

APPLICABILITY OF ACCOUNTING STANDARDS



LEARNING OUTCOMES

After studying this chapter, you will be able to:

- ◆ Comprehend the status of Accounting Standards;
- ◆ Understand the applicability of Accounting Standards.

CHAPTER OVERVIEW



Status of
AS

Applicability of AS
for Corporate
Entities

Applicability
of AS for
Non-Corporate Entities



1. STATUS OF ACCOUNTING STANDARDS

It has already been mentioned in chapter 1 that the standards are developed by the Accounting Standards Board (ASB) of the Institute of Chartered Accountants of India and are issued under the authority of its Council which are approved by the MCA (Ministry of Corporate Affairs) for Corporate entities. The standards cannot override laws and local regulations. The Accounting Standards are nevertheless made mandatory from the dates notified by the MCA and are generally applicable to all enterprises, subject to certain exceptions as stated below. The implication of mandatory status of an Accounting Standard depends on whether the statute governing the enterprise concerned requires compliance with the Standard, e.g., the Ministry of Corporate Affairs have notified Accounting Standards for companies incorporated under the Companies Act, 1956 (or the Companies Act, 2013).

In assessing whether an accounting standard is applicable, one must find correct answer to the following three questions.

- (a) Does it apply to the enterprise concerned? If yes, the next question is:
- (b) Does it apply to the financial statement concerned? If yes, the next question is:
- (c) Does it apply to the financial item concerned?

The preface to the statements of accounting standards answers the above questions.

Enterprises to which the accounting standards apply?

Accounting Standards apply in respect of any enterprise (whether organised in corporate, co-operative or other forms) engaged in commercial, industrial or business activities, whether or not profit oriented and even if established for charitable or religious purposes. Accounting Standards, however, do not apply to enterprises solely carrying on the activities, which are not of commercial, industrial or business nature, (e.g., an activity of collecting donations and giving them to flood affected people). Exclusion of an enterprise from the applicability of the Accounting Standards would be permissible only if no part of the activity of such

enterprise is commercial, industrial or business in nature. Even if a very small proportion of the activities of an enterprise were considered to be commercial, industrial or business in nature, the Accounting Standards would apply to all its activities including those, which are not commercial, industrial or business in nature.

Implication of mandatory status

Where the statute governing the enterprise does not require compliance with the accounting standards, e.g. a partnership firm, the mandatory status of an accounting standard implies that, in discharging their attest functions, the members of the Institute are required to examine whether the financial statements are prepared in compliance with the applicable accounting standards. In the event of any deviation from the accounting standards, they have the duty to make adequate disclosures in their reports so that the users of financial statements may be aware of such deviations. It should nevertheless be noted that responsibility for the preparation of financial statements and for making adequate disclosure is that of the management of the enterprise. The auditor's responsibility is to form his opinion and report on such financial statements.

Section 129 (1) of the Companies Act, 2013 requires companies to present their financial statements in accordance with the accounting standards notified under Section 133 of the Companies Act, 2013 (refer Note below). Also, the auditor is required by Section 143(3)(e) to report whether, in his opinion, the financial statements of the company audited, comply with the accounting standards referred to in Section 133 of the Companies Act, 2013. Where the financial statements of a company do not comply with the accounting standards, the company should disclose in its financial statements, the deviation from the accounting standards, the reasons for such deviation and the financial effects, if any, arising out of such deviations as per Section 129(5) of the Companies Act, 2013. Provided also that the financial statements should not be treated as not disclosing a true and fair view of the state of affairs of the company, merely by reason of the fact that they do not disclose—

- (a) in the case of an insurance company, any matters which are not required to be disclosed by the Insurance Act, 1938, or the Insurance Regulatory and Development Authority Act, 1999;

- (b) in the case of a banking company, any matters which are not required to be disclosed by the Banking Regulation Act, 1949;
- (c) in the case of a company engaged in the generation or supply of electricity, any matters which are not required to be disclosed by the Electricity Act, 2003;
- (d) in the case of a company governed by any other law for the time being in force, any matters which are not required to be disclosed by that law.

Note: As per the Companies Act, 2013, the Central Government may prescribe standards of accounting or addendum thereto, as recommended by the Institute of Chartered Accountants of India, in consultation with the National Financial Reporting Authority (NFRA).

Financial items to which the accounting standards apply

The Accounting Standards are intended to apply only to items, which are material. An item is considered material, if its omission or misstatement is likely to affect economic decision of the user. Materiality is not necessarily a function of size; it is the information content i.e. the financial item which is important. A penalty of ₹ 50,000 paid for breach of law by a company can seem to be a relatively small amount for a company incurring crores of rupees in a year, yet is a material item because of the information it conveys. The materiality should, therefore, be judged on a case-to-case basis. If an item is material, it should be shown separately instead of clubbing it with other items. For example, it is not appropriate to club the penalties paid with legal charges.

Accounting Standards and Income Tax Act, 1961

Accounting standards intend to reduce diversity in application of accounting principles. They improve comparability of financial statements and promote transparency and fairness in their presentation. Deductions and exemptions allowed in computation of taxable income on the other hand, is a matter of fiscal policy of the government.

