Regulatory Compliances – Schedule II & III of Companies Act, 2013

Awareness Programme on Financial Reporting Practices – Jamnagar Branch (WIRC)

12th November 2016

By CA Amit Purohit

Coverage

- Schedule II- Depreciation

- Schedule III- Financial statements-compliance disclosure requirements

Schedule –III (Background)

- Schedule III read with section 129 of the Companies Act, 2013 prescribes the format of the financial statements (i.e. Balance sheet and Statement of Profit and Loss) and general instructions for preparation of the same. Format of Cash flow statement is governed by AS-3.

- Schedule III of Companies Act, 2013 replaces Revised Schedule VI (with additional requirements for preparation of CFS).

- Recently, Schedule III amended to also prescribe format for Ind-AS compliant financial statements.

Overview

- If compliance with the requirements of the Act including Accounting Standards requires a change in the treatment or disclosure in the financial statements, then the changes as per the requirements of the Act/Accounting Standards shall be made and the requirements of Schedule III shall stand modified accordingly.

- Information relating to each item on the face of the Balance Sheet and the Statement of Profit & Loss to be disclosed in the notes with a cross reference.

Schedule III and AS

- Disclosure Requirements specified in Schedule III are **in addition to** and not in substitution of the Disclosure Requirements specified in Accounting Standards prescribed under the Companies Act.

- Additional Disclosures specified in the Accounting Standards to be made in the **Notes to Accounts** or by way of **Additional Statement**, unless required to be disclosed on the face of the Financial Statements.

- All other disclosures as required by the Companies Act to be made in the **Notes to Accounts** in addition to requirements set out in Schedule III.

Consolidated financial statements

- Requirement of Schedule III applies to Consolidated financial statements too. Earlier, consolidated financial statements were required only for listed companies.

- Additional information by way of parent / subsidiaries share in the net assets and profit or loss etc. are required to be given.

- Consolidated financial statements to be audited, approved and adopted in similar way as standalone financial statements.

Non-Compliance/Inadequate Disclosures	**Technical Requirement as per Schedule III**
<u>Operating Cycle</u>	
1.Non disclosure of the Operating Cycle	Operating Cycle should be disclosed especially, if it is beyond 12 months. Such disclosure would be of help to the users of FS where determination of operating cycle involves significant judgment. (Q34 of FAQs)
<u>Share Capital</u>	
1. Company having only one class of shares – Equity. It did not disclose rights, preferences and restrictions, if any w.r.t. such shares.	As per Para 6A(e), a Company has to disclose the rights, preferences and restrictions attaching to each class of shares, even if it has only class of shares.
2. Reconciliation of each class of shares outstanding was not disclosed	Para 6A(d) read with GN Para 8.1.1.9 mandates disclosure for each class of shares with opening number of shares outstanding, shares issued, bought back, other movements, etc and closing number of shares outstanding.

Non-Compliance/Inadequate Disclosures	**Technical Requirement as per Schedule III**
3. Disclosure made of shareholders holding more than 5% shares, from where it was noticed that there was a company holding more than 51% shares. However, disclosures regarding holding company not made.	As per Para 6A(f), company has to disclose in each class of shares, the shareholding of its holding company, or by subsidiaries or associates of the holding company or the holding company in aggregate.
4. Unpaid Calls not reflected as reduction from Share Capital but shown as receivable without adequate disclosure.	Para 6A(b) requires details of shares subscribed and fully paid up as well as shares subscribed and not fully paid up to be shown separately. Further, Para 6A(k) requires disclosure of calls unpaid, with a separate disclosure for the aggregate value of calls unpaid by directors and officers of the company. Hence gross amount of Share Capital should be disclosed first and then calls unpaid should be reflected as a deduction.(Refer Q45 of FAQs)

Non-Compliance/Inadequate Disclosures	Technical Requirement as per Schedule III
5.Share Application Money reflected as part of Share Capital	Share Application Money pending allotment is a separate line item after Shareholders' Funds and before Non-Current Liabilities.
<u>Reserves & Surplus</u>	
1.For each item only the final amount at the end were reflected, without the movements during the year.	As per Para 6B(i) additions and deductions since last balance sheet has to be shown under each of the specified heads.
2. Appropriations from Profit for the year were reflected on the face of the Statement of Profit and Loss.	This was the practice as per Old Schedule VI. However, as per Para 6B(i)(h), the appropriations and allocations such as dividend, transfer to/from reserves has to be through Reserves and Surplus after transfer of Surplus from Statement of Profit and Loss.

