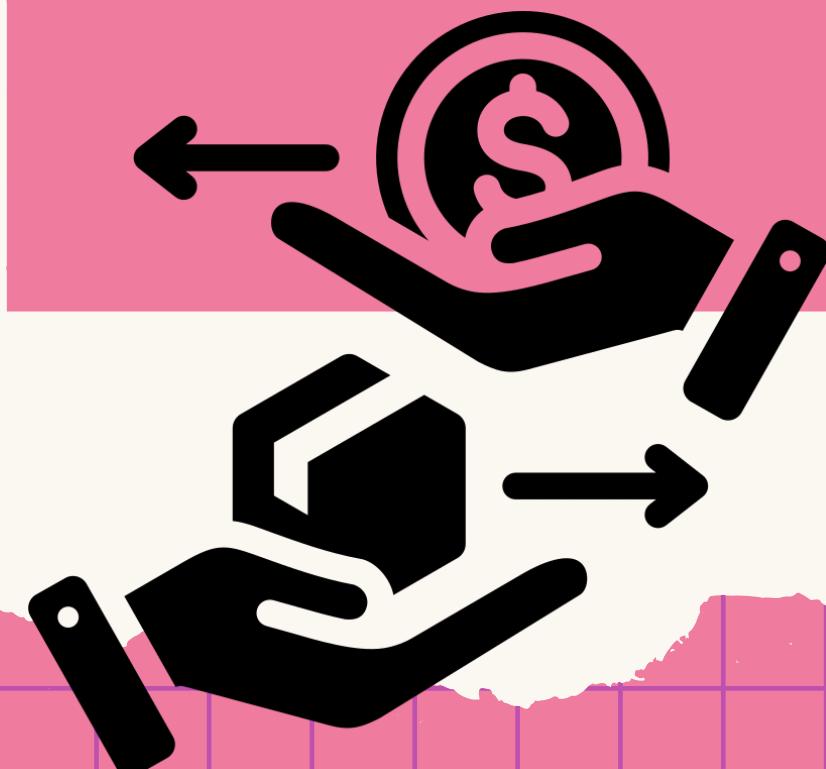
But when should revenue truly be recognized?

AS 9 provides the framework to ensure that enterprises accurately and consistently reflect their earnings in the statement of profit and loss. It's not just about what's earned, but when and how it's recorded, aligning financial results with real-world activities.

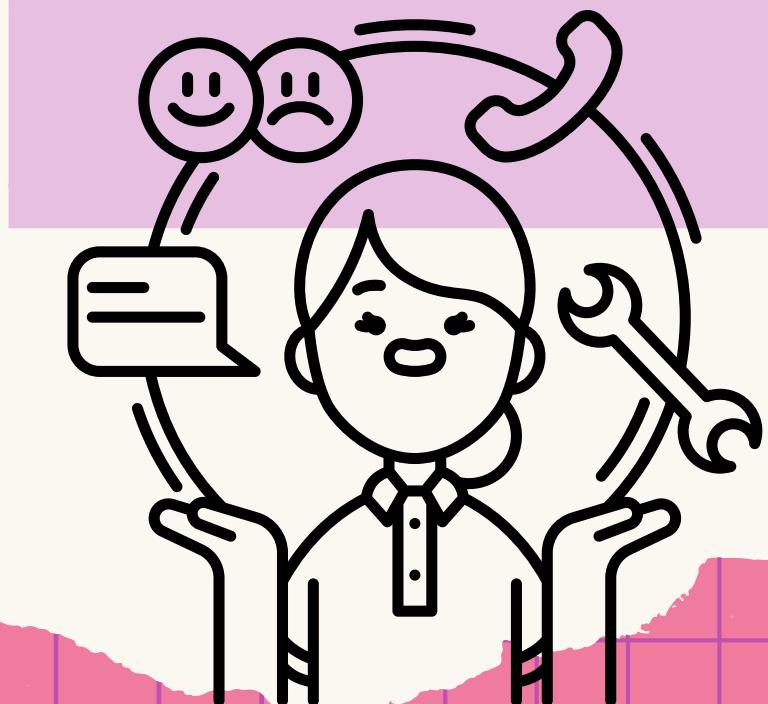
Key Revenue Sources

The Standard is concerned with the recognition of revenue arising in the course of the ordinary activities of the enterprise from:

