IAS / Ind AS 16 – Property Plant & Equipment
IAS / Ind AS 38 – Intangible Assets

Study Group Meeting on IFRS, WIRC
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PPE – IAS 16 / Ind AS 16

1. Scope – Tangible Asset + Bearer Plants
2. Start up costs
3. Dismantling costs / ARO
4. Accounting for Rehabilitation and Resettlement
5. Asset purchased on extended credit terms
6. Major inspections
7. Initial recognition - Unit of measurement
8. Revaluation – Deferred tax
9. Recycling of revaluation reserve
10. Profit & loss on revalued asset
11. Depreciation method – Policy / Estimate
12. Residual value assessment and impact of change
13. Held for Sale
14. Exchange of assets – Commercial sense
15. Stripping cost

PPE – IAS 16 / Ind AS 16

The **cost** of an item of property, plant and equipment is recognised as an asset if, and only if:

(a) it is probable that future economic benefits associated with the item will flow to the entity; and

(b) the cost of the item can be measured reliably

Utensils, Spares!!

Tangible items that:

(a) are held for use in the production or supply of goods or services, for rental to others, or for administrative purposes; and

(b) are expected to be used during more than one period

Start Up Cost

- Start-up costs and similar pre-production costs do not form part of the cost of an asset.
- Initial operating losses incurred prior to an asset achieving its planned performance are recognised as an expense and not capitalised
- Example: where a hotel is being refurbished and is, therefore, closed for a period. All costs incurred in that period (rents, wages etc) would be expensed as incurred as they would not form part of the cost of improvements.

Case:

An amusement park has a 'soft' opening to the public, to trial run its attractions. Tickets are sold at a 50% discount during this period and the operating capacity is 80%. **The official opening day of the amusement park is three months later.**

Cost of Acquired or Self-Constructed Assets

INCLUDES

Purchase price (including import duties and non-refundable purchase taxes)

Less

- any discounts or rebates deducted
- implicit interest in deferred payment

Plus

- borrowing costs in the case of "qualifying assets" (refer IAS 23)
- any other directly attributable costs (e.g. employee benefits, site preparation, initial delivery and handling costs etc.)
- initial estimate of costs of dismantling & removing the item & restoring the site on which it is located

EXCLUDES

Costs related to

- Abnormal amounts of wasted material, labour and other resources
- Opening a new facility
- introducing a new product or service (including costs of advertising and promotional activities)
- Conducting business in a new location or with a new class of customer (including costs of staff training)
- Administration & other general overhead costs
- Using or redeploying an item
- Certain incidental operations
- Period when construction is interrupted, unless certain criteria are

Acquired in Exchange of Another Asset

- Cost of exchanged asset is measured at fair value unless
  - Exchange transaction lacks commercial substance, or
  - Fair value of neither asset received nor given up can be measured reliably

Cost of PPE acquired in exchange of another Asset

Fair value of asset given up is used, unless fair value of asset received is more clearly evident

OR

If not measured at fair value, carrying amount of the asset given up becomes the new cost

Treatment of Revaluation Reserve

Increase in carrying amount (on Revaluation)

- Increase in OCI (under revaluation reserve)
- Increase in PL to the extent of previous debit to PL

Decrease in carrying amount (on Revaluation)

- Decrease in PL
- Decrease in OCI to the extent of previous credit balance in OCI

On Disposal

Revaluation reserve transferred to retained earnings when it is realized.

Under *no circumstances can the revaluation* reserve, or part thereof, be credited to the income statement.

GAAP Difference

Sl No	Indian GAAP	Ind AS
1.	Primary guidance: AS 6, AS 10	Primary guidance: IAS 16
2.	Cost of fixed assets include purchase price for **deferred payment** term unless interest element is specifically identified in the arrangement.	Difference between the purchase price under **normal credit terms** and the amount paid, is recognised as interest expense over the period of the financing.
3.	There is no specific reference on whether cost of an item of PPE includes **costs of its dismantlement**, removal or restoration, the obligation for which an entity incurs as a consequence of installing the item.	The cost of an item of PPE includes such costs.
4.	**Cost of major inspections** and overhauls are generally expensed when incurred, unless that increases the future benefits from the existing asset beyond its previously assessed standard of performance.	Cost of major inspections and overhauls are capitalised only when it is probable that it will give rise to future economic benefits.