Non-Compliance/Inadequate Disclosures	**Technical Requirement as per Schedule III**
3.Debit Balance of Statement of Profit and Loss was reflected on Assets side of the Balance Sheet.	As per Para 6B(iii), debit balance of Statement of Profit & Loss shall be shown as a negative figure under the head surplus. Even, after adjusting the balances of other Reserves the final balance is negative, the same will continue to be reflected as a negative figure in Reserves and Surplus.
<u>Long Term and Short Term Borrowings</u>	
1. Secured Borrowings includes loan availed by creating charge on the property of a director and his personal security.	As per GN Para 8.3.1.13 and Q.14 of FAQs, if the borrowing is on security of promoters, shareholders or other third party, there has to be a disclosure of such security offered for borrowing. However, such security does not result in the classification of such borrowing as secured.

Non-Compliance/Inadequate Disclosures	Technical Requirement as per Schedule III
2. Current Maturities of Long Term Borrowings were reflected as Short Term Borrowings.	As per Para 6G(a) current maturities of Long Term Debts are to be disclosed under the head "Other Current Liabilities". GN Para 8.3.1.10 also reiterates that the current maturities of all long term borrowings will not be disclosed under "Short Term Borrowings".
3.Bonds/Debentures were disclosed with the type of bonds/debentures and rate of interest only.	As per Para 6C(iv) disclosure for bonds/debentures should also include particulars of redemption/conversion and shall be stated in descending order of maturity or conversion date.
4. Short Term Borrowings included Working Capital Limits, however separate disclosure was not made.	As per Para 6F(i)(a), Loans Repayable on Demand have to be disclosed separately with further break up (a) From Banks and (b) From Others Parties.

Non-Compliance/Inadequate Disclosures	**Technical Requirement as per Schedule III**
5. Classification of Loan as a non-current liability in the previous year, which on becoming a current liability during the current financial year, the company re-classifies the loan as current for previous year also.	Classification of current/non-current is as of a particular date i.e balance sheet date. If there is a change in classification during subsequent year it is so for that year. It would not change the position as of previous year and hence previous year classification should remain unchanged. (Refer Q.15 of FAQs).
6. A Convertible Debt instrument maturing after 2 years, where the conversion option for issuance of equity is exercisable by the holder at any time classified as "Short Term Borrowing".	The terms of settlement of a liability do not affect its classification. In the instant case the maturity for cash settlement was after 2 years and accordingly the same should have been classified as "Non-Current". (Refer GN Para 7.5.1).

Non-Compliance/Inadequate Disclosures	Technical Requirement as per Schedule III
Trade Payables	
1.Trade Payables includes dues payable in respect of statutory obligations like PF, dues towards purchase of fixed assets and other contractual obligations.	Any Payable which is in respect of amount due towards goods purchased or services received in the ordinary course of business, shall be classified as Trade Payable. Other payables as in this case cannot form part of Trade Payables, but would be classified as "Other Current/Non-Current Liabilities".(Refer Para 8.4.1 of GN).
Provisions (Long Term/Short Term)	
1.Valuation of Gratuity/Leave Encashment done by Actuary provided current and non-current portion for both, but Gratuity classified as Long Term Provision and Leave Encashment classified as Short Term Provision	If there is a classification provided by Actuary on the basis of retirement and attrition rate, then the current portion of both should be treated as Short Term Provision and non-current portion of both should be treated as Long Term Provision. (Refer Q.30 of FAQs).

Non-Compliance/Inadequate Disclosures	Technical Requirement as per Schedule III
2. Provision for Tax (net of advance tax) for the year disclosed as Long Term Provision.	Current Year's Provision for Tax should generally be classified as Short Term Provision as the same would be payable within 12 months from the Balance Sheet date. (Refer Q.31 of FAQs).
<u>Fixed Assets</u>	
1. A company having Tangible and Intangible assets did not categorize the same accordingly.	As per Para 6 I and J, there is a requirement to classify assets into Tangible and Intangible Assets. Further, as in Tangible Assets where the work in under progress is disclosed separately as Capital Work in Progress, for Intangible Assets also which are under development, there is a requirement to disclose separately as Intangible Assets under Development.

