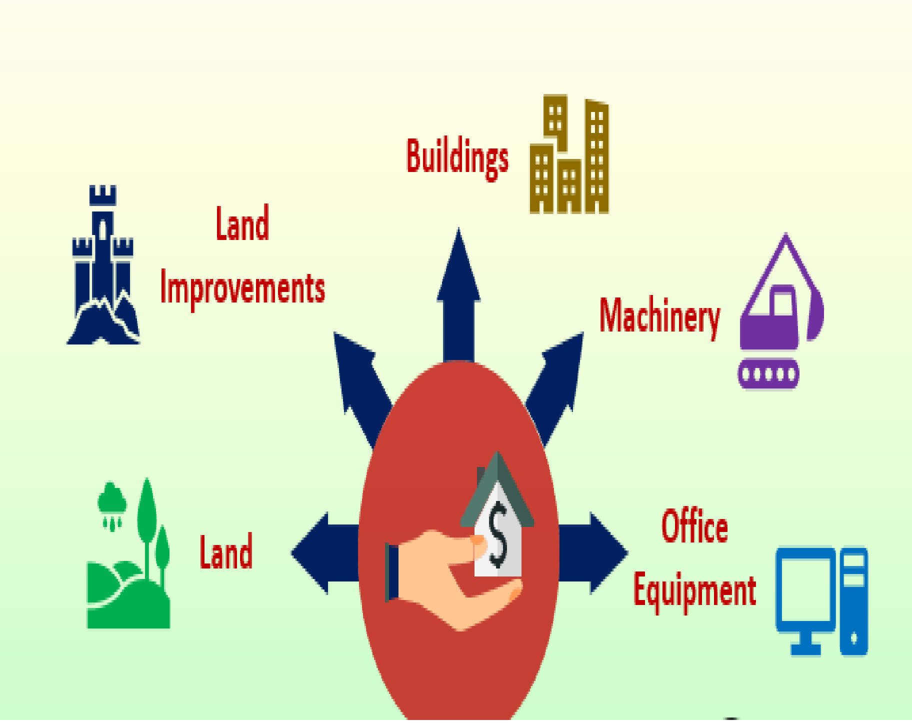
Property, Plant and Equipment (PPE)

And

Intangible Assets



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IND AS -16: Property Plant and Equipment

Definition

Property, Plant and Equipment ('PPE')

- Held for:
  - Use in production or supply of goods or services
  - Rental to others
  - Administrative purposes

- Expected to be used during more than one period.

Recognition Principle

PPE should be recognised if both of the following conditions are satisfied:

a) It is probable that future economic benefits will flow to entity and
b) Its cost can be reliably measured.

If any of the above conditions is not satisfied, PPE cannot be recorded.

Above recognition principle is to be applied on 'Initial' recognition of PPE and 'Subsequent' recognition.

Past expenditure which has been written off in P&L cannot be capitalised later.

Measurement

- Property, Plant Equipment is measured initially at cost.
- Elements of Cost: All costs involved in bringing the asset to the present location and condition necessary for it to be capable of operating in the manner intended by management.

Cost Elements

•Purchase Costs:

•Purchase Cost

•Import Duties/Non Refundable Taxes

•Deduct trade discounts/ rebates

Directly Attributable Costs:

-Cost of Employee benefits

-Cost of Site Preparation

-Initial delivery and handling costs

-Transport handling charges

-Installation and assembly costs

-Cost of testing

-Professional Fees

Other Costs:

-Initial estimates of Dismantling costs

-Initial estimates of site restoration costs

-Major inspection costs

-Cost of replacements

Measurement (Cont.)

- Initial operating losses charged to P&L
- Abnormal losses and profits in case of self constructed asset charged to P&L
- Incidental operations during construction period charged to P&L
- Payment is deferred beyond normal credit terms, the difference between the cash price equivalent and the total payment is recognized as Financing Cost

- Spare parts, stand-by equipment & Servicing Equipment:
  - These are recognized in accordance with this IND AS when they meet the definition of PPE
  - Otherwise such items are classified as Inventory

Cost Element - Exclusion

- Costs of Opening a new facility
- Costs of introducing a new product or service or conducting business in a new location;
- Administrative and other general overheads

Cost of PPE

- PPE can be
  - Purchase/ constructed or
  - Obtained through Exchange or
  - Through business combination

Ind AS 103 deals with PPE acquired through Business Combination.