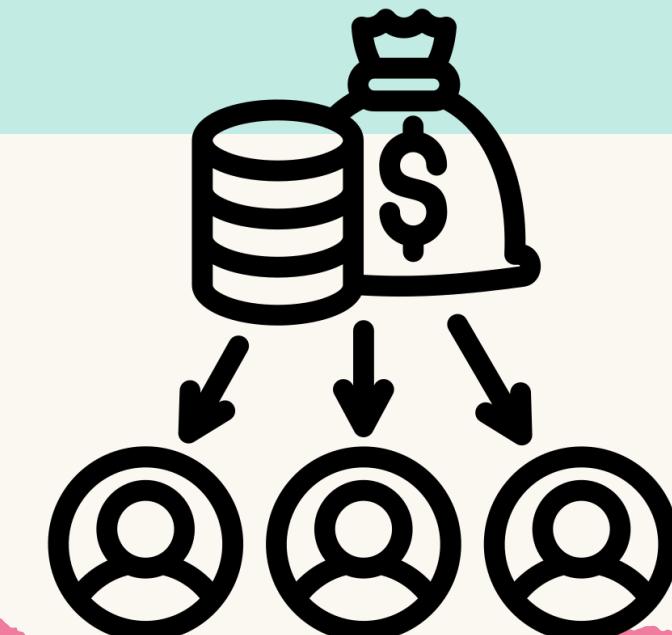
1. the sale
of goods



2. the
rendering of
services



3. the use of
interest,
royalties and
dividends.



What AS 9 doesn't deal with?

1. construction contracts

AS 7
(Accounting for Construction Contracts)



2. lease agreements

AS 19 (Leases)

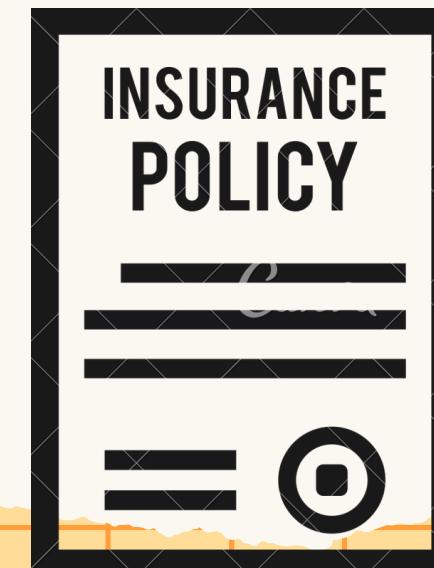


Revenue from:



3. government grants & subsidies

AS 20 (Earnings Per Share)



4. insurance contracts

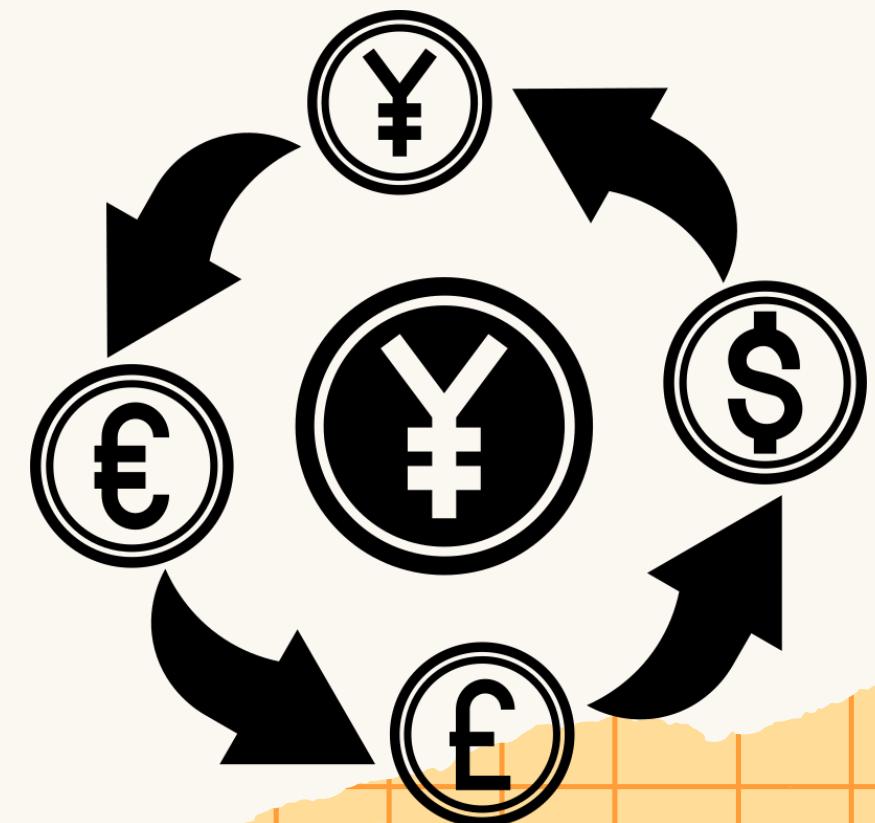
AS 4 (Insurance Contracts)