Non-Compliance/Inadequate Disclosures	**Technical Requirement as per Schedule III**
2. Advance given for Capital Asset where the work is under progress included in Capital Work in Progress.	Any advance for purchase/creation of fixed assets has to be classified as Long Term Loans and Advances. (Refer Para 6 L(i)(a) Capital Advances).
3. Assets identified as "Fixed Assets Held for Sale" were included in Fixed Assets Schedule.	Such assets should be classified as Current Assets, since the intent to sell such assets is established by the Company. (Refer Q.17 of FAQs).
4. Tangible Assets included owned assets as well as leased assets, however no such break up provided in the Tangible Assets schedule.	As per Para 6 I (ii) under classification of Tangible Assets into various categories, assets under lease have to be separately specified for each such category of asset.
Investments	
1. Investment in Associate and Joint Venture was not disclosed, though such disclosure made in Related Party Transactions.	There is a requirement as per Para 6 K(i) to separately categorize investments in subsidiaries, associates, joint ventures with extent of investment in such entities.

Non-Compliance/Inadequate Disclosures	Technical Requirement as per Schedule III
2. Total Long Term Investment was disclosed and Total Provision for all the Investments together was reflected.	As per AS-13, value of each Long Term Investment has to be carried at cost less Provision for other than temporary diminution in value thereof. However, aggregate amount of provision made in respect of all Non-Current Investment should also be disclosed separately as per the requirement of Schedule III Para 6K(iii). (Refer GN Para 8.7.2.3).

Non-Compliance/Inadequate Disclosures	Technical Requirement as per Schedule III
3. Investment in Partnership Firms included investment in LLPs.	LLP is a body corporate and not a partnership firm. Hence disclosures of investment in Partnership Firms would not include investment in LLPs. Such investments should be disclosed separately under "Other Investments". Other disclosures required for Partnership Firms also need not be made for LLPs.
Inventories	
1. Trading Stock of the Company into manufacturing and trading was included in Finished Goods Stock.	As per Para 6O(i)(d) there is a requirement to disclose separately Stock-in-Trade (in respect of goods acquired for trading).
2. Goods in Transit including towards Raw Materials, Stock-in-trade and Stores and Spares was disclosed together as such.	As per Para 6O(i)(ii) there is a requirement that Good-in-transit for each category of inventory should be disclosed under the relevant sub-head of inventories.

Non-Compliance/Inadequate Disclosures	**Technical Requirement as per Schedule III**
<u>Trade Receivables</u>	
1. Trade Receivables outstanding for more than six months were considered from the date of invoice.	As per Para 6P(i) Trade Receivables outstanding for a period exceeding six months is to be considered from the date they are due for payment.
2. Trade Receivables included receivables due from sale of Fixed Assets and Investments.	A Trade Receivable is only in respect of the amount due on account of goods sold or services rendered in the ordinary course of business. Amount due on account of other contractual obligations cannot form part of Trade Receivables but are to be classified as "Others" (Refer Para 8.7.4 of GN).

Non-Compliance/Inadequate Disclosures	Technical Requirement as per Schedule III
<u>Cash and Cash Equivalents</u>	
1. Fixed Deposits having maturity beyond 12 months disclosed under this head.	Fixed Deposits with more than 12 months maturity have to be disclosed as "Other Bank Balances" and the non-current portion of such deposits should be classified under the head "Other Non-Current Assets". (Refer Para 8.8.4 of GN).
2. Balance in Unpaid Dividend Account included in Balances with Banks while preparing Cash Flow Statement.	As per Para 6Q(ii) earmarked balances with banks like unpaid dividend shall be separately stated and this should not form part of the Cash Flow of the Company.
<u>Loans and Advances (Long Term/Short Term)</u>	
1. Provision for Bad and Doubtful Advances were disclosed combined for all types of Loans and Advances.	As per Para Para 6L(iii)(b) and 6R(iii) allowance for bad and doubtful loans and advances shall be disclosed under the relevant heads separately.

Non-Compliance/Inadequate Disclosures	Technical Requirement as per Schedule III
2. Loans and Advances to Related Parties was not disclosed.	As per Para 6L(i)(c) and 6R(i)(a) Loans and Advances to Related parties are to be disclosed separately with details thereof. The term "details" should be interpreted to understand the disclosure requirements as per AS-18 Related Party Disclosure.
3. Advance Tax (Net of Provision) disclosed as Current Asset.	As per Para 8.7.3 of GN and Q31 of FAQs, current year's advance tax (net of provision) as well as earlier year's advance tax shall generally be classified as non-current. However, advance tax against which refund orders have been passed will only be treated as current.