Cost of PPE obtained through Exchange of Non Monetary Assets

Exchange has commercial substances, i.e. cash flow from asset will change due to exchange

Journal entry-
PPE(obtained) Dr @ Fair value of PPE obtained
Cash Dr/Cr
To PPE (old Asset) Book value
To P&L
(being PPE exchanged)

Exchange does not have commercial substances or fair value of asset obtained/ given cannot be reliably estimated, its cost is measured at the carrying amount of the asset given up.

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Subsequent Cost - Part Replacement

- Day to day servicing cost are charged to P&L
- Some items involve a series of linked parts which require regular replacement at different intervals and have different useful lives.
- Recognize the cost of replacing a part in the carrying amount, if recognition criteria are met.
- The carrying amount of replaced parts is derecognized.
- For Example, a furnace may require relining after a specified number of hours of use, or aircraft interiors such as seats and galleys may require replacement several times during the life of the airframe.
- Performing regular major inspections for faults, regardless of parts being replaced or not, may be a condition of continuing to operate an item of Property Plant and Equipment.
- Cost of each major inspection performed is recognized in carrying amount, as a replacement, if the recognition criteria are met.
- Any remaining carrying amount of the cost of the previous inspection is derecognized.

Subsequent Measurement

- Entity can follow Cost Model or Revaluation Model as its accounting policy.
- Entity should apply its model to class of PPE.
- Class means "similar assets, with similar use" i.e. whose nature and use are similar.
- All assets in a class should be either at cost model or revaluation model.
- Revaluation shall be done with sufficient regularity to ensure that there is no significant gap between FV and Carrying Value.
- Under revaluation model, carrying amount restated with reference to available observable market data.
- Under cost model, asset will be shown at-

  Cost- Accumulated Depreciation- Accumulated Impairment loss = Book Value.

Revaluation Model

Revaluation

Upward: Recognized directly in Other Comprehensive Income & accumulated under Equity in revaluation surplus

Downward: Debit revaluation Surplus to the extent recognized previously and balance, if any, Charge to Profit or Loss A/c.

- Additional depreciation will be written off against P&L Account. But entity have option to transfer additional depreciation amount from revaluation reserve to retained earnings in SOCE.
- Revaluation Reserve will be transferred to retained earnings upon sale of asset/ disposal/ fully written off.
- The revaluation surplus may be transferred to retained earnings when the assets is derecognized or as it is used by the entity (not through Profit & Loss)
- Ind AS-16 does not specify any frequency of revaluation. It can be
  - Annual (if fair value keep on changing) or
  - 3-5 years (if fair value remain stable)
- No fixed date has been given for revaluation. It can be any date of year.

Depreciation

- 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) & continues until the asset is derecognized or classifies as held for sale.
- Charging of depreciation is **MUST**, even if asset is not used
- Depreciation amount may be zero due to residual value being more than carrying amount.
- Depreciation is systematic allocation of depreciable value over useful life of asset.
  - Systematic allocation can be with SLM, WDV or any other method reflecting consumption of asset.
  - **Depreciable amount means** carrying amount less residual value.
  - Useful life is **management estimate**. It is part of economic life for which management expects usage of asset.
  - The **residual value & the useful life** of an asset shall be **reviewed at least at each financial year end**, and if expectations differs from previous estimates, the change shall be accounted for as a change in accounting estimates.

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Depreciation (Cont.)

- Depreciation should cease when
  - Asset is derecognized (sale/ written off)
  - Held for sale (Ind AS 105)
- Depreciation is not charged on land, unless it has limited life (Landfill has limited life, hence it will be depreciated).

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Disclosures

- Measurement basis for determining gross carrying value
- Depreciation methods used
- Useful lives or depreciation rates used
- Gross carrying amount and accumulated depreciation at the beginning and end of the period
- Reconciliation of the carrying amount at the beginning and end of the period (Addition, Deletion, Assets classified as held for sale, Business Combination, Revaluation, impairment, exchange difference & Other charges)
- Existence and amounts of restrictions on title to assets
- Property Plant and equipments pledged as security for liabilities
- Contractual commitments for acquisition of Property Plant and Equipment
- Amount of compensation from third parties for items of property plant and equipments (if not disclosed separately in P&L)

Disclosure for Revalued Assets

- Effective date of Revaluation
- Whether an independent valuer was involved.
- Methods and significant assumptions applied in estimating fair values.
- Extent to which fair value were determined based on observable prices or other valuation techniques.
- Carrying amount of each class of revalued Property Plant and Equipment if the cost model had been applied.
- Revaluation surplus, including movement and any restrictions on distribution of balance to shareholders.