Thus, an expense required to be taken to the Statement of profit and loss by an accounting standard does not imply that the same is always deductible for income tax purposes. For example, depreciation on assets taken on finance lease is charged in the books of lessee as per AS 19 but depreciation for tax purposes is allowed to lessor, being legal owner of the asset, rather than to lessee. Likewise, recognition

of revenue in the financial statements cannot be avoided simply because it is exempted under Section 10 of the Income Tax Act, 1961.

Income Computation and Disclosure Standards

Section 145(2) of the Income Tax Act, 1961, empowers the Central Government to notify in the Official Gazette from time to time, Income Computation and Disclosure Standards to be followed by any class of assesses or in respect of any class of income. Accordingly, the Central Government has, in exercise of the powers conferred under Section 145(2) of the Income Tax Act, 1961, notified ten Income Computation and Disclosure Standards (ICDSs) to be followed by all assesses (other than an individual or a Hindu undivided family who is not required to get his accounts of the previous year audited in accordance with the provisions of Section 44AB of the Income Tax Act, 1961) following the mercantile system of accounting, for the purposes of computation of income chargeable to income-tax under the head "Profit and gains of business or profession" or "Income from other sources", from the Assessment Year (A.Y.) 2017-18. The ten notified ICDSs are:

ICDS I : Accounting Policies

ICDS II : Valuation of Inventories

ICDS III : Construction Contracts

ICDS IV : Revenue Recognition

ICDS V : Tangible Fixed Assets

ICDS VI : The Effects of Changes in Foreign Exchange Rates

ICDS VII : Government Grants

ICDS VIII : Securities

ICDS IX : Borrowing Costs

ICDS X : Provisions, Contingent Liabilities and Contingent Assets

2. APPLICABILITY OF ACCOUNTING STANDARDS

For the purpose of compliance of the accounting Standards, the ICAI has issued an announcement on 'Criteria for Classification of Entities and Applicability of Accounting Standards'. As per the announcement, entities are classified into four levels. Level IV, Level III and Level II entities as per the said Announcement were referred to as Micro, Small and Medium Entities (MSMEs).

However, when the accounting standards were notified by the Central Government in consultation with the National Advisory Committee on Accounting Standards*, the Central Government also issued the 'Criteria for Classification of Entities and Applicability of Accounting Standards' for the companies.

According to the 'Criteria for Classification of Entities and Applicability of Accounting Standards' as issued by the Government, there are two levels, namely, Small and Medium-sized Companies (SMCs) as defined in the Companies (Accounting Standards) Rules, 2021 and companies other than SMCs (Non-SMCs). Non-SMCs are required to comply with all the Accounting Standards in their entirety, while certain exemptions/ relaxations have been given to SMCs.

"Criteria for Classification of Entities and Applicability of Accounting Standards" for corporate entities and non-corporate entities have been explained in the coming paragraphs.

2.1. Criteria for classification of Non-company entities for applicability of Accounting Standards

The Council of the ICAI, at its 400th meeting, held on March 18-19, 2021, considered the matter relating to applicability of Accounting Standards issued by the ICAI, to Non-company entities (Enterprises). The scheme for applicability of

*The Companies Act, 1956 is being replaced by the Companies Act 2013 in a phased manner. Now, as per Section 133 of the Companies Act, 2013, the Central Government may prescribe the standards of accounting or any addendum thereto, as recommended by the Institute of Chartered Accountants of India, constituted under section 3 of the Chartered Accountants Act, 1949, in consultation with and after examination of the recommendations made by the National Financial Reporting Authority (NFRA). Section 132 of the Companies Act, 2013 deals with constitution of NFRA..

Accounting Standards to Non-company entities shall come into effect in respect of accounting periods commencing on or after 1 April 2020.

1. For the purpose of applicability of Accounting Standards, Non-company entities are classified into four categories, viz., Level I, Level II, Level III and Level IV.

Level I entities are large size entities, Level II entities are medium size entities, Level III entities are small size entities and Level IV entities are micro entities. Level IV, Level III and Level II entities are referred to as Micro, Small and Medium size entities (MSMEs). The criteria for classification of Non-company entities into different levels are given in Annexure 1.

The terms 'Small and Medium Enterprise' and 'SME' used in Accounting Standards shall be read as 'Micro, Small and Medium size entity' and 'MSME' respectively.