Items Not Considered Revenue

Gains from

- disposal/holding of non-current assets
- disposal/holding of current assets
- foreign exchange rate changes
- discharging obligations at less than carrying amount
- restating obligations



Definitions

The following terms are used in this Standard with the meanings specified:

- **Revenue**

Revenue is the gross inflow of cash, receivables, or other consideration from:

- Sale of goods
- Rendering of services
- Use of enterprise resources (interest, royalties, dividends)

In agency relationships, revenue is the commission earned, not the total cash inflow.

- **Completed service contract method**

is a method of accounting which recognises revenue in the statement of profit and loss only when the rendering of services under a contract is completed or substantially completed.

- **Proportionate completion method**

is a method of accounting which recognises revenue in the statement of profit and loss proportionately with the degree of completion of services under a contract.

Measurement of Revenue

Revenue is recognised at the nominal amount of Consideration Receivable.

a) Any **trade Discounts or Rebates** shall be deducted and revenue is measured net of these items

Transaction Price -----> XXXX
(contract price)

(-) Trade Discount -----> XXX

Revenue

b) With regard to exchange of goods or services

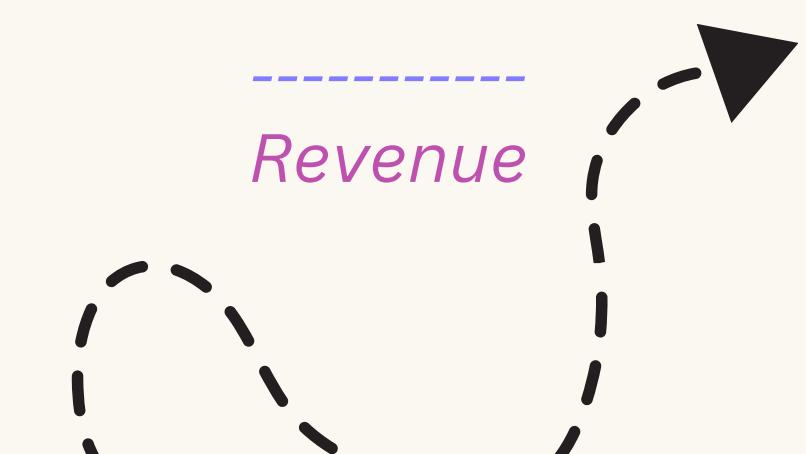
- If goods/services exchanged are **similar** in nature then **No Revenue** to be recognized
- If revenue is in **cash & kind both** then:

Amount of cash to be received -----> XXXX

*(+) Fair value of Goods/
services/Assets received
in a **dissimilar** nature of
exchange*

-----> XXX

Revenue



SALES OF GOODS

Revenue Recognition



Revenue from sales transaction should be recognised when the requirements as to performance set out below are satisfied:

1. The seller of goods has **transferred the ownership** to buyer.
2. All significant **risks & rewards** of ownership has been transferred to buyer.
3. **No significant uncertainty** exists regarding the amount of consideration.

Example 1: Retail Transaction - "A retail company sells goods online. Revenue is recorded once goods are delivered to the customer, transferring control."