GAAP Difference

Sl No	Indian GAAP	Ind AS
5.	Revaluation is permitted. No specific requirement on **frequency of revaluation.**	Revaluation is required to be carried out at sufficient regularity such that the carrying amount is not materially different from the fair value at the end of the reporting period.
6.	The Companies Act specifies the depreciation rates to be used for different categories of assets. Component accounting is permitted but is rarely followed in practice.	Depreciation is based on the 'component' approach; depreciation is charged over the estimated useful life of the asset.
7.	There is no specific requirement to **reassess depreciation method**, residual value and useful life.	Depreciation method, residual value and useful life are reassessed at each balance sheet date.

GAAP Difference

Sl No	Indian GAAP	Ind AS
8.	In existing AS 6, change in depreciation method can be made only if the adoption of the new method is required by statute or for compliance with an accounting standard or if it is considered that the change would result in a more appropriate preparation or presentation of the financial statements.	Ind AS 16 requires that the depreciation method applied to an asset should be reviewed at least at each financial year-end and, <u>if there has been a significant change in the expected pattern of consumption of the future economic benefits embodied in the asset</u>, the method should be changed to reflect the changed pattern.
9.	In existing AS 6, it is considered as a change in accounting policy and treated accordingly.	Ind AS 16 requires that change in depreciation method should be considered as a change in accounting estimate and treated accordingly.

GAAP Difference

Sl No	Indian GAAP	Ind AS
10.	Existing AS 10 is silent on this aspect.	Ind AS 16 specifically provides that gains arising on derecognition of an item of property, plant and equipment should not be treated as revenue under Ind AS 115
11.	No such provision is there in existing AS 10.	Ind AS 16 deals with the situation where entities hold the items of property, plant and equipment for rental to others and subsequently sell the same. It shall transfer the item to inventory and book revenue under Ind AS 115. (Paragraph 68A of Ind AS 16)

Ind AS 40 - Investment property

Quick Check??

S. N.	Situation	Applicability of IAS-40?
1.	An entity has a factory which due to a decline in activity is no longer required and is now being held for sale.	Property held for sale and not investment property.
2.	Farming land is purchased for its investment potential. Planning permission has not been obtained for building construction of any kind.	Land held for long term capital appreciation and therefore investment property.
3.	A factory is in the process of being constructed on behalf of government.	Property being constructed for third party and covered under IAS 11 Construction Contracts.
4.	A new office building used by entity as its head office which was specifically in the center of major city in order to exploit its capital gain potential.	Building generates cashflow as part of larger org. Owner occupied property covered under IAS 16.

Case Study A

D Company bought a private jet for the use of its official purposes. The cost of the private jet is Rs. 100 crores. It is expected to be used over a period of 7 years. The engine of the jet has a useful life of 5 years. The private jet's tires are replaced every 2 years, Chasis for 10 years. It will require major overhaul every 3 year, costing Rs 5 Crs.

How should D recognize acquisition of Private jet? What will be its useful life?

Will your answer be different if the purpose of jet is to rent out on long term basis?

Case Study B

An entity purchased an asset selling at Rs. 20,00,000, net of a trade discount of Rs. 5,00,000. The asset was used in a jurisdiction that imposed a legal requirement on users to dismantle such assets at the end of their useful economic lives and dispose of them safely. The entity estimates that the present value of the cost of dismantling the asset at the end of its useful life is Rs. 4,00,000. The entity requested for a credit period of 1 year, for which the seller agreed subject to a reduction of Rs 1,00,000 from trade discount. Buyer gave a post dated cheque of Rs 21,00,000

What is the amount that should be included as the cost of PPE under the provisions of Ind AS 16?

(a) Rs. 19,00,000

(b) Rs. 25,00,000

(c) Rs. 24,00,000

(d) Rs. 20,00,000

Case Study C

Prime Limited is in the business of manufacturing Steel at its Plant in Odissa. It has vehicles in plant that ply employees and visitors within plant premises. On 1st January 2010 it exchanges its two year old Car X with a book value of INR 13,00,000 and a fair value of INR 14,50,000 with a vendor for cash of INR 1,50,000 and similar two year old Car Y which has a fair value of INR 13,00,000. Company policy is to depreciate vehicle over its estimated useful life of 12 years on SLM basis.

On January 1st 2012 it exchanges surplus land with a book value of INR 10 Crores for cash of INR 2Cr and machinery valued at INR 9 Crs. The machinery will optimize the steel purity post installation in the existing plant set up in January 1st 2000. The new machinery component has a useful life of 20 years. The Company depreciates its steel plant over its useful life of 20 years on SLM basis.