2. Level I entities are required to comply in full with all the Accounting Standards.
3. Certain exemptions/relaxations have been provided to Level II, Level III and Level IV Non-company entities. Applicability of Accounting Standards and exemptions/relaxations to such entities are given in Annexure 2.
4. This Announcement supersedes the earlier Announcement of the ICAI on '**Harmonisation of various differences between the Accounting Standards issued by the ICAI and the Accounting Standards notified by the Central Government**' issued in February 2008, to the extent it prescribes the criteria for classification of Non-company entities (Non-corporate entities) and applicability of Accounting Standards to non-company entities, and the Announcement '**Revision in the criteria for classifying Level II non-corporate entities**' issued in January 2013.
5. This Announcement is not relevant for Non-company entities who may be required to follow Ind AS as per relevant regulatory requirements applicable to such entities. recurrence

Annexure 1**Criteria for classification of Non-company Entities as decided by the Institute of Chartered Accountants of India****Level I Entities**

Non-company entities which fall in any one or more of the following categories, at the end of the relevant accounting period, are classified as Level I entities:

- (i) Entities whose securities are listed or are in the process of listing on any stock exchange, whether in India or outside India.
- (ii) Banks (including co-operative banks), financial institutions or entities carrying on insurance business.
- (iii) All entities engaged in commercial, industrial or business activities, whose turnover (excluding other income) exceeds rupees two-fifty crore in the immediately preceding accounting year.
- (iv) All entities engaged in commercial, industrial or business activities having borrowings (including public deposits) in excess of rupees fifty crore at any time during the immediately preceding accounting year.
- (v) Holding and subsidiary entities of any one of the above.

Level II Entities

Non-company entities which are not Level I entities but fall in any one or more of the following categories are classified as Level II entities:

- (i) All entities engaged in commercial, industrial or business activities, whose turnover (excluding other income) exceeds rupees fifty crore but does not exceed rupees two-fifty crore in the immediately preceding accounting year.
- (ii) All entities engaged in commercial, industrial or business activities having borrowings (including public deposits) in excess of rupees ten crore but not in excess of rupees fifty crore at any time during the immediately preceding accounting year.
- (iii) Holding and subsidiary entities of any one of the above.

Level III Entities

Non-company entities which are not covered under Level I and Level II but fall in any one or more of the following categories are classified as Level III entities:

- (i) All entities engaged in commercial, industrial or business activities, whose turnover (excluding other income) exceeds rupees ten crore but does not exceed rupees fifty crore in the immediately preceding accounting year.
- (ii) All entities engaged in commercial, industrial or business activities having borrowings (including public deposits) in excess of rupees two crore but does not exceed rupees ten crore at any time during the immediately preceding accounting year.
- (iii) Holding and subsidiary entities of any one of the above.

Level IV Entities

Non-company entities which are not covered under Level I, Level II and Level III are considered as Level IV entities.

Additional requirements

- (1) An MSME which avails the exemptions or relaxations given to it shall disclose (by way of a note to its financial statements) the fact that it is an MSME, the Level of MSME and that it has complied with the Accounting Standards insofar as they are applicable to entities falling in Level II or Level III or Level IV, as the case may be.
- (2) Where an entity, being covered in Level II or Level III or Level IV, had qualified for any exemption or relaxation previously but no longer qualifies for the relevant exemption or relaxation in the current accounting period, the relevant standards or requirements become applicable from the current period and the figures for the corresponding period of the previous accounting period need not be revised merely by reason of its having ceased to be covered in Level II or Level III or Level IV, as the case may be. The fact that the entity was covered in Level II or Level III or Level IV, as the case may be, in the previous period and it had availed of the exemptions or relaxations available to that Level of entities shall be disclosed in the notes to the financial statements. The fact that previous period figures have not been revised shall also be disclosed in the notes to the financial statements.

- (3) Where an entity has been covered in Level I and subsequently, ceases to be so covered and gets covered in Level II or Level III or Level IV, the entity will not qualify for exemption/relaxation available to that Level, until the entity ceases to be covered in Level I for two consecutive years. Similar is the case in respect of an entity, which has been covered in Level II or Level III and subsequently, gets covered under Level III or Level IV.
- (4) If an entity covered in Level II or Level III or Level IV opts not to avail of the exemptions or relaxations available to that Level of entities in respect of any but not all of the Accounting Standards, it shall disclose the Standard(s) in respect of which it has availed the exemption or relaxation.
- (5) If an entity covered in Level II or Level III or Level IV opts not to avail any one or more of the exemptions or relaxations available to that Level of entities, it shall comply with the relevant requirements of the Accounting Standard.
- (6) An entity covered in Level II or Level III or Level IV may opt for availing certain exemptions or relaxations from compliance with the requirements prescribed in an Accounting Standard:

Provided that such a partial exemption or relaxation and disclosure shall not be permitted to mislead any person or public.

- (7) In respect of Accounting Standard (AS) 15, *Employee Benefits*, exemptions/relaxations are available to Level II and Level III entities, under two sub-classifications, viz., (i) entities whose average number of persons employed during the year is 50 or more, and (ii) entities whose average number of persons employed during the year is less than 50. The requirements stated in paragraphs (1) to (6) above, mutatis mutandis, apply to these sub-classifications.