Explanation: Since the goods have been delivered and control transferred, risks and rewards are with the buyer.

Example 2: Shipping with Risk Transfer - "A business ships goods under FOB (Free on Board) terms. Revenue is recorded once goods leave the warehouse, as risk and reward are transferred at shipping."

Explanation: FOB terms make the buyer responsible for goods once they're shipped, so revenue can be recorded.

FOB means that as soon as the goods are shipped (leave the seller's warehouse), the responsibility (risk and reward) is transferred to the buyer.

Transaction	Revenue Recognition
Goods Shipped Subject to Conditions	
-installation & inspection	When the buyer accepts delivery and installation & inspection is completed
-on approval	When the buyer formally accepts the shipment
-with limited right of return	When the goods were delivered and time for return lapsed
-consignment sales	After the consignee sells goods to the final customer
-cash on delivery sales(e.g., amazon/flipkart)	When delivery is made and cash is received by the seller



RENDERING OF SERVICES

Revenue Recognition Criteria:

1. Performance of Services:

- Revenue is recognized as services are rendered or milestones are achieved.
- Use appropriate methods to measure progress:
 - **Percentage of Completion Method:** Revenue is recognized based on the proportion of work completed.
 - **Completed Contract Method:** Revenue is recognized only after the service is fully rendered.

Methods for Measuring Progress:

- **Cost-to-Cost Method:** Compares costs incurred to total estimated costs.
- **Surveys of Work Performed:** Based on assessments of completed work.
- **Units of Delivery:** Revenue is recognized as per deliverables completed.

Examples:

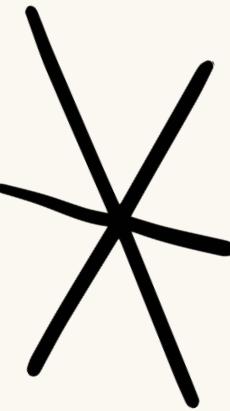
1. **Consulting Services:** Revenue is recognized as the consultancy is delivered over time or in phases.
2. **Construction Projects:** Revenue is recognized progressively using the percentage of completion method.
3. **Software Implementation:** Recognized as per project phases, such as design, testing, and deployment.

Interest

This is the fee charged for the use of money. If others use the company's cash or owe money to the enterprise, they pay interest, which usually collect over time based on the amount and interest rate set.

Example: Imagine you lend 1,000 Rs. to a friend, and they agree to pay you back with a 5% interest rate after one year. At the end of the year, they pay you 1,050 Rs. (1,000 Rs. principal + 50 Rs. interest). The 50 Rs. is the interest, a payment for the use of your money. Interest is commonly seen in loans or savings accounts where banks pay interest to account holders.

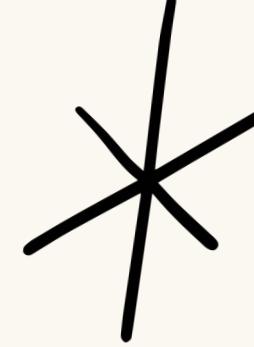
Royalties



These are fees for using the company's intellectual property—like patents, trademarks, or specialized knowledge. Royalties are typically recognized as income according to the terms in the agreement, though sometimes it might make more sense to recognize them in a way that better reflects the nature of the transaction.

Example: An author writes a book and signs a contract with a publisher. For every copy sold, the publisher pays the author \$1 as a royalty.

The \$1 per book is a royalty—a fee paid for the use of the author's intellectual property. Royalties are also common in music, technology, and patent licensing, where creators earn a percentage of sales or usage fees for their work or inventions.



Dividends

These are returns from holding investments in shares of other companies. Dividends represent the company's share of profits from these investments.

Example: You buy shares in a company that makes profits throughout the year. At the end of the year, the company decides to distribute some of those profits to its shareholders, paying \$2 per share as a dividend. If you own 100 shares, you receive \$200.