Prime limited follows calendar year for its financial statements.

What is the value of vehicle and new machinery component as on December 31 2013?

Solution C

The transaction lacks commercial substance as the company's cash flows are not expected to change as a result of the exchange; it is in the same position as it was before the transaction. There is no profit or loss in the transaction.

The entity recognises Car Y received at the book value of car X, less cash received. Therefore, it recognises cash of INR 200,000 and Car Y as property, plant and equipment with a carrying value of INR 11,00,000/-

Car Y will be depreciated over its remaining useful life of 10 years and thus depreciation for 3 years would be INR 4,12,500/-, WDV as on December 31st 2013 is INR 6,87,500/-

The transaction has commercial substance as the new machinery component will add to quality of the product and thus gives an advantage over competitors. The machinery component would be recorded at INR 9 Cr and profit of Rs 1 Cr on sale of land. Assuming Nil residual value, the component will be depreciated over the remaining useful life of the parent asset ie Plant, over a period of 9 years. WDV of the component as on December 31 2013 is INR 8 Crs. (9 Crs less depreciation of Rs 1 Cr)

Case Study D

C Ltd revalued its Property Plant and equipment by 10% and passed an entry debiting PPE and credited Revaluation reserve in Statement of Other Comprehensive Income by Rs. 50 lakhs.

In a subsequent year, due to huge fluctuation in fair values in the economy the valuer was engaged again and the revalued amount resulted in a net decrease by Rs. 15 lakhs. The revaluation decrease shall be accounted as:

a) A charge to Profit and loss account of Rs. 15 lakhs
b) A charge to revaluation reserve in Statement of Other Comprehensive income of Rs. 15 lakhs
c) A charge to Profit and loss account of Rs. 35 lakhs
d) A charge to Revaluation reserve in Statement of Other Comprehensive income of Rs. 35 lakhs.

Case Study E

On April 1, 2012 an entity acquired a land for Rs. 5,00,000 including Rs.10,000 non-refundable purchase taxes. The purchase agreement provided for payment to be made in full on March 31, 2013.

Legal fees of Rs. 3,000 were incurred in acquiring the land and paid on April 1, 2012. The land is held for capital appreciation. An appropriate discount rate is 10 per cent per annum.

The entity shall measure the initial cost of the land at:

(a) Rs. 5,03,000

(b) Rs. 5,13,000

(c) Rs. 4,93,000

(d) Rs. 4,57,545

IAS / Ind AS 38
Intangible assets

Intangible Assets – IAS 38 / Ind AS 38

1. Finite v/s Indefinite
2. Research and Development cost
3. Internally generated brands, mastheads, customers lists
4. Intangibles in Business Combination e.g. ??
5. Past expenses
6. Revaluation model
7. Amortization period – Goodwill on Merger
8. Impairment
9. Defensive Intangibles!
10. Service Concession!

Case 1

Which of the following intangible is prohibited from being recognised as an asset?

(a) Separately acquired intangible.

(b) Acquired through exchange of intangible asset.

(c) Acquired through amalgamation in the nature of purchase.

(d) Internally generated goodwill

Answer d)

Case 2

Which of the following statements relating to intangible asset is correct?

(a) The development expenses, cost of internal project also to be expensed as incurred unless they meet the asset recognition criteria.

(b) An amount expensed can be added back to cost when the intangible meets the asset recognition criteria.

(c) An asset should never be capitalised unless it has physical substance.

(d) Revaluation model allows the initial recognition of asset at amount other than cost.

Answer a)

Case 3

Which of the following cost does not form part of cost of internally generated intangible asset?

(a) Expenditure on materials and services used or consumed in developing the intangible asset.

(b) Selling, administrative overheads, not directly attributable.

(c) Salaries, wages, cost of personnel engaged in developing the intangible asst.

(d) Any expenditure directly attributable to the generation of intangible asset.

Answer b)

Case 4

Rolex Ltd has incurred Rs 10,00,000 of research expenditure on a project to develop a new type of watch moment which was under research phase. It had registered a few patents in its name. Timex purchases the research project, including certain patents that have been registered by Rolex for Rs 25,00,000.