Annexure 2**Applicability of Accounting Standards to Non-company Entities**

The Accounting Standards issued by the ICAI, as on April 1, 2020, and such standards as issued from time-to-time are applicable to Non-company entities subject to the relaxations and exemptions in the announcement. The Accounting Standards issued by ICAI as on April 1, 2020, are:

AS 1	Disclosure of Accounting Policies
AS 2	Valuation of Inventories
AS 3	Cash Flow Statements
AS 4	Contingencies and Events Occurring After the Balance Sheet Date
AS 5	Net Profit or Loss for the Period, Prior Period Items and Changes in Accounting Policies
AS 7	Construction Contracts
AS 9	Revenue Recognition
AS 10	Property, Plant and Equipment
AS 11	The Effects of Changes in Foreign Exchange Rates
AS 12	Accounting for Government Grants
AS 13	Accounting for Investments
AS 14	Accounting for Amalgamations
AS 15	Employee Benefits
AS 16	Borrowing Costs
AS 17	Segment Reporting
AS 18	Related Party Disclosures
AS 19	Leases
AS 20	Earnings Per Share
AS 21	Consolidated Financial Statements
AS 22	Accounting for Taxes on Income

AS 23	Accounting for Investments in Associates in Consolidated Financial Statements
AS 24	Discontinuing Operations
AS 25	Interim Financial Reporting
AS 26	Intangible Assets
AS 27	Financial Reporting of Interests in Joint Ventures
AS 28	Impairment of Assets
AS 29	Provisions, Contingent Liabilities and Contingent Assets

(1) Applicability of the Accounting Standards to Level 1 Non- company entities.

Level I entities are required to comply in full with all the Accounting Standards.

(2) Applicability of the Accounting Standards and exemptions/relaxations for Level II, Level III and Level IV Non-company entities

(A) Accounting Standards applicable to Non-company entities

AS	Level II Entities	Level III Entities	Level IV Entities
AS 1	Applicable	Applicable	Applicable
AS 2	Applicable	Applicable	Applicable
AS 3	Not Applicable	Not Applicable	Not Applicable
AS 4	Applicable	Applicable	Applicable
AS 5	Applicable	Applicable	Applicable
AS 7	Applicable	Applicable	Applicable
AS 9	Applicable	Applicable	Applicable
AS 10	Applicable	Applicable with disclosures exemption	Applicable with disclosures exemption

AS 11	Applicable	Applicable with disclosures exemption	Applicable with disclosures exemption	with
AS 12	Applicable	Applicable	Applicable	
AS 13	Applicable	Applicable	Applicable with disclosures exemption	with
AS 14	Applicable	Applicable	Not Applicable (Refer note 2(C))	
AS 15	Applicable with exemptions	Applicable with exemptions	Applicable with exemptions	with
AS 16	Applicable	Applicable	Applicable	
AS 17	Not Applicable	Not Applicable	Not Applicable	
AS 18	Applicable	Not Applicable	Not Applicable	
AS 19	Applicable with disclosures exemption	Applicable with disclosures exemption	Applicable with disclosures exemption	with
AS 20	Not Applicable	Not Applicable	Not Applicable	
AS 21	Not Applicable (Refer note 2(D))	Not Applicable (Refer note 2(D))	Not Applicable (Refer note 2(D))	
AS 22	Applicable	Applicable	Applicable only for current tax related provisions (Refer note 2(B)(vi))	
AS 23	Not Applicable (Refer note 2(D))	Not Applicable (Refer note 2(D))	Not Applicable (Refer note 2(D))	
AS 24	Applicable	Not Applicable	Not Applicable	
AS 25	Not Applicable (Refer note 2(D))	Not Applicable (Refer note 2(D))	Not Applicable (Refer note 2(D))	

AS 26	Applicable		Applicable		Applicable with disclosures exemption
AS 27	Not Applicable (Refer notes 2(C) and 2(D))	2(C)	Not Applicable (Refer notes 2(C) and 2(D))	2(C) and 2(D))	Not Applicable (Refer notes 2(C) and 2(D))
AS 28	Applicable disclosures exemption	with	Applicable disclosures exemption	with	Not Applicable
AS 29	Applicable disclosures exemption	with	Applicable disclosures exemption	with	Applicable disclosures exemption

(B) Accounting Standards in respect of which relaxations/exemptions from certain requirements have been given to Level II, Level III and Level IV Non-company entities:

- (i) Accounting Standard (AS) 10, Property, Plant and Equipments
Paragraph 87 relating to encouraged disclosures is not applicable to Level III and Level IV Non-company entities.
- (ii) AS 11, The Effects of Changes in Foreign Exchange Rates (revised 2018)
Paragraph 44 relating to encouraged disclosures is not applicable to Level III and Level IV Non-company entities.
- (iii) AS 13, Accounting for Investments
Paragraph 35(f) relating to disclosures is not applicable to Level IV Non-company entities.
- (iv) Accounting Standard (AS) 15, Employee Benefits (revised 2005)
 - (1) Level II and Level III Non-company entities whose average number of persons employed during the year is 50 or more are exempted from the applicability of the following paragraphs:
 - (a) paragraphs 11 to 16 of the standard to the extent they deal with recognition and measurement of short-term accumulating compensated absences which are non-vesting