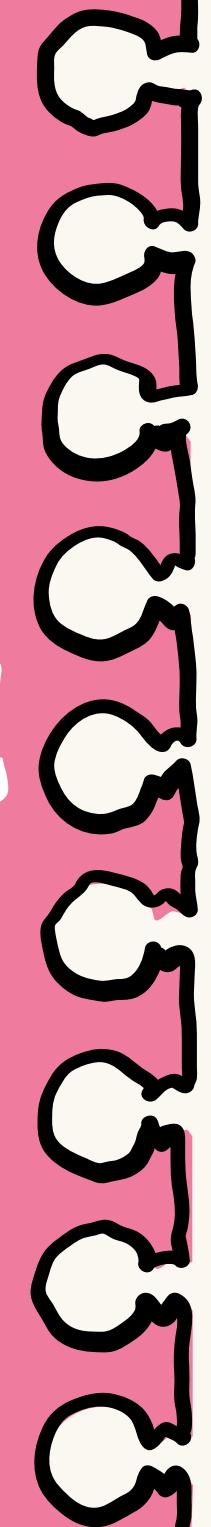
The \$200 you receive is a dividend—a reward for holding shares in the company. Dividends are typically paid by established companies as a way to share profits with their investors.

Effect of Uncertainties on Revenue Recognition

- 1. Revenue Should Be Reliable and Collectible:** Record revenue only if it can be measured and you can reasonably expect to get paid.
- 2. Delay Revenue if Collection is Uncertain:** If it's unclear whether certain payments will be collected (like extra charges or incentives), wait until you're fairly sure of payment before recording it. But if there's no uncertainty, record revenue right at the sale, even if payments are spread out.
- 3. Handling New Uncertainty After Sale:** If doubts about payment come up after the sale, create a reserve to cover this instead of changing the original revenue recorded.
- 4. Revenue Must Be Clearly Measurable:** Only record revenue if the expected payment is clear and can be estimated; if not, hold off on recording it.
- 5. Record Delayed Revenue When Certain:** Any postponed revenue should be recorded in the period when you're confident it will be collected.

AS - 10

Property, Plant
and Equipment



Objective

1. This Standard explains how to **account for property, plant, and equipment**. It helps people who read financial statements understand the company's investments in these assets and any changes to them. The main points include when to recognize these assets, how to calculate their value, and how to account for depreciation and any loss in value.

Scope

2. This Standard should be applied in accounting for property, plant and equipment except when another Accounting Standard requires or permits a different accounting treatment.

3. This Standard does **not** apply to:

- (a) biological assets related to agricultural activity **other than bearer plants**. This Standard applies to bearer plants but it does not apply to the produce on bearer plants; and
- (b) wasting assets including mineral rights, expenditure on the exploration for and extraction of minerals, oil, natural gas and similar non-regenerative resources.

However, this Standard applies to property, plant and equipment used to develop or maintain the assets described in (a) and (b) above.

4. Other Accounting Standards may require recognition of an item of property, plant and equipment based on an approach different from that in this Standard. For example, AS 19, Leases, requires an enterprise to evaluate its recognition of an item of leased property, plant and equipment on the basis of the transfer of risks and rewards. However, in such cases other aspects of the accounting treatment for these assets, including depreciation, are prescribed by this Standard.

5. Investment property, as defined in AS 13, Accounting for Investments, should be accounted for only in accordance with the cost model prescribed in this standard.

Recognition

7. The cost of an item of property, plant and equipment should be recognised as an asset if, and only if:
 - (a) it is probable that future **economic benefits** associated with the item will **flow to the enterprise**; and
 - (b) the cost of the item can be **measured reliably**.

8. Items such as spare parts, stand-by equipment and servicing equipment are recognised in accordance with this Standard when they meet the definition of **property, plant and equipment**. Otherwise, such items are classified as **inventory**.

9. This Standard **does not prescribe the unit of measure for recognition**, i.e., what constitutes an item of property, plant and equipment. Thus, judgement is required in applying the recognition criteria to specific circumstances of an enterprise. An example of a ‘unit of measure’ can be a ‘project’ of construction of a manufacturing plant rather than individual assets comprising the project in appropriate cases for the purpose of capitalisation of expenditure incurred during construction period.

Similarly, it may be appropriate to aggregate individually insignificant items, such as moulds, tools and dies and to apply the criteria to the aggregate value. An enterprise may decide to expense an item which could otherwise have been included as property, plant and equipment, because the amount of the expenditure is not material.