Non-Compliance/Inadequate Disclosures	Technical Requirement as per Schedule III
<u>Commitments</u>	
1. Company was having ongoing expansion; however there was no disclosure of Capital Commitments.	As per Para 8.8.7.4 of GN, future liability for capital expenditure in respect of which contract have been made should be disclosed. The Capital Commitments have to be disclosed net of advances, if any which would have been disclosed as Capital Advances.
<u>Revenue from Operations/Other Income</u>	
1. Company had revenue from sale of products as well as services which were disclosed combined.	As per Part II Para 2A, Revenue from Operations shall have break up of Sale of Products; Sale of Services and Other Operating Revenues.
2. Profit from Sale of Scrap arising from manufacturing operations was disclosed as Other Income.	Such income should be treated as Other Operating Revenue, since the same arises on account of the company's main operating activity. (Refer Para 9.1.8 of GN).

Non-Compliance/Inadequate Disclosures	**Technical Requirement as per Schedule III**
3. Profit on Sale of Fixed Assets and Net Foreign Exchange Gain was classified as Other Operating Revenue.	Sale of fixed assets is not an operating activity and hence profit from such sale should be classified as Other Income. Similarly, gain from Foreign Exchange, is purely earned on account of fluctuation in exchange rates and not on account of sale of products/services. Hence the same should be classified as Other Income. (Refer Para 9.1.8 and 9.1.9 of GN).
4. Details of Other Operating Revenue were not disclosed.	As per Para 2A there is a requirement to disclose separately.
<u>Expenses</u>	
1. Details of Raw Materials and Goods Traded by the Company were not disclosed under broad heads.	As per Para 5A (ii)(a) there is a requirement to disclose Raw Materials and Goods Purchased under the broad heads.

Non-Compliance/Inadequate Disclosures	**Technical Requirement as per Schedule III**
2. Expenses classification provided as per the functions carried out in the company.	The format laid down in Schedule III for presentation of items of income and expense indicates that the expenses should be aggregated based on their nature and hence functional classification of expenses is prohibited. (Refer Para 9 of GN).
3. Payment to Auditors was disclosed as a single line item.	As per Para 5A(j) there is a requirement to give break up of Payment to Auditors as (a) Auditor; (b) for taxation matters; (c) for company law matters; (d) for management services; (e) for other services and (f) for reimbursement of expenses.

Non-Compliance/Inadequate Disclosures	**Technical Requirement as per Schedule III**
<u>Notes to Financial Statements</u>	
1. MSMED disclosure was not made.	Disclosures as mandated by other acts or statutes will have to be made in the FS. This applies to other disclosure requirements as per MSMED Act, 2006, Clause 32 of Listing Agreement, etc. (Refer Para 6.8 and 6.9 of GN). **[Schedule III amended to include disclosures required under MSMED Act]**
2. Proposed dividend was disclosed in Notes and there was no provision made.	As per AS-4 there is a requirement to provide for the dividend for the period covered by the FS. Though Schedule III requires dividend to be disclosed by way of a note, the AS would override Schedule III requirements and hence provision is required. (Refer Para 8.8.7.7 of GN). **[newly notified AS-4 does not require provision]**
3. Expenditure in Foreign Currency disclosed on payment basis.	Such disclosure is required to be made on accrual basis since all the items in Statement of Profit and Loss are stated on accrual basis. (Refer Para 11.2.5 of GN).

Schedule II-Depreciation (Coverage)

- Key concepts (Depreciation, Useful life, Residual value, Componentisation etc.)
- Key differences between Schedule II and Schedule XIV
- Pronouncements / Guidance from ICAI

Key concepts

- **Depreciation** is the systematic allocation of the depreciable amount of an asset over its useful life.
- **The depreciable amount** of an asset is the cost of an asset or other amount substituted for cost, less its residual value.
- **Useful life** is the period over which an asset is expected to be available for use by an entity, or the number of production or similar units expected to be obtained from the asset by the entity.