- (i.e., short-term accumulating compensated absences in respect of which employees are not entitled to cash payment for unused entitlement on leaving);
- (b) paragraphs 46 and 139 of the Standard which deal with discounting of amounts that fall due more than 12 months after the balance sheet date;
 - (c) recognition and measurement principles laid down in paragraphs 50 to 116 and presentation and disclosure requirements laid down in paragraphs 117 to 123 of the Standard in respect of accounting for defined benefit plans. However, such entities should actuarially determine and provide for the accrued liability in respect of defined benefit plans by using the Projected Unit Credit Method and the discount rate used should be determined by reference to market yields at the balance sheet date on government bonds as per paragraph 78 of the Standard. Such entities should disclose actuarial assumptions as per paragraph 120(l) of the Standard; and
 - (d) recognition and measurement principles laid down in paragraphs 129 to 131 of the Standard in respect of accounting for other long-term employee benefits. However, such entities should actuarially determine and provide for the accrued liability in respect of other long-term employee benefits by using the Projected Unit Credit Method and the discount rate used should be determined by reference to market yields at the balance sheet date on government bonds as per paragraph 78 of the Standard.
- (2) Level II and Level III Non-company entities whose average number of persons employed during the year is less than 50 and Level IV Non-company entities irrespective of number of employees are exempted from the applicability of the following paragraphs:
- (a) paragraphs 11 to 16 of the standard to the extent they deal with recognition and measurement of short-term accumulating compensated absences which are non-vesting (i.e., short-term accumulating compensated absences in

- respect of which employees are not entitled to cash payment for unused entitlement on leaving);
- (b) paragraphs 46 and 139 of the Standard which deal with discounting of amounts that fall due more than 12 months after the balance sheet date;
 - (c) recognition and measurement principles laid down in paragraphs 50 to 116 and presentation and disclosure requirements laid down in paragraphs 117 to 123 of the Standard in respect of accounting for defined benefit plans. However, such entities may calculate and account for the accrued liability under the defined benefit plans by reference to some other rational method, e.g., a method based on the assumption that such benefits are payable to all employees at the end of the accounting year; and
 - (d) recognition and measurement principles laid down in paragraphs 129 to 131 of the Standard in respect of accounting for other long-term employee benefits. Such entities may calculate and account for the accrued liability under the other long-term employee benefits by reference to some other rational method, e.g., a method based on the assumption that such benefits are payable to all employees at the end of the accounting year.
- (v) AS 19, Leases
- (a) Paragraphs 22 (c),(e) and (f); 25 (a), (b) and (e); 37 (a) and (f); and 46 (b) and (d) relating to disclosures are not applicable to Level II Non-company entities.
 - (b) Paragraphs 22 (c),(e) and (f); 25 (a), (b) and (e); 37 (a), (f) and (g); and 46 (b), (d) and (e) relating to disclosures are not applicable to Level III Non-company entities.
 - (c) Paragraphs 22 (c),(e) and (f); 25 (a), (b) and (e); 37 (a), (f) and (g); 38; and 46 (b), (d) and (e) relating to disclosures are not applicable to Level IV Non-company entities.

- (vi) AS 22, Accounting for Taxes on Income
 - (a) Level IV Non-company entities shall apply the requirements of AS 22, Accounting for Taxes on Income, for Current tax defined in paragraph 4.4 of AS 22, with recognition as per paragraph 9, measurement as per paragraph 20 of AS 22, and presentation and disclosure as per paragraphs 27-28 of AS 22.
 - (b) Transitional requirements

On the first occasion when a Non-company entity gets classified as Level IV entity, the accumulated deferred tax asset/liability appearing in the financial statements of immediate previous accounting period, shall be adjusted against the opening revenue reserves.
- (vii) AS 26, Intangible Assets

Paragraphs 90(d)(iii); 90(d)(iv) and 98 relating to disclosures are not applicable to Level IV Non-company entities.
- (viii) AS 28, Impairment of Assets
 - (a) Level II and Level III Non-company entities are allowed to measure the 'value in use' on the basis of reasonable estimate thereof instead of computing the value in use by present value technique. Consequently, if Level II or Level III Non-company entity chooses to measure the 'value in use' by not using the present value technique, the relevant provisions of AS 28, such as discount rate etc., would not be applicable to such an entity. Further, such an entity need not disclose the information required by paragraph 121(g) of the Standard.
 - (b) Also, paragraphs 121(c) (ii); 121(d) (i); 121(d) (ii) and 123 relating to disclosures are not applicable to Level III Non-company entities.
- (ix) AS 29, Provisions, Contingent Liabilities and Contingent Assets (revised 2016)

Paragraphs 66 and 67 relating to disclosures are not applicable to Level II, Level III and Level IV Non-company entities.

