



CBDT issues FAQs on Income Computation and Disclosure Standards

The Central Board of Direct Taxes (CBDT) has notified¹ Income Computation and Disclosure Standards (ICDS), with effect from the assessment year 2016-17.

Subsequently, various stakeholders have brought to the notice of the CBDT that certain provisions of ICDS may require amendment/clarification for proper implementation. The matter was referred to an expert committee. The committee after duly consulting the stakeholders in this regard has 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 Frequently Asked Questions (FAQs) for the rest of issues. Accordingly, the government notified amended ICDS² with effect from the assessment year 2017-18.

Recently, CBDT vide circular³ has issued FAQs clarifying certain ICDS related issues. The FAQs are summarised as follows:

Question No.	Question	Answer
1	Preamble of ICDS states that it 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 purposes of maintenance of books of accounts. However, ICDS-I states that accounting policies are applied for maintenance of books of accounts and preparing financial statements. What is the interplay between ICDS-I and maintenance of books of accounts?	ICDS is not meant for maintenance of books of accounts or preparing financial statements. Persons are required to maintain books of accounts and prepare financial statements as per accounting policies applicable to them.
2	Certain ICDS provisions are inconsistent with judicial precedents. Whether these judicial precedents would prevail over ICDS?	The ICDS have been notified after due deliberation and after examining judicial views for bringing certainty on the issues covered by it. Certain judicial precedents were pronounced in the absence of authoritative guidance under the Income-tax Act, 1961 (the Act). However, certainty is provided in ICDS, and hence the provisions of ICDS shall prevail over judicial

¹ Notification No. S.O. 892(E), dated 31 March 2015

² Notification No. 87, dated 29 September 2016

³ Circular No. 10/2017, dated 23 March 2017

		precedents from the assessment year 2017-18 onwards.
3	Whether ICDS apply to non-corporate taxpayers, who are not required to maintain books of account and/or those who are covered by the presumptive scheme of taxation?	ICDS is applicable to specified persons having income chargeable under the head 'Profits and gains of business or profession' or 'Income from other sources'. Therefore, the relevant provisions of ICDS shall also apply to the persons computing income under the relevant presumptive taxation scheme. For example, for computing presumptive income of a partnership firm under Section 44AD of the Act, the provisions of ICDS on construction contract or revenue recognition shall apply for determining the receipts or turnover, as the case may be.
4	If there is a conflict between ICDS and provisions of the Income-tax Rules, 1962 (the Rules) governing the taxation of income like Rules 9A, 9B, etc. of the Rules, which provisions shall prevail?	In the case of conflict, if any, between the provisions of Rules and ICDS, the provisions of Rules, which deal with specific circumstances, shall prevail.
5	ICDS is framed on the basis of accounting standards notified by Ministry of Corporate Affairs (MCA). However, in February 2015, MCA has notified a new set of Ind-AS. How will ICDS apply to companies which adopted Ind-AS?	ICDS shall apply for computation of taxable income under the head 'profit and gains of business or profession' or 'income from other sources' under the Act. This is irrespective of the accounting standards adopted by companies i.e. either Accounting Standards or Ind-AS.
6	Whether ICDS shall apply to the computation of Minimum Alternate Tax (MAT) under Section 115JB of the Act or Alternate Minimum Tax (AMT) under Section 115JC of the Act?	Since, 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 MAT. AMT under Section 115JC of the Act is computed on adjusted total income which is derived by making specified adjustments to total income computed as per the regular provisions of the Act and hence, the provisions of ICDS shall apply for computation of AMT.
7	Whether the provisions of ICDS shall apply 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. For e.g. ICDS VIII provides specific provisions for banks and certain financial institutions and Schedule I of the Act contains specific provisions for insurance business.
8	ICDS-I provides that Marked to Market (MTM) loss or an expected loss shall not be recognised unless the recognition is in accordance with the provisions of any other ICDS. Whether similar consideration applies to the	Same principle as contained in ICDS-I relating to MTM losses or an expected loss shall apply <i>mutatis mutandis</i> to MTM gains or an expected profit.