Key concepts

- Depreciation begins when the asset is available for use, *i.e.*, when it is in the location and condition necessary for it to be capable of operating in the manner intended by management.

- Depreciation ceases when the asset is retired from active use and is held for disposal / the date that the asset is derecognised.

- Depreciation does not cease when the asset becomes idle unless the asset is fully depreciated.

Key concepts

- The depreciation method should reflect the pattern in which the future economic benefits of the asset are expected to be consumed by the enterprise.

- The depreciation method should be reviewed at least at each financial year-end.

- If there has been a significant change in the expected pattern of consumption of the future economic benefits embodied in the asset, the depreciation method should be changed to reflect the changed pattern. Such a change should be accounted for as a change in an accounting estimate in accordance with AS 5.

Key changes in Schedule II
(as compared to Schedule XIV)

- Schedule II prescribes **indicative** useful lives of various assets instead of Straight Line Method (SLM)/ Written Down Value (WDV) rates for calculating depreciation. Schedule XIV rates were minimum rates.

- Companies are allowed to follow different useful life/residual value if an appropriate justification is given which is supported by technical advice.

Key changes in Schedule II
(as compared to Schedule XIV)

- Useful lives of significant parts of an asset to be determined separately (componentisation).

- No separate rate for double/ triple shift; depreciation to be increased based on the double shift/triple shift use of the assets.

- No reference to depreciation on low value assets.

Pronouncements / Guidance from ICAI / MCA

- Guidance Note on Accounting for Depreciation in Companies in the context of Schedule II to the Companies Act, 2013 [(effective 1st April 2016)-early application encouraged].

- Application Guide on the provisions of Schedule II to the Companies Act, 2013.

- AS-6 –Depreciation Accounting (omitted by the Companies (Accounting Standards) Amendment Rules, 2016 w.e.f. 1/4/2016.

- AS-10 –Accounting for Fixed Assets [new AS-10 "Property, Plant and Equipment" substituted by the Companies (Accounting Standards) Amendment Rules, 2016 w.e.f. 1/4/2016].

Indicative rates
(neither minimum or maximum)

- The useful life of an asset shall not ordinarily be different from the useful life specified in Part C of Schedule II. Further, residual value of an asset shall not to be more than five percent of the original cost of the asset-

  Provided that where a company adopts a useful life different from what is specified in Part C or uses a residual value different from the limit specified above, the financial statements to disclose such difference and provide justification in this behalf duly supported by technical advice.

Residual value

- If lower than 5 % of the original cost- **no disclosure**
- If equal to 5 % of the original cost- **no disclosure**
- If higher than 5 % of the original cost- **disclosure required**

Arriving rates for SLM / WDV

- In case of straight line method (SLM) of depreciation, the asset will be depreciated equally over the new remaining useful life of the asset.

- In case of Written Down Value (WDV) method of depreciation, company will need to calculate a new rate for depreciation by using the following formula:

  R= {1 – (s/c)^1/n } x 100
  Where R = Rate of Depreciation (in %)
  n = Remaining useful life of the asset (in years)
  s = Scrap value at the end of useful life of the asset
  c= Cost of the asset/Written down value of the asset

Regulatory rates

Part B of Schedule II

- In case a Regulatory Authority prescribes useful life, rate of depreciation or residual value for any specific asset for accounting purposes, then company should use the same even though it is different from that as estimated by the management.

Intangible Assets

- Intangible assets other than those arising from toll-roads to be amortised in accordance with Accounting Standards (AS) 26, *Intangible Assets.*

- Intangible assets arising from toll-roads **may be** amortised based on **revenue-based methodology.**

- Thus option available to either follow or not to follow revenue based methodology.

Intangible Assets

Amortisation to be calculated as follows:

$$\text{Amortization Rate} = \frac{\text{Amortization Amount}}{\text{Cost of Intangible Assets}} \times 100$$

$$\text{Amortization Amount} = \text{Cost of Intangible Asset} \times \frac{\text{Actual Revenue for the year}}{\text{Projected Revenue from Intangible Asset (till the end of the concession period)}}$$

Illustration

Here we understand the concept with the help of an illustration on Toll Road.