- (C) In case of Level IV Non-company entities, generally there are no such transactions that are covered under AS 14, Accounting for Amalgamations, or jointly controlled operations or jointly controlled assets covered under AS 27, Financial Reporting of Interests in Joint Ventures. Therefore, these standards are not applicable to Level IV Non-company entities. However, if there are any such transactions, these entities shall apply the requirements of the relevant standard.
- (D) AS 21, Consolidated Financial Statements, AS 23, Accounting for Investments in Associates in Consolidated Financial Statements, AS 27, Financial Reporting of Interests in Joint Ventures (to the extent of requirements relating to Consolidated Financial Statements), and AS 25, Interim Financial Reporting, do not require a Non-company entity to present consolidated financial statements and interim financial report, respectively. Relevant AS is applicable only if a Non-company entity is required or elects to prepare and present consolidated financial statements or interim financial report.

Example 1

M/s Omega & Co. (a partnership firm), had a turnover of ₹ 1.25 crores (excluding other income) and borrowings of ₹ 0.95 crores in the previous year. It wants to avail the exemptions available in application of Accounting Standards to non-corporate entities for the year ended 31.3.20X1. Advise the management of M/s Omega & Co in respect of the exemptions of provisions of ASs, as per the directive issued by the ICAI.

Solution

The question deals with the issue of Applicability of Accounting Standards to a non-corporate entity. For availment of the exemptions, first of all, it has to be seen that M/s Omega & Co. falls in which level of the non-corporate entities. Its classification will be done on the basis of the classification of non-corporate entities as prescribed by the ICAI. According to the ICAI, non-corporate entities can be classified under 4 levels viz Level I, Level II, Level III and Level IV entities.

Non-corporate entities which meet following criteria are classified as Level IV entities:

- (i) All entities engaged in commercial, industrial or business activities, whose turnover (excluding other income) does not exceed rupees ten crores in the immediately preceding accounting year.
- (ii) All entities engaged in commercial, industrial or business activities having borrowings (including public deposits) does not exceed rupees two crores at any time during the immediately preceding accounting year.
- (iii) Holding and subsidiary entities of any one of the above.

As the turnover of M/s Omega & Co. is less than ₹ 10 crores and borrowings less than ₹ 2 crores, it falls under Level IV non-corporate entities. In this case, AS 3, AS 14, AS 17, AS 18, AS 20, AS 21, AS 23, AS 24, AS 25, AS 27 and AS 28 will not be applicable to M/s Omega & Co. Relaxations from certain requirements in respect of AS 10, AS 11, AS 13, AS 15, AS 19, AS 22, AS 26 and AS 29 are also available to M/s Omega & Co.

2.2 Criteria for classification of Companies under the Companies (Accounting Standards) Rules, 2021

Small and Medium-Sized Company (SMC) as defined in Clause 2(e) of the Companies (Accounting Standards) Rules, 2021:

“Small and Medium Sized Company” (SMC) means, a company-

- (i) whose equity or debt securities are not listed or are not in the process of listing on any stock exchange, whether in India or outside India;
- (ii) which is not a bank, financial institution or an insurance company;
- (iii) whose turnover (excluding other income) does not exceed rupees two-fifty crores in the immediately preceding accounting year;
- (iv) which does not have borrowings (including public deposits) in excess of rupees fifty crores at any time during the immediately preceding accounting year; and
- (v) which is not a holding or subsidiary company of a company which is not a small and medium-sized company.

Explanation: For the purposes of clause 2(e), a company should qualify as a Small and Medium Sized Company, if the conditions mentioned therein are satisfied as at the end of the relevant accounting period.

Non-SMCs

Companies not falling within the definition of SMC are considered as Non-SMCs.

Instructions

- **General Instructions**

1. SMCs should follow the following instructions while complying with Accounting Standards under these Rules:

1.1 The SMC which does not disclose certain information pursuant to the exemptions or relaxations given to it should disclose (by way of a note to its financial statements) the fact that it is an SMC and has complied with the Accounting Standards insofar as they are applicable to an SMC on the following lines:

“The Company is a Small and Medium Sized Company (SMC) as defined in the Companies (Accounting Standards) Rules, 2021 notified under the Companies Act, 2013. Accordingly, the Company has complied with the Accounting Standards as applicable to a Small and Medium Sized Company.”

1.2 Where a company, being an SMC, has qualified for any exemption or relaxation previously but no longer qualifies for the relevant exemption or relaxation in the current accounting period, the relevant standards or requirements become applicable from the current period and the figures for the corresponding period of the previous accounting period need not be revised merely by reason of its having ceased to be an SMC. The fact that the company was an SMC in the previous period and it had availed of the exemptions or relaxations available to SMCs should be disclosed in the notes to the financial statements.

1.3 If an SMC opts not to avail of the exemptions or relaxations available to an SMC in respect of any but not all of the Accounting Standards, it should

disclose the standard(s) in respect of which it has availed the exemption or relaxation.

1.4 If an SMC desires to disclose the information not required to be disclosed pursuant to the exemptions or relaxations available to the SMCs, it should disclose that information in compliance with the relevant accounting standard.

1.5 The SMC may opt for availing certain exemptions or relaxations from compliance with the requirements prescribed in an Accounting Standard:

Provided that such a partial exemption or relaxation and disclosure should not be permitted to mislead any person or public.