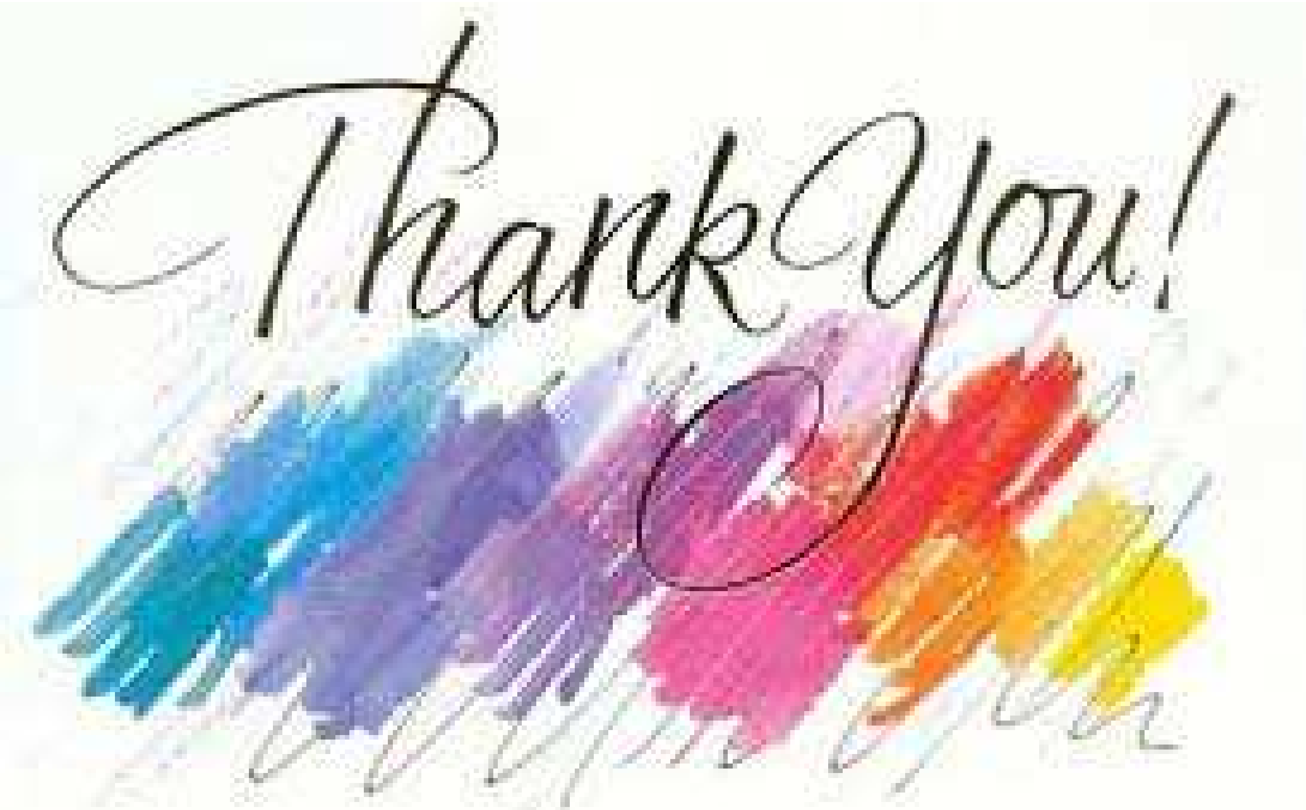
Subsequently, Timex incurs Rs 20,00,000 of expenditure on completing the research phase and decides to develop the product commercially. It incurs a further INR 300,000 of costs in bringing the product to a stage where the conditions for recognising development costs as an internally generated intangible asset are met.

Further costs of Rs 10 Crs are incurred in bringing the product into a condition where it is ready for use in the manner that management intend. Initial marketing costs and losses are incurred of Rs 9,00,000 before the product reaches the target audience

What is the accounting for the costs in the books of Rolex and Timex?

Solution 4

- Rolex expenses the amount of Rs 10 Lacs during the research phase.
- Timex recognises Rs 25,00,000 as the cost of the acquired research project. The subsequent research costs of Rs 20,00,000 may not be recognised and must be expensed as incurred.
- The subsequent development costs incurred of Rs 300,000 do not meet the conditions for recognition and are expensed as incurred.
- Further development costs of Rs 10 Cr must be recognised, because they meet the conditions for recognition as an intangible asset.
- The previously written off development costs are not reinstated.
- The marketing costs and initial losses of Rs 9,00,000 are expensed as incurred.
- The intangible asset's carrying amount when production and sale of the product commences is, therefore, Rs 10.25 Crs.


Thank You!