	recognition of MTM gain or expected incomes?	
9	ICDS-I provides that an accounting policy shall not be changed without 'reasonable cause'. The term 'reasonable cause' is not defined. What shall constitute 'reasonable cause'?	Under the Act, 'reasonable cause' is an existing concept and has evolved well over a period of time conferring desired flexibility to the tax payer in deserving cases.
10	Which ICDS would govern derivative instruments?	ICDS – VI (subject to para 3 of ICDS VIII) provides guidance on accounting for derivative contracts such as forward contracts and other similar contracts. For derivatives, not within the scope of ICDS-VI, provisions of ICDS-I would apply.
11	Whether the recognition of retention money, receipt of which is contingent on the satisfaction of certain performance criterion is to be recognised as revenue on billing?	Retention money, being part of overall contract revenue, shall be recognised as revenue subject to the reasonable certainty of its ultimate collection condition provided in ICDS-III on Construction contracts.
12	Since there is no specific scope exclusion for real estate developers and Build-Operate-Transfer (BOT) projects from ICDS-IV on revenue recognition, Whether ICDS-III and ICDS-IV should be applied by real estate developers and BOT operators? Also, whether ICDS is applicable for leases?	There is no specific ICDS notified for real estate developers, BOT projects, and leases. Therefore, relevant provisions of the Act and ICDS shall apply to these transactions as may be applicable.
13	The condition of reasonable certainty of ultimate collection is not laid down for taxation of interest, royalty, and dividend. Whether the taxpayer is obliged to account for such income even when the collection thereof is uncertain?	As a principle, interest accrues on time basis, and royalty accrues on the basis of contractual terms. Subsequent non recovery in either case can be claimed as a deduction in view of the amendment to Section 36(1)(vii) of the Act. Further, the provision of the Act (e.g. Section 43D) shall prevail over the provisions of ICDS.
14	Whether ICDS is applicable to revenues which are liable to tax on a gross basis like interest, royalty, and fees for technical services for non-residents <i>under Section 115A</i> of the Act.	Yes, the provisions of ICDS shall also apply for computation of these incomes on, the gross basis for arriving at the amount chargeable to tax.
15	Para 8 of ICDS-V states expenditure incurred on commissioning of the project, including expenditure incurred on test runs and experimental production shall be capitalised. It also states that expenditure incurred after the plant has begun commercial production. What shall be the treatment of expense incurred after the conduct of test runs and experimental production but before the commencement of commercial production?	As clarified in paragraph 8 of ICDS-V, the expenditure incurred till the plant has begun commercial production shall be treated as capital expenditure.
16	What is the taxability of opening balance as on 1 April 2016 of Foreign Currency Translation Reserve (FCTR) relating to the non-integral foreign operation, if any, recognised as per Accounting Standards (AS) 11?	FCTR balance as on 1 April 2016 pertaining to exchange differences on monetary items for non-integral operations, shall be recognised in the previous year relevant for Assessment Year 2017-18 to the extent not recognised in the income computation in the past.

17	For subsidy received prior to 1 April 2016 but not recognised in the books pending satisfaction of related conditions and achieving reasonable certainty of receipt, how shall the same be recognised under ICDS on or after 1 April 2016?	<p>Para 4 of ICDS-VII read with Para 5 to Para 9 of ICDS-VII provides for the timing of recognition of government grant. The transitional provision in Para 13 of ICDS-VII provides that a government grant which meets the recognition criteria on or after 1 April 2016 shall be recognised in accordance with ICDS-VII. All government grants actually received prior to 1st day of April 2016 shall be deemed to have been recognised on its receipt in accordance with Para 4(2) of (CDS-VII and accordingly will be outside the transitional provision, and therefore the government grants received on or after 1 April 2016 and for which recognition criteria provided in Para 5 to Para 9 of ICDS-VII is also satisfied thereafter, the same shall be recognised as per the provisions of ICDS-VII. The grants received prior to 1st day of April 2016 shall continue to be recognised as per the law prevailing prior to that date⁴.</p> <p>But if the subsidy is already received prior to 1 April 2016, Para 13 of ICDS-VII shall not apply even if some of the related conditions are met on or after 1 April 2016. This is in view of Para 4(2) of ICDS-VII which provides that Government grant shall not be postponed beyond the date of actual receipt. Such grants shall continue to be governed by the provisions of law applicable prior to 1 April 2016.</p>
18	If the taxpayer sells a security on the 30 April 2017. The interest payment dates are December and June. The actual date of receipt of interest is on the 30 June 2017, but the interest on accrual basis has been accounted as income on 31 March 2017. Whether the taxpayer shall be permitted to claim a deduction of such interest i.e. offered to tax but not received while computing the capital gain?	Yes, the amount already taxed as interest income on an accrual basis shall be taken into account for computation of income arising from such sale.
19	ICDS-VIII on securities requires securities held as stock-in-trade shall be valued at an actual cost initially recognised or net realisable value (NRV) at the end of <i>that</i> previous year, whichever is lower. Para 10 of Part-A of ICDS-VIII requires the said exercise to be carried out category wise. How shall the same be computed?	For subsequent measurement of securities held as stock-in-trade, the securities are first aggregated category wise. The aggregate cost and NRV of each category of security are compared, and the lower of the two is to be taken as carrying value as per ICDS-VIII. This has been explained by way of an example given in Annexure.
20	There are specific provisions in the Act read with Rules under which a portion of borrowing cost may get disallowed under Sections like 14A, 438, 40(a)(i), 40(a)(i3), 40A(2)(b), etc., of the Act. Whether borrowing costs to be capitalised under ICDS-IX should exclude a portion of borrowing costs which gets disallowed under such specific provisions?	Since specific provisions of the Act override the provisions of ICDS, it is clarified that borrowing costs to be considered for capitalisation under ICDS IX shall exclude those borrowing costs which are disallowed under specific provisions of the Act. Capitalisation of borrowing cost shall apply for that portion of the borrowing cost which is otherwise allowable as a deduction under the Act.