10. An enterprise evaluates under this recognition principle all its costs on property, plant and equipment at the time they are incurred. These costs include costs incurred:

- (a) initially to acquire or construct an item of property, plant and equipment; and
- (b) subsequently to add to, replace part of, or service it.

6 The cost of an item of property, plant and equipment should be recognised as an asset if, and only if:

- (a) it is probable that future economic benefits associated with the item will flow to the enterprise; and
- (b) the cost of the item can be measured reliably.

7 Spare parts, backup equipment, and maintenance tools are treated as property, plant, and equipment if they meet the requirements of this Standard. If not, they are counted as inventory.

8 This Standard does not specify what counts as a single item of property, plant, and equipment. Companies need to use their judgment to apply the rules based on their specific situation. For example, a “unit” might be a whole project, like building a manufacturing plant, instead of looking at each asset separately when adding up costs during construction. Also, small items like molds, tools, and dies can be grouped together and treated as one unit. A company might also choose to record a small expense right away, even if it could have been counted as property, plant, and equipment, if the cost is not significant.

9 A company reviews all costs related to property, plant, and equipment based on this principle when the costs happen. These costs include: (a) the initial costs to buy or build the property, plant, and equipment; and (b) later costs to add to it, replace parts, or maintain it.

Evaluating Costs

Initial cost-

- Initial Costs refer to the expenses incurred to acquire or construct an item of Property, Plant, and Equipment (PPE) and make it ready for use.
- These costs are essential to bringing the asset to a location and condition where it can be used for its intended purpose.
- This includes the purchase price, installation, and any necessary modifications to get the asset ready for use.

Components of Initial Costs

1. **Purchase Price**: The cost of buying the asset, less any trade discounts.

2. **Directly Attributable Costs**: These are costs necessary to bring the asset to the location and condition required for its intended use.

Examples include:

- **Delivery and Handling Costs**: The expense of transporting the asset to its operating site.
- **Installation and Assembly Costs**: Costs for setting up the asset so it's ready to operate.

- **Professional Fees**: Fees paid for legal or consulting services directly related to acquiring or constructing the asset.

3. **Dismantling and Site Restoration Costs**: Some assets require initial setup or installation costs, and part of that might involve an obligation to remove the asset or restore the site in the future.

EXAMPLE :-

Suppose a manufacturing company purchases a machine for \$50,000. To get the machine operational, they incur additional costs:

- Delivery charges: \$2,000
- Installation: \$3,000
- Testing: \$1,000

Total Initial Cost = \$50,000 (purchase price) + \$2,000 (delivery) + \$3,000 (installation) + \$1,000 (testing) = \$56,000.

Subsequent Costs:

Subsequent Costs refer to the expenses incurred after the initial construction of an item of Property, Plant, and Equipment (PPE). These costs are for maintaining, improving, or replacing parts of an asset during its useful life.

They can fall into two main categories:

1. Day-to-day Servicing Costs
2. Replacement Costs
3. Major Inspection Costs

Measurement at Recognition

An item of property, plant and equipment that qualifies for recognition as an asset should be measured at its cost.

Elements of Cost

- Purchase price including import duties and purchase taxes, deducting trade discounts
- Directly attributable costs. Example: installation, delivery costs
- Decommissioning, restoration and similar liabilities

Exclusions from cost

- Inauguration costs
- New product introduction(including costs of advertising and promotional activities)
- Administration and other general overhead costs
- Exclusions from carrying amount :
 - Relocation expenses and operating losses
 - Cost incurred while PPE either is not in operation or operates at less than full capacity

Self-Constructed Asset

- It is accounted for using the same principles for an acquired asset. Abnormal waste, labour costs are ignored.

Bearer Plants

- Includes the following :
 - production & supply of agricultural produce
 - expected period of produce is greater than 12 months
 - remote likelihood of sale, incidental sale as scrap
- Accounted for the same as self-constructed assets.