Note:

An existing company which was previously not a SMC and subsequently becomes a SMC, shall not be qualified for exemption or relaxation in respect of Accounting Standards available to a SMC until the company remains a SMC for two consecutive accounting periods.

2.3 Applicability of Accounting Standards to Companies other than those following Indian Accounting Standards (Ind AS)¹

2.3.1 Accounting Standards applicable in their entirety to companies

- AS 1 Disclosures of Accounting Policies
- AS 2 Valuation of Inventories (revised 2016)
- AS 3 Cash Flow Statements
- AS 4 Contingencies and Events Occurring After the Balance Sheet Date (revised 2016)

¹ For applicability of Ind AS to companies, refer Notification dated 16th February, 2015, issued by the Ministry of Corporate Affairs, Government of India.

- AS 5 Net Profit or Loss for the Period, Prior Period Items and Changes in Accounting Policies
- AS 7 Construction Contracts (revised 2002)
- AS 9 Revenue Recognition
- AS 10 Property, Plant and Equipment
- AS 11 The Effects of Changes in Foreign Exchange Rates (revised 2003)
- AS 12 Accounting for Government Grants
- AS 13 Accounting for Investments (revised 2016)
- AS 14 Accounting for Amalgamations (revised 2016)
- AS 16 Borrowing Costs
- AS 18 Related Party Disclosures
- AS 21 Consolidated Financial Statements (revised 2016)
- AS 22 Accounting for Taxes on Income
- AS 23 Accounting for Investments in Associates in Consolidated Financial Statements
- AS 24 Discontinuing Operations
- AS 26 Intangible Assets
- AS 27 Financial Reporting of Interest in Joint Ventures

2.3.2 Exemptions or Relaxations for Small and Medium Sized Companies (SMCs) as defined in the Notification dated June 23, 2021, issued by the Ministry of Corporate Affairs, Government of India

- (1) *Accounting Standards not applicable to SMCs in their entirety:*
 - AS 17 Segment Reporting
- (2) *Accounting Standards in respect of which relaxations from certain requirements have been given to SMCs:*
 - (i) Accounting Standard (AS) 15, Employee Benefits (revised 2005)

- (a) paragraphs 11 to 16 of the standard to the extent they deal with recognition and measurement of short-term accumulating compensated absences which are non-vesting (i.e., short-term accumulating compensated absences in respect of which employees are not entitled to cash payment for unused entitlement on leaving);
 - (b) paragraphs 46 and 139 of the Standard which deal with discounting of amounts that fall due more than 12 months after the balance sheet date;
 - (c) recognition and measurement principles laid down in paragraphs 50 to 116 and presentation and disclosure requirements laid down in paragraphs 117 to 123 of the Standard in respect of accounting for defined benefit plans. However, such companies should actuarially determine and provide for the accrued liability in respect of defined benefit plans by using the Projected Unit Credit Method and the discount rate used should be determined by reference to market yields at the balance sheet date on government bonds as per paragraph 78 of the Standard. Such companies should disclose actuarial assumptions as per paragraph 120(l) of the Standard; and
 - (d) recognition and measurement principles laid down in paragraphs 129 to 131 of the Standard in respect of accounting for other long-term employee benefits. However, such companies should actuarially determine and provide for the accrued liability in respect of other long-term employee benefits by using the Projected Unit Credit Method and the discount rate used should be determined by reference to market yields at the balance sheet date on government bonds as per paragraph 78 of the Standard.
- (ii) AS 19, Leases
- Paragraphs 22 (c), (e) and (f); 25 (a), (b) and (e); 37 (a) and (f); and 46 (b) and (d) relating to disclosures are not applicable to SMCs.

- (iii) AS 20, Earnings Per Share
Disclosure of diluted earnings per share (both including and excluding extraordinary items) is exempted for SMCs.
 - (iv) AS 28, Impairment of Assets
SMCs are allowed to measure the 'value in use' on the basis of reasonable estimate thereof instead of computing the value in use by present value technique. Consequently, if an SMC chooses to measure the 'value in use' by not using the present value technique, the relevant provisions of AS 28, such as discount rate etc., would not be applicable to such an SMC. Further, such an SMC need not disclose the information required by paragraph 121(g) of the Standard.
 - (v) AS 29, Provisions, Contingent Liabilities and Contingent Assets (revised)
Paragraphs 66 and 67 relating to disclosures are not applicable to SMCs.
- (3) *AS 25, Interim Financial Reporting, does not require a company to present interim financial report. It is applicable only if a company is required or elects to prepare and present an interim financial report. Only certain Non-SMCs are required by the concerned regulators to present interim financial results, e.g., quarterly financial results required by the SEBI. Therefore, the recognition and measurement requirements contained in this Standard are applicable to those Non-SMCs for preparation of interim financial results.*

SUMMARY

According to the Criteria for Classification of Entities and Applicability of Accounting Standards as issued by the Government, there are two levels, namely, Small and Medium-sized Companies (SMCs) as defined in the Companies (Accounting Standards) Rules and companies other than SMCs. Non-SMCs are required to comply with all the Accounting Standards in their entirety, while certain exemptions/ relaxations have been given to SMCs. Criteria for classification of entities for applicability of accounting standards for corporate and non-corporate entities have been prescribed as per the Govt. notification.