Following are the assumptions to the Illustration :

Cost of Creation of Toll Road = Rs. 800 Crore

Total period of Agreement = 17 years

Time for creation of Toll Road = 2 years

Balance years for amortization

of Toll Road = 15 years

Total Revenue to be generated

Out of Toll Road = Rs. 1000 Crore

The year wise generation of revenue shall be as follows :

Year No.	Revenue (In Crores)
1	6
2	11
3	22
4	28
5	37
6	46
7	54
8	62
9	73
10	85
11	91
12	104
13	113
14	128
15	140
Total	**1000**

Year	Revenue (In Crores)	Computation	Charged to P & L	Amortization Rate	
1	6	6/1000*800	4.8	4.8/800*100	0.6 %
2	11	11/1000*800	8.8	8.8/800*100	1.1 %
3	22	22/1000*800	17.6	17.6/800*100	2.2 %
4	28	28/1000*800	22.4	22.4/800*100	2.8 %
5	37	37/1000*800	29.6	29.6/800*100	3.7 %
6	46	46/1000*800	36.8	36.8/800*100	4.6 %
7	54	54/1000*800	43.2	43.2/800*100	5.4 %
8	62	62/1000*800	49.6	49.6/800*100	6.2 %
9	73	73/1000*800	58.4	58.4/800*100	7.3 %
10	85	85/1000*800	68	68/800*100	8.5 %
11	91	91/1000*800	72.8	72.8/800*100	9.1 %
12	104	104/1000*800	83.2	83.2/800*100	10.4 %
13	113	113/1000*800	90.4	90.4/800*100	11.3 %
14	128	128/1000*800	102.4	102.4/800*100	12.8 %
15	140	140/1000*800	112	112/800*100	14 %
Total	**1000**		**800**		

Revaluation of Assets

- Paragraph 1 of Part A of Schedule II defines 'depreciable amount' as:

  "The depreciable amount of an asset is the cost of an asset or other amount substituted for cost, less its residual value."

- AS 6, also defines the term 'depreciable amount' in the same way.

Revaluation of Assets

- Therefore, Schedule II requires depreciation to be provided on historical cost or the amount substituted for the historical cost (i.e. revalued amount).

- With Schedule II becoming applicable, companies which hitherto followed the policy of recouping additional depreciation as a credit to the statement of profit and loss, will need to start recouping additional depreciation on account of revaluation as a credit to revenue reserves.

- Such change is treated as change in accounting policy under AS 5 requiring adequate disclosures.

Component approach

- As per note 4 of Schedule II -*"Useful life specified in Part C of the Schedule is for whole of the asset. Where cost of a part of the asset is significant to total cost of the asset and useful life of that part is different from the useful life of the remaining asset, useful life of that significant part shall be determined separately."*

- Two important factors-

  (a) cost of the part needs to be significant to the total cost of an asset

  (b) Useful life of the component to be different from the useful life of the remaining asset

Component approach

- The determination as to whether a part of an asset is significant requires a careful assessment of the facts and circumstances.

- As a part of the assessment, the company should:

  - determine the threshold value to determine which asset requires componentisation.
  - Threshold value in percentage of cost of component to the total cost of the asset
  - Proportion of useful life of that part as compared to the useful life of the asset
  - Potential impact on the total depreciation expenditure

Component approach

- Component approach already allowed under AS-10.
- Voluntary for financial year commencing on or after 1st April 2014
- Mandatory from financial years commencing from 1st April 2015

Illustration-Componentisation

Let us understand how Depreciation is to be calculated for components of an asset and difference in depreciation calculation between Companies Act, 1956 and 2013.

The following are the assumptions for calculating Depreciation of a Blast Furnace held by a Steel Company ABC Ltd. :

The company assumes the furnace to have a useful life of 30 years based on past experience.

Illustration-Componentisation

Components	Useful Life	Cost (Rs. in Crores)
Structure	30	75
Internal lining of refractory	5	20
Heating Components	7	14
Motors and other operating parts for controlling them	10	35
Total		**144**

Illustration-Componentisation
(Depreciation under Companies Act, 1956)

Component Accounting was not mandatory as per Companies Act, 1956.

Therefore, Depreciation of the furnace (SLM Basis)

= Rs. 144 Crores/30 years

= Rs. 4.8 Crore per annum

Here, the Replacement Cost of various components will be charged to the Statement of Profit and Loss, as and when incurred.