⁴ For example, if out of total subsidy entitlement of INR 10 Crore an amount of INR 6 Crore is recognised in the books of accounts till 31 March 2016 and recognition of balance INR 4 Crore is deferred pending satisfaction of related conditions and/or achieving reasonable certainty of receipt. The balance amount of INR 4 Crore will be taxed in the year in which related conditions are met, and reasonable certainty is achieved. If these conditions are met over two years, the amount of INR 4 Crore shall be taxed over the period of two years. The amount of 6 crores for which recognition criteria were met prior to 1 April 2016 shall not be taxable post prior to 1 April 2016.

21	Whether bill discounting charges and other similar charges would fall under the definition of borrowing cost?	The definition of borrowing cost is an inclusive definition. Bill discounting charges and other similar charges are covered as borrowing cost.
22	How to allocate borrowing costs relating to general borrowing, as computed in accordance with the formula provided under Para 6 of ICDS-IX to different qualifying assets?	The capitalisation of general borrowing cost under ICDS-IX shall be done on an asset-by-asset basis.
23	What is the impact of Para 20 of ICDS X containing transitional provisions'?	Para 20 of ICDS X provides that all the provisions or assets and related income shall be recognised for the previous year commencing on or after 1 April 2016 after taking into account the amount recognised, if any, for the same for any previous year ending on or before 31 March 2016. The intent of the transitional provision is that there is neither 'double taxation' of income due to the application of ICDS nor there should be escape of any income due to the application of ICDS from a particular date. This has been explained by way of an example.
24	Expenditure on post-retirement benefits like provident fund, gratuity, etc. are covered by specific provisions. There are other post-retirement benefits offered by companies like medical benefits. Such benefits are covered by AS-15 for which no parallel ICDS has been notified. Whether the provision for these liabilities are excluded from the scope of ICDS X?	The provisioning for employee benefit which are otherwise covered by AS 15 shall continue to be governed by specific provisions of the Act and are not dealt with by ICDS-X.
25	ICDS-I requires disclosure of significant accounting policies, and other ICDS requires specific disclosures. Where is the taxpayer required to make such disclosures specified in ICDS?	Net effect on the income due to the application of ICDS is to be disclosed in the return of income. The disclosures required under ICDS shall be made in the tax audit report in Form 3CD. However, there shall not be any separate disclosure requirements for persons who are not liable to tax audit.

Our comments

After the introduction of ICDS, stakeholders raised concerns/issues with respect to certain aspects of ICDS. After duly consulting the stakeholders, CBDT has issued these FAQs which seek to provide much needed clarity on such issues.