TEST YOUR KNOWLEDGE

Multiple Choice Questions

1. *Non-corporate entities which are not Level I entities whose turnover (excluding other income) exceeds rupees _____ but does not exceed rupees two-fifty crores in the immediately preceding accounting year are classified as Level II entities.*

 - (a) five crores.*
 - (b) two crores.*
 - (c) fifty crores.*
 - (d) ten crores.*
2. *The following Accounting Standard is not applicable to Non-corporate Entities falling in Level II in its entirety*

 - (a) AS 10.*
 - (b) AS 17.*
 - (c) AS 2.*
 - (d) AS 13.*
3. *All non-corporate entities engaged in commercial, industrial and business reporting entities, whose turnover (excluding other income) exceeds rupees 250 crores in the immediately preceding accounting year, are classified as*

 - (a) Level II entities.*
 - (b) Level I entities.*
 - (c) Level III entities.*
 - (d) Level IV entities.*
4. *All non-corporate entities engaged in commercial, industrial or business activities having borrowings (including public deposits) in excess of rupees two crores but does not exceed rupees ten crores at any time during the immediately preceding accounting year.*

 - (a) Level II entities.*

- (b) Level IV entities.
 - (c) Level III entities.
 - (d) Level I entities.
5. "Small and Medium Sized Company" (SMC) means, a company-
- (a) which may be a bank, financial institution or an insurance company.
 - (b) whose turnover (excluding other income) does not exceed rupees two-fifty crores in the immediately preceding accounting year;
 - (c) whose turnover (excluding other income) does not exceed rupees fifty crores in the immediately preceding accounting year;
 - (d) whose turnover (excluding other income) does not exceed rupees five hundred crores in the immediately preceding accounting year.

Theoretical Questions

6. What are the issues, with which Accounting Standards deal?
7. List the criteria to be applied for rating a non-corporate entity as Level-I entity and Level II entity for the purpose of compliance of Accounting Standards in India.
8. List the criteria to be applied for rating a non-corporate entity as Level IV entity for the purpose of compliance of Accounting Standards in India.

Scenario based Question

9. XYZ Ltd., with a turnover of ₹50 crores during previous year and borrowings of ₹1 crore during any time in the previous year, wants to avail the exemptions available in adoption of Accounting Standards applicable to companies for the year ended 31.3.20X1. Advise the management on the exemptions that are available as per the Companies (Accounting Standards) Rules, 2021.
10. A company was classified as Non-SMC in 20X1-X2. In 20X2-X3, it has been classified as SMC. The management desires to avail the exemptions or relaxations available for SMCs in 20X2-X3. However, the accountant of the company does not agree with the same. Comment.

ANSWERS/HINTS

Answers to the Multiple Choice Questions

1	(c)	2	(b)	3	(b)	4	(c)	5	(b)
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Answers to the Theoretical Questions

- Accounting Standards deal with the issues of (i) Recognition of events and transactions in the financial statements, (ii) Measurement of these transactions and events, (iii) Presentation of these transactions and events in the financial statements in a manner that is meaningful and understandable to the reader, and (iv) Disclosure requirements.
- Refer para 1.2.1 for Criteria to be applied for rating a non-corporate entity as Level-I entity and Level II entity for the purpose of compliance of Accounting Standards in India.
- Refer para 1.2.1 for Criteria to be applied for rating a non-corporate entity as Level IV entity for the purpose of compliance of Accounting Standards in India.

Answers to the Scenario based Question

- The question deals with the issue of Applicability of Accounting Standards for corporate entities.

The companies can be classified under two categories viz SMCs and Non SMCs under the Companies (Accounting Standards) Rules, 2021.

As per the Companies (Accounting Standards) Rules, 2021, criteria for above classification as SMCs, are:

“Small and Medium Sized Company” (SMC) means, a company-

- whose equity or debt securities are not listed or are not in the process of listing on any stock exchange, whether in India or outside India;
- which is not a bank, financial institution or an insurance company;
- whose turnover (excluding other income) does not exceed rupees two-

fifty crores in the immediately preceding accounting year;

- which does not have borrowings (including public deposits) in excess of rupees fifty crores at any time during the immediately preceding accounting year; and
- which is not a holding or subsidiary company of a company which is not a small and medium-sized company.

Since, XYZ Ltd.'s turnover was ₹ 50 crores which does not exceed ₹ 250 crores and borrowings of ₹ 1 crore are less than ₹ 50 crores, it is a small and medium sized company (SMC).

- 10.** As per Companies (Accounting Standards) Rules, 2021, an existing company, which was previously not a SMC and subsequently becomes a SMC, should not be qualified for exemption or relaxation in respect of accounting standards available to a SMC until the company remains a SMC for two consecutive accounting periods. Therefore, the management of the company cannot avail the exemptions/ relaxations available to the SMCs for the FY 20X2-X3.