Measurement of Cost

- Consolidated purchase of PPE is recorded at respective fair values
- Finance leases - AS 19 (Leases)
- Reduction in carrying amount - AS 12 (Accounting for Government Grants)

Measurement after Recognition

Cost Model

- Accounts for the PPE at cost
- Less accumulated depreciation and any accumulated impairment losses

Revaluation Model

- Fair value on date of revaluation, less depreciation and impairment losses
- Revaluations are made regularly

Frequency of revaluation

- Fair value differs from it's carrying amount, further revaluation is required.
- Annual revaluation - significant changes in fair value.
- Examples: office furniture, land in commercial area

Carrying amount

- Increase - Credited directly to owners' interests under surplus in the Statement of P&L and reverses a revaluation decrease
- Decrease - Debited and reverses a revaluation increase

Depreciation

Depreciation is the process of systematically allocating the cost of a tangible fixed asset over its useful life. It reflects the gradual consumption of the asset's economic value as it is used in operations.

For instance, if a company buys machinery for ₹1,00,000 and expects it to be useful for 10 years, depreciation spreads this cost, perhaps allocating ₹10,000 per year, rather than recognizing the entire ₹1,00,000 expense in the year of purchase.

SIGNIFICANT PARTS DEPRECIATION

When an item of property, plant, and equipment (PPE) has parts that are significant in cost and have different useful lives, each significant part should be depreciated separately. This ensures that depreciation reflects the actual consumption pattern of each component's value over time.

Example: In the case of an aircraft, major parts like the airframe and engines have substantial costs and distinct useful lives. Since these components are critical and may need replacement or major overhauls at different intervals, they are depreciated individually rather than as a single unit. This provides a more accurate allocation of the aircraft's cost over its operational life.

DEPRECIABLE AMOUNT & USEFUL LIFE

DEPRECIABLE AMOUNT

This is the portion of an asset's cost that will be allocated as depreciation over its useful life. It is calculated as the asset's cost minus its residual value (the estimated amount the asset will be worth at the end of its useful life).

USEFUL LIFE

The useful life of an asset is the expected period during which the asset will contribute to the company's operations and revenue generation.

Land and Buildings

Land and buildings, even when acquired together, are considered distinct assets and are accounted for separately. This distinction is essential because the two have different characteristics and useful lives.

Land

Typically, land has an unlimited useful life and does not wear out or depreciate over time. Therefore, it is generally not depreciated.

Buildings

Unlike land, buildings have a limited useful life due to factors like wear and tear, aging, and potential obsolescence. Consequently, buildings are depreciable assets, and their cost is allocated over their estimated useful life through depreciation.

Depreciation Methods

1. Straight-Line Method

This method applies a fixed, constant depreciation charge over the asset's useful life, making it simple and easy to calculate. Each period's depreciation expense remains the same, assuming the asset's residual value does not change. It is often used for assets that provide consistent benefits throughout their life, such as office furniture or buildings.

Depreciation Methods

2. Diminishing Balance Method

Under this method, depreciation is calculated as a fixed percentage of the asset's remaining book value each period, resulting in a higher depreciation expense at the beginning of the asset's life, which gradually decreases over time. This method is suitable for assets that lose value quickly or require more maintenance as they age, such as machinery and vehicles.

Example

- You buy a machine for ₹1,00,000.
- Depreciation rate = 20% per year.

Year 1: ₹1,00,000 × 20% = ₹20,000 depreciation. Remaining value = ₹80,000.

Year 2: ₹80,000 × 20% = ₹16,000 depreciation. Remaining value = ₹64,000.

Year 3: ₹64,000 × 20% = ₹12,800 depreciation. Remaining value = ₹51,200.

This way, you reduce more in the beginning (when the asset is new and valuable) and less later (as it gets older and worth less).

Depreciation Methods

3. Units of Production Method

This method bases depreciation on the actual usage or output of the asset, making it ideal for assets where wear and tear correlate directly with production. For example, depreciation for manufacturing equipment might be calculated based on the number of units produced or hours operated.

Example

- You buy a machine for ₹5,00,000.
- Residual value = ₹50,000.
- Total estimated production = 1,00,000 units.

Depreciable amount = ₹5,00,000 - ₹50,000 = ₹4,50,000.

Depreciation per unit = ₹4,50,000 ÷ 1,00,000 = ₹4.50 per unit.

If the machine produces 20,000 units in a year:

Depreciation = 20,000 × ₹4.50 = ₹90,000.

This method ensures you match depreciation with how much the asset actually works!

**THANK
YOU!**