Illustration-Componentisation (Depreciation under Companies Act, 2013)

Furnace	Depreciable Amount (Rs. In Crores) (A)	Useful Life (B)	Depreciation Amount (Rs. In Crores) (A/B)
Structure	75	30	2.5
Internal lining of refractory	20	5	4
Heating Components	14	7	2
Motors and other operating parts for controlling them	35	10	3.5
Total			**12**

Illustration
(Depreciation under Companies Act, 2013)

- When at the end of respective useful lives, the components are replaced, the replacement cost should be capitalized because by that time, they are fully depreciated and the carrying value at the end of their respective useful lives is NIL.

Depreciation on low value items

- Schedule XIV allowed 100% depreciation on low value items (costing Rs. 5,000 or less).

- Schedule II does not prescribe any such requirement to provide depreciation at the rate of hundred per cent.

- Guidance note allows 100% depreciation on low value items based on materiality considerations.

Multiple shift depreciation

- The useful lives of assets working on shift basis have been specified in Schedule II, based on their single shift working.

- If an asset is used for any time during the year for double shift, the depreciation will increase by 50% for that period and in case of the triple shift the depreciation shall be calculated on the basis of 100% for that period.

- In contrast, Schedule XIV gave specific rates for double and triple shift.

Definition of the term “Shift”

- The term “Shift” is not defined in the Companies Act, 1956 as well as Companies Act, 2013. As per Section 2(r) of the Factories Act, 1948, the definition of the term “shift” is as follows:

“Where work of the same kind is carried out by two or more sets of workers working during different periods of the day, each of such sets is called ‘group’ or ‘relay’ and each of such period is called “Shift””.

ILLUSTRATION

Assumptions to the Illustration

Cost of Plant and Machinery = Rs. 30 Crore

Residual Value = Rs. 1.5 Crore

Depreciable Amount = Rs. 28.5 Crore

Useful Life as per Schedule II = 15 years

Normal Working Days = 300 Days

Working Days for Double Shift = 60 Days

Therefore, Depreciation amount as per SLM Basis

$$= \frac{\text{Rs. 30 Crore} - \text{Rs. 1.5 Crore}}{\text{15 years}}$$

= Rs. 1.9 Crore

= Depreciation for Single Shift Working

Now,

Depreciation amount for Double Shift Working

= [Rs. 1.9 Crore (i.e. for Single Shift Working) + 50% (Rs. 1.9 Crore X 60 Days /300 Days

= Rs. 0.19 Crore

Therefore, Total Depreciation to be charged to Plant and Machinery

= Rs. 1.9 Crore + Rs. 0.19 Crore

= Rs. 2.09 Crore

Continuous Process plant (CPP)

- CPP is a plant which is required and designed to operate 24 hours a day.

- Blast Furnace is required and designed to operate 24 hours a day. It may be shut down due to planned maintenance , lack of demand, etc. It would still be considered a Continuous Process Plant.

- CPP for which no special rates have been prescribed can be depreciated over a 25 year period. The period of 25 years was earlier stated as 8 years in Schedule II which was later rectified through a Notification.

Transitional provisions

As per note 7 to Schedule II-

From the date this Schedule comes into effect, the carrying amount of the asset as on that date-

(a) shall be depreciated over the remaining useful life of the asset as per this Schedule;

(b) after retaining the residual value, may be recognised in the opening balance of retained earnings where the remaining useful life of an asset is nil.

Illustration

Name of the Asset	Date put to use	Cost	Depreciation	WDV as on 31.03.2014	Salvage Value	No of years the asset is used	Balance Useful Life	Carrying amount adjusted Against Reserves	Depreciation for C. Y. on Residual Carrying amount
Plant & Machinery	01.04.1996	5,00,000	4,51,440	48,560	25,000	18	-	23,560	-
Plant & Machinery	01.04.2001	10,00,000	6,52,080	3,47,920	50,000	13	2	-	1,48,960
Furniture	01.04.2008	15,00,000	4,06,125	10,93,875	75,000	6	4	-	2,54,719
Computers	01.04.2011	10,00,000	4,61,985	5,38,015	50,000	3	-	4,88,015	-
Server	01.04.2011	10,00,000	4,61,985	5,38,015	50,000	3	3	-	1,62,672

Disclosure requirements

- Apart from the disclosures required under the accounting standards, Schedule II requires disclosure of:
  - Depreciation methods used;
  - Useful life and/or residual value, if they are different from those specified under that Schedule along with the fact that the said useful lives/residual values are supported by technical advice.

Thank You