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General Points (Transition Provisions)

- Net book value/ carrying amount after depreciation and rectification of any error should be considered as Deemed Cost.
- Such deemed cost cannot be adjusted for any other reason like capitalisation of borrowing costs.
- Earlier accumulated depreciation will be cancelled. Entity will start accumulating depreciation after application of Ind AS.
- Earlier impairment cannot be reversed after application of Ind AS.
- Earlier revaluation reserve will be transferred to retained earnings.

IND AS -38: Intangible Assets

Objectives:

- The objective of IND AS 38 is to prescribe the accounting treatment for intangible assets that are not dealt with specifically in another IND AS.
- The Standard requires an entity to recognize an intangible asset if, and only if, certain criteria are met.
- The Standard also specifies how to measure the carrying amount of intangible assets and requires certain disclosures regarding intangible assets.

Scope

IND AS 38 applies to all intangible assets other than:

- Financial assets.

- Exploration and evaluation assets (extractive industries).

- Expenditure on the development and extraction of minerals, oil, natural gas, and similar resources.

- Intangible assets arising from insurance contracts issued by insurance companies.

- Intangible assets covered by another IND AS, such as:
  - Intangibles held for sale
  - Deferred tax assets
  - Lease assets
  - Assets arising from employee benefits plan
  - Intangibles acquired under business combination.

Meaning of 'Intangible Assets'

Intangible assets are assets which

- arises from contractual or other legal rights
- are identifiable
- non monetary in nature
- without physical substance

Is Identifiable asset means separable asset?

- Not necessarily
- If separable, that means the asset is capable of being rented, sold or exchanged, independent of other assets. So identity is easily established.
- Even if not separable, a legal right to use makes it identifiable.

Recognition Principle

- IND AS 38 requires an entity to recognize an intangible asset, whether purchased or self-created (at cost) if, and only if:
    a. It is probable that the future economic benefits that are attributable to the asset will flow to the entity; and
    b. The cost of the asset can be measured reliably.

- An entity shall assess the probability of expected future economic benefits using reasonable and supportable assumptions that represent management's best estimate of the set of economic conditions that will exist over the useful life of the asset.

- If an intangible item does not meet both the definition of and the criteria for recognition as an intangible asset, IND AS 38 requires the expenditure on this item to be recognized as an expense when it is incurred.

Recognition

Separately Acquired	Acquisition in Business Combination	Internally generated Intangibles	Government Grants
↓	↓	↓	↓
Acquisition Cost	Cost equals to fair value (Ind AS 103)	Expenditure incurred in Development phase	Fair value or Nominal Value

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Recognition: Separately Purchased Intangible

- Separately Purchased Cost includes:
  - Purchase price
  - import duties
  - non-refundable purchase taxes
  - Less: trade discounts and rebates

- Directly attributable expenditure on preparing the asset for its intended use e.g., employee benefits, professional fees, function testing.

Exchange of Intangible Assets

Cost in case of Exchanged Intangible assets

Exchange has commercial substances

Journal entry-

Intangible Asset	Dr @ Fair value of Asset obtained	
Cash	Dr/Cr	
To Asset (old Asset)	Book value	
To P&L (Difference charged)		

(Being Intangible asset exchanged)

Exchange does not have commercial substances or fair value of asset obtained/ given cannot be reliably estimated, its cost is measured at the carrying amount of the asset given up.

Acquisition in Business Combination

- Goodwill is recognised on business combination (it is a difference between purchase consideration and identifiable net assets acquired). Calculation of goodwill is dealt by Ind AS 103.

- If any intangible assets is not appearing in books of vendor company, but it satisfies meaning of intangible assets, it should be recorded at fair value.

- In case of research which is acquired as part of business combination, it “should be” capitalised as part of intangible asset acquired.
  - Further research cannot be capitalised
  - Development cost can be capitalised.

