

## **INCOME COMPUTATION AND DISCLOSURE STANDARDS**

### **CHECKLIST FOR ICDS IN TAX AUDIT**

**ICDS are applicable for all** Assessee following Mercantile system of accounting for computing the Income from Business & Profession and Other Sources except those individual and HUF who are not liable for audit u/s 44AB. Since Form 3CD for tax audit and return forms have been amended to incorporate impact and disclosure stipulated in the ICDS, therefore a checklist is provided here for the benefit of members as follows:

#### **ICDS –I ACCOUNTING POLICIES**

1. Verify if the Assessee is a Going Concern?
2. Verify whether there is any change in Accounting Policies from earlier year? If yes, then verify the cause for change is reasonable or not?
3. Verify all income and expenditure have been recorded on accrual basis and there is no deviation from Accrual system?
4. Verify if any prior period expenses have been debited during the year?
5. Verify small and immaterial capital items like calculator, etc have been charged off to Profit and loss account?
6. Ensure Substance over Form has prevailed for treatment and presentation of transactions and events
7. Verify if any marks to market loss of derivatives or expected losses of contract have been recognized during the year as per principle of Prudence?
8. The same is not allowable and has to be disallowed in Return of Income
9. Ensure disclosure is made properly in Tax Audit report

## **ICDS – II VALUATION OF INVENTORIES**

1. Verify if in case of Service providers following Mercantile system, inventory of Work in progress has been recognized and effect of such WIP has been given in Income.
2. Verify if the inventory is valued at lower of Cost or Net Realisable Value
3. Please do not write that “ Inventory Valuation is taken as certified by Management” The same is violation of Standards on Auditing and is serious matter
4. Interest and other borrowing cost not to be considered for inventory valuation except for the case provided in ICDS on Borrowing costs
5. Verify if cost of inventory is not valued by method other than FIFO or Weighted Average
6. Verify if there is change in constitution of firm or profit sharing ratio
7. Please verify the Partnership deed contains the clause that on retirement or death of Partner the remaining partners shall continue the business of firm. If such clause is not mentioned than Whether the inventory has been valued at NRV on the date of dissolution of partnership due to retirement, death, etc. of a partner (irrespective of continuation of business)

## **ICDS – III CONSTRUCTION CONTRACTS**

(Applicable on determination of income for a construction contract of a contractor)

1. Only Percentage of Completion method is allowed under ICDS therefore if Project completion method is used then the impact of deviation be considered as income. (If Project completion method followed then make adjustment as per POCM to income)
2. If the life of service or contract is upto 90 days the same can be recognized using Project completion method.

3. Verify whether retention money has been recognized as income on the basis of actual receipt and not on accrual basis? Check running/progress bills have been accounted for and offered to income
4. Whether any expected losses in the project have been claimed in the year under consideration based on prudence? If yes specify
5. Verify whether early stage of contract is considered even after 25% of project has been completed and no revenue is recorded? (If not recognized, then revenue should be recorded and adjustment to be made to income. Till early stage the contract revenue should be equal to contract cost incurred)

#### **ICDS – IV REVENUE RECOGNITION**

1. Sale of Goods – Revenue to be recorded after transfer of significant risks and rewards and when there is reasonable certainty of its ultimate collection
2. Sale of Services – Revenue to be recorded by Percentage of Completion method.
3. Reasonable certainty of ultimate collection is not a condition precedent for recognition of revenue in case of sale of services
4. Interest - Interest shall accrue on the time basis.
5. No condition of reasonable certainty of ultimate collection therefore strictly as per ICDS Interest has to be recorded on Bad and doubtful loans on one hand and the same have to written off as bad debts on other hand.
6. In case of export incentives whether revenue has been recorded when the claim is lodged
7. If any refund has been assessed, recognize interest on refund only on actual receipt and not on time basis.
8. Verify that incidental income has been offered as income from other sources and has not been reduced from project cost or cost of asset.

## **ICDS – V TANGIBLE FIXED ASSETS**

At the outset the provisions of Act with regard to Actual cost shall continue to be governed by Section 43(1) and explanations thereto. ICDS is not applicable on transfer of fixed assets being dealt under capital gains and depreciation shall be allowed as per Section 32 of the Act therefore the standard may not have any impact on income. Therefore the ICDS may be purely academic.

## **ICDS – VI EFFECTS OF CHANGES IN FOREIGN EXCHANGE RATES**

1. Exchange difference on conversion of Integral and Non integral foreign operations has to be charged to Profit and Loss account.
2. All the monetary items i.e. Creditors for import, Debtors for export, etc. have to be marked to market on the date of Balance Sheet. The exchange gain / loss on monetary items has to be recorded and is allowed as per ICDS.
3. All non monetary items the forex gain loss has to be calculated based on date of transaction. For eg. Date of transaction and actual settlement of payment is allowable and not difference between date of transaction and Balance Sheet date.

## **ICDS – VII GOVERNMENT GRANTS**

1. Verify whether all the subsidies received for any purpose have been offered to tax as income? If No, then add to income
2. Verify whether all grants received in respect of non depreciable assets have been credit to profit and loss account and offered as income.
3. Verify whether grant received specifically towards depreciable assets has been reduced from the cost of such assets?
4. Verify whether grants received not specifically but generally towards depreciable assets has been reduced from cost of all the depreciable assets.

5. Verify whether there is any grant which has already been received but not offered to income?

Recognition cannot be postponed after the actual receipt. Such grant has to be offered as income?

### **ICDS – VIII SECURITIES**

(Applies only to securities held as stock in trade and not as investments)

1. Verify whether Securities held as stock in trade have been valued at actual cost
2. However if the Net realizable value of category of securities Eg. Equity shares, is less than actual cost of category of securities then the valuation has to be done at NRV
3. If the valuation is done based on lower of cost of NRV of individual script, the same has to be recomputed based on category wise total cost and NRV and the difference has to be adjusted to income.
4. In respect of unlisted securities or listed but not regularly quoted the inventory of securities has to be valued at cost

### **ICDS – IX BORROWING COSTS**

1. Acquisition of Foreign Asset - Exchange difference is excluded from the definition of borrowing cost under ICDS and the exchange difference on borrowings made for acquisition of fixed assets from abroad should be capitalized.
2. Acquisition of Indian Asset – Exchange difference on borrowing cost of foreign loan for asset acquired/ constructed/produced in India is not required to be capitalized and can be charged to Profit and loss account.
3. Qualifying asset would be only those assets which take more than one year in getting ready
4. Verify if Borrowing costs has been computed based on formula provided in ICDS

5. Verify whether borrowing costs have been computed on inventories which have taken substantial time i.e. more than one year.
6. Verify that the capitalization of borrowing costs has not been suspended during the interruption of active development of asset (AS 16 provides for suspension of borrowing cost in such situation)
7. Verify that income from temporary investments has not been reduced from borrowing costs eligible for capitalization under ICDS.

#### **ICDS – X PROVISIONS, CONTINGENT LIABILITIES AND CONTINGENT ASSETS**

1. Whether any provision is made without any proper basis and without reasonable certainty? If yes then qualify the same as contingent and disallow in return and report in TAR Cl.21(g)
2. Whether there are any escalation claims which have been accepted during the year and not recognized?
3. If any refund or claim has been accepted either under any law, the same has to be recognized as income and corresponding contingent asset has to be created if there is reasonable certainty of receipt. (Note that no contingent asset is allowed to be recognized as per accounting standard and the recognition shall only be for the purposes of ICDS)
4. Only disclose provisions in this clause and not liabilities for eg. Telephone Bill, Electricity bill which are recorded as outstanding based on actual bills received subsequently