The ICDS clarified that it is subordinate to the statutory provisions of the Act and in the case of any conflict the provisions of the Act will prevail over the ICDS. Over the years, the statutory provisions have been interpreted by the courts. These rulings constitute part of the operative law. Therefore, ICDS should be subordinate also to the judicial rulings. However, the FAQs provide that the ICDS have been notified after due deliberations and after examining judicial views for bringing certainty on the issues covered by it. Certain judicial pronouncements were pronounced in the absence of authoritative guidance on these issues under the Act. Since certainty is now provided by notifying ICDS under Section 145(2) of the Act, the provisions of ICDS shall be applicable to transactional issues dealt therein in relation to the assessment year 2017-18 and onwards.

ICDS III provides that contract revenue shall be recognised when there is a reasonable certainty of its ultimate collection. Contract revenue shall, inter alia, comprise of the initial amount of revenue agreed in the contract, including retention money; to the extent that it is probable that they will result in revenue and they are capable of being reliably measured. AS 7 and Ind AS 11 dealing with the Construction Contract do not prescribe to include the retention amount into contract revenue. Further, the accrual and recognition of retention amount in a

construction contract have been a subject matter of litigation before the courts. Various courts have laid down the principles for accrual and recognition of retention amount i.e. on the date of submission of bills, the taxpayer does not have the right to receive the entire amount including retention amount⁵, the retention amount will accrue in the hands of taxpayer upon completion of work⁶, the right to receive retention amount did not accrue till the performance warranty period was over⁷. When the above tests are applied with respect to the retention amount, the general inference would be that the same does not accrue till the completion of work/satisfaction of conditions as per the terms of the contract. However, the FAQs provide that retention money, being part of overall contract revenue, shall be recognised as revenue subject to a reasonable certainty of its ultimate collection.

As per the ICDS I, the accounting policy shall not be changed without 'reasonable cause'. However, the term 'reasonable cause' has not been defined under the ICDS. Now, the FAQs provide that under the Act, 'reasonable cause' is an existing concept and has evolved well over a period of time conferring desired flexibility to the taxpayer in deserving cases. Under the Act, various Courts⁸ have held that reasonable cause can be reasonably said to be a cause which prevents a man of average intelligence and ordinary prudence, acting under normal circumstances without negligence or inaction or want of bonafide.

ICDS-I provides that MTM loss or an expected loss shall not be recognised unless the recognition is in accordance with the provisions of any other ICDS. The FAQs clarified that same principle relating to MTM losses or an expected loss shall be *mutatis mutandis* applicable to MTM gains or expected gains⁹.

CBDT has dealt with various specific issues like applicability of ICDS to MAT/AMT, real estate developers, BOT projects and leases, income liable to tax on gross basis/presumptive basis, derivative instrument, issues relating to subsidies, borrowing costs, etc. to provide clarity and bring certainty. These FAQs will help to resolve various issues raised by the stakeholders, and it will provide a roadmap for the application of ICDS.

⁵ CIT v. Simplex Concrete Piles India (P.) Ltd. [1989] 45 Taxman 370 (Cal), CIT v. East Coast Constructions & Ind. Ltd. [2007] 160 Taxman 399 (Mad)

⁶ DIT (International Taxation) v. Ballast Nedam International [2013] 33 taxmann.com 139 (Guj), CIT v. Ignifluid Boilers (I) Ltd. [2006] 283 ITR 295 (Mad), CIT v. Associated Cables Ltd. [2006] 286 ITR 596 (Bom), CIT v. East Coast Constructions & Ind. Ltd. [2007] 160 Taxman 399 (Mad)

⁷ Amarshiv Construction (P.) Ltd. v. DCIT [2014] 367 ITR 659 (Guj)

⁸ Azadi Bachao Andolan v. Union of India [2001] 252 ITR 471 (Del); CWT v. Jagdish Prasad Choudhary [1995] 211 ITR 472 (Patna)

⁹ The Supreme Court in the case of CIT v. Woodward Governor India Private Ltd [2009] 312 ITR 254 (SC) held that in terms of mercantile method accounting, the exchange fluctuation loss arising on MTM restatement of liability in foreign currency at the year-end is an allowable loss.

Annexure

Security	Category	Cost	NRV	Lower of cost or NRV	ICDS Value
A	Share	100	75	75	
B	Share	120	150	120	
C	Share	140	120	120	
D	Share	200	190	190	
	Total	560	535	505	535
E	Debt Security	150	160	150	
F	Debt Security	105	90	90	
G	Debt Security	125	135	125	
H	Debt Security	220	230	220	
	Total	600	615	585	600
Securities Total		1160	1150	1090	1135

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