Internally generated Intangible Assets

- Charge all Research cost to expense.
- Development costs are capitalised when entity able to demonstrate :
  - Technical feasibility.
  - Intention to complete the intangible asset and use or sell it.
  - Ability to use or sell the intangible asset.
  - How the intangible asset will generate probable future economic benefits.
  - Adequate technical, financial and other resources to complete the development.
  - Ability to measure the expenditure attributable to the intangible asset.
- If an entity cannot distinguish the research phase of an internal project to create an intangible asset from the development phase, the entity treats the expenditure for that project as if it were incurred in the research phase only.

Internally generated Intangible Assets (Cont.)

- Costs not to recognise
  - Selling, administrative and other general overhead expenditure unless it can be directly attributed to preparing the asset for use
  - Inefficiencies and initial operating losses
  - Expenditure on training staff to operate the asset
  - Internally generated brands, mastheads, publishing titles, customer list & items "similar in substance"
  - Research
  - Start-up costs (establishment, pre-opening and pre- operating costs)
  - Training
  - Advertising and promotional activities
  - Relocating and re- organising (restructuring)

- COST ALREADY EXPENSED ARE SUNK COST HENCE NEVER RECOGNISED

Intangibles obtained by way of Government Grants

In case of any intangible asset is obtained by way of grant then it should be recorded at Fair value with credit to Deferred Grant.

Alternatively, it can be recorded at Nominal Value.

Subsequent Recognition

Subsequent expenditure is capitalized when the item meets

- Definition of an intangible asset
- General recognition criteria for intangible assets

For example, A Ltd. incurred INR1,00,000 on improvement of its software, it will be capitalized if it meets the recognition principle, i.e.

(a) Future economic benefits from improvement will flow to entity and

(b) Cost can be reliably estimanted.

Measurement

- Intangible should be initially recognised at cost.
- Intangible assets can be subsequently measured using cost model (Cost-Amortisation- impairment loss) or fair value model (fair value- Amortisation-impairment loss).
- Cost model and fair value model of Ind AS 38 are same as Ind AS 16.
- Revaluation Increase in carrying amount Recognise to P&L (To the extent of previously recognised loss) Recognise to Other Comprehensive Income (Remaining increased value).
- Decrease in carrying amount Recognise to Other Comprehensive Income (To the extent of previously recognised Profit Recognise to P&L (Remaining decreased value).

Amortisation of intangible Asset

- Intangible assets have "Indefinite life", hence amortisation can be zero. Ind AS-36 says that if intangible asset has indefinite life, it should be tested each year for impairment loss.

- Intangible assets should be amortised each year in ratio of consumption. This ratio is estimate of management and should be reviewed each year.

- In case of amortisation, it should be on prospective basis. It is called as change in accounting estimate.

Disclosure Requirements

- For each class of intangible asset, disclose:
  - useful life or amortization rate.
  - Amortization method.
  - Gross carrying amount.
  - Accumulated amortisation and impairment losses.
  - Line items in the income statement in which amortisation is included.
  - Basis for determining that an intangible has an indefinite life.
  - Description and carrying amount of individually material intangible assets.
  - Certain special disclosures about intangible assets acquired by way of government grants.
  - Information about intangible assets whose title is restricted.
  - Contractual commitments to acquire intangible assets.

- Revaluation policy or cost model followed should be disclosed.

Disclosure Requirements (Cont.)

- Reconciliation of the carrying amount at the beginning and the end of the period showing:
  - Additions (business combinations separately)
  - Assets held for sale
  - Retirements and other disposals
  - Revaluations
  - Impairments
  - Reversals of impairments
  - Amortisation
  - Foreign exchange differences
  - Other changes

- Measurement policy of intangible asset.

- Frequency of revaluation should be disclosed.

Companies(Auditor's Report) Order 2020

(Reporting points on Property, Plant & Equipment And Intangible Assets)

Fixed Assets Para 3(i)(a)(A)

Whether the company is maintaining proper records showing full particulars, including quantitative details and situation of Property, Plant and Equipment.

Fixed Assets Para 3(i)(a)(A) (Explanations)

Whether the company is maintaining proper records In general, however, the records relating to property, plant and equipment (PPE) should contain, inter alia, the following details:

(i) sufficient description of the PPE to make identification possible;

(ii) classification, that is, the head under which it is shown in the accounts, e.g., plant and machinery, office equipment, etc;

(iii) situation;

(iv) quantity, i.e., number of units;

(v) original cost;

(vi) year of purchase and date of put to use;

(vii) useful life;

(viii) residual Value;

(ix) component-wise breakup; (Wherever applicable)

(x) adjustment for revaluation or for any increase or decrease in cost;

(xi) date of revaluation, if any;

(xii) rate(s)/basis of depreciation

(xiii) depreciation for the current year;

(xiv) accumulated depreciation;

(xv) particulars regarding impairment;

(xvi) particulars regarding sale, discarding, demolition, destruction, etc.

Fixed Assets Para 3(i)(a)(A) (Explanations)

- The records should contain the abovementioned particulars in respect of all items of PPE, self-financed or right to use assets (under Ind AS 116) acquired through finance lease.

- These records should also contain particulars in respect of those items of PPE that have been fully depreciated or have been retired from active use and held for disposal.

- The records should also contain necessary particulars in respect of items of PPE that have been fully impaired during the period covered by the audit report.

Fixed Assets Para 3(i)(a)(B)

Whether the company is maintaining proper records showing full particulars of intangible assets

Following are the types of illustrative intangible assets:

- Customer lists / customer loyalty;
- Trademark, formula;
- Music copyright / literary works/musical works;
- Air route authority / permit;
- Recipe, trade secrets, processes, designs;
- Internet domain names, distribution network;
- Royalty agreements, employment contracts;
- Operating rights/marketing rights/servicing rights;
- Website development.

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Fixed Assets Para 3(i)(a)(B) (Explanations)

In general, however, the records relating to intangible assets should contain, inter alia, the following details:

- Sufficient description of the intangible asset and controls around capitalization;
- Situation;
- Original cost;
- Year of purchase;
- Date of put to use;
- Useful life and residual value;
- Adjustment for revaluation or for any increase or decrease in cost;
- Date of revaluation, if any;
- Rate(s)/basis of amortization;
- Amortization for the current year;
- Accumulated amortization;
- Particulars regarding impairment;
- Particulars regarding sale, discard etc.

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Fixed assets Para 3(i)(b)

Whether these Property, Plant and Equipment have been physically verified by the management at reasonable intervals; whether any material discrepancies were noticed on such verification and if so, whether the same have been properly dealt with in the books of account

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Fixed assets Para 3(i)(b) (Explanations)

This clause requires the auditor to comment whether the property, plant and equipment (PPE) of the company have been physically verified by the management at reasonable intervals.

It may be noted that in case of right of use (ROU) assets covered under Ind AS 116, where the auditee, under a lease agreement, obtains the right to use an asset, the same should be considered for reporting under this clause. It may also be noted that investment property (as defined under Ind AS 40) and non-current assets held for sale (as defined under Ind AS 105) will be considered by the auditor for reporting under this clause.

Physical verification of the assets is the responsibility of the management and, therefore, has to be carried out by the management itself and not by the auditor.

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Fixed Assets Para 3(i)(c)

Whether the title deeds of immovable properties (other than properties where the company is the lessee and the lease agreements are duly executed in favour of the lessee) disclosed in the financial statements are held in the name of the company. If not, provide the details thereof:

- Description of property, including location, identification number from land records, municipal records, etc.;
- Gross carrying value as per balance sheet of the company;
- Name of the individual (s) who are holding the title of the immovable property;
- Whether promoter, director or their relative or employee;
- Period held – indicate range, where appropriate;
- Reason for not being held in name of company (*also indicate if in dispute);

Fixed Assets Para 3(i)(d)

Whether the company has revalued its Property, Plant and Equipment (including Right of Use assets) or intangible assets or both during the year and, if so,

Whether the revaluation is based on the valuation by a Registered Valuer;

Specify the amount of change, if change is 10% or more in the aggregate of the net carrying value of each class of Property, Plant and Equipment or intangible assets

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Fixed Assets Para 3(i)(d) (Explanations)

Reporting under this clause would be limited to revaluation model since under cost model revaluation is not permitted.

Further, reporting under this clause will cover both upward and downward revaluation under revaluation model.

It may be noted that for the purpose of reporting under this clause, revaluation shall not include:

- Fair valuation of PPE upon first time adoption of Ind AS.
- Remeasurements (i.e., changes in value due to interest or foreign exchange rates).
- Changes to ROU assets due to lease modification as per Ind AS 116.

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Thank You!!