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**Accounting for Fixed Assets for SMEs in India vs. IFRS for  
SMEs:  
A Comparative Study and the Challenges Ahead**

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**ABSTRACT:**

*India is moving towards converged IFRSs in a phased manner. SMEs play a very vital role in the economic development of any country. There are differences across the globe on financial reporting policies and practices of SMEs. To address the problem, in 2009 IASB issued 'IFRS for SMEs'. It is a simplified version of full IFRS aimed in response to the compelling need expressed by both developed and emerging economies for a simplified common set of accounting standards for smaller and medium-sized enterprises.*

*In this backdrop the aim of the paper is to assess the gap in accounting and reporting to be faced by the Indian SMEs if IFRS for SMEs is adopted in India. This paper attempts to study degree of comparability in financial reporting practices of IFRS for SMEs on Property, Plant and Equipment and AS 10 on Accounting for Fixed Assets. The paper is an exploratory research carried out without any formulation of hypothesis, and both qualitative and quantitative approaches are adopted in the study. The statistical tools were used in the study for measuring the degree of comparability between the IFRS for SMEs on PPE and AS 10 on Accounting for Fixed Assets. The result shows significant degree of dissimilarity between IFRS for SMEs on PPE and AS 10 on Fixed Assets.*

*The paper has been divided into ten sections, namely: 1. Introduction, 2. Definition of SME 3. Scope of the Study, 4. Objective of the Study, 5. Research Methodology, 6. AS 10 vs IFRS for SMEs in respect of Fixed Assets/PPE, 7. Statistical Analysis, 8. Challenges before SMEs, 9. Findings & Conclusion, and 10. Limitation of the Study.*

**Key Words :** *IFRS for SMEs, SMEs, AS 10, Property, Plant and Equipment, Fixed Assets*

**JEL Classification :** *M40, M41 and M48*

**1. INTRODUCTION:**

“There is an urgent need to converge the current Indian Accounting Standards with the International Financial Reporting Standards (IFRS). I propose for adoption of the new Indian Accounting Standards (Ind. AS) by the Indian companies from the financial year 2015-16 voluntarily and from the financial year 2016-17 on a mandatory basis. Based on the international consensus, the regulators will separately notify the date of implementation of Ind. AS for the Banks, Insurance companies etc. Standards for the computation of tax would be notified separately.”--Abstract from Speech of Arun Jaitley 10th July 2014.(GoI, 2014, Page- 24).

IASB recognizes that full IFRSs will be difficult to adopt by the (Small and Medium Enterprises) SMEs. Therefore, they have issued a separate IFRS for SMEs in 2009. India has a plan for the time being to converge (and not adopt) with IFRSs and for that purpose Ind- ASs have been drafted and notified. However, no corresponding Ind. AS has been drafted against IFRS for SMEs. It is most likely that it would be done sooner or later. The same view has been subscribed by the Institute of Chartered Accountants of India in the “Concept Paper on Convergence with IFRS in India” dated October 10, 2007. It says that “In respect of entities other than public interest entities (termed as ‘small and medium sized entities’ (SMEs)), a separate standard for SMEs may be formulated based on the IFRS for Small and Medium-sized Enterprises when finally issued by the IASB, after modifications, if necessary.....”. (ICAI, 2007, page-10)

## 2. DEFINITIONS OF SME/ SMC:

The term ‘SMEs’ has been defined by IASB as- (a) do not have **public accountability**, and (b) publish **general purpose financial statements** for external users. Examples of external users include owners who are not involved in managing the business, existing and potential creditors, and credit rating agencies (IASB, 2009, page-10).

## 3. SCOPE OF THE STUDY :

In the above background SMEs in India will face a great challenge in financial reporting when the said IFRS is implemented in India with or without modification. Therefore, an in depth study in this domain is urgently required. Our Study is limited to only Accounting for Property, Plant and Equipment (i.e. Section 17) in IFRS for SMEs and corresponding requirements in AS 10 Accounting for Fixed Assets. Section 16: Investment Property, and Section 18: Intangible Assets, are outside the scope of our Study. IFRS 5: Non-Current Assets Held for Sale and Discontinued Operation has not been considered in the IFRS for SMEs, reason for which is not known. (Gandhi, 2012, page-29)

In Section 17 of IFRS of SMEs in addition to PPE, it also deals with depreciation and impairment of assets but there are separate accounting standards in India for Depreciation Accounting (AS 6) and Impairment of Assets (AS 28). In our study we have concentrated only on provision relating to Fixed Assets and those relating to depreciation and impairment of assets have not been considered.

## 4. OBJECTIVE OF THE STUDY :

Based on the above discussion, the objects of the present study, for which we are motivated to undertake this research work, may be enumerated as follows:-

1. To study the existing reporting practices of SMEs in the arena of accounting for fixed assets in India.
2. To assess the similarities and the differences between IFRS for SMEs on PPE and AS 10.
3. To statically measure the degree of association between Accounting for PPE in IFRS for SMEs and corresponding existing Indian Accounting Standard.

4. To identify the area of challenges before the SMEs in India while adopting IFRS for SMEs in respect of PPE.

## **5. RESEARCH METHODOLOGY:**

The research encompassed both qualitative data analysis and empirical study. The paper is exploratory research carried out without any formulation of hypotheses. We began our research by first analysing requirement of IFRS for SMEs and existing Indian Accounting Standard for Accounting for Fixed Assets. An empirical analysis was also performed by testing the similarities and dissimilarities between standards, taken two at a time in order to draw a well-established conclusion regarding the comparability degree existent between them.

The data collection was done mainly from the secondary data sources such as official web site of accounting body of the country, IASB web site, news article, journal, papers and various other websites. The source of information for the empirical analysis was also the information gathered by closely analyzing the regulations mentioned above which were accordingly codified and assayed by using some statistical methods which are being discussed in detail in a subsequent section.

## **6. AS 10 VS. IFRS FOR SMES.IN RESPECT OF FIXED ASSETS / PPE:**

Fixed Assets are universally present in every enterprise. Proper and correct accounting of Fixed Assets is very important to show the correct financial position of any enterprise. It is valued by the financial institutions also at the time of giving financial assistance to any enterprise. Since rising of loan is crucial for a SME, proper accounting of Fixed Assets is very important.

Section 17 of the IFRS for SMEs deals with Property, Plant and Equipment where as in India Accounting Standard 10 deals with Accounting for Fixed Assets. AS 10 became mandatory with effect from 01-04-1993 and is applicable to all types of enterprises.

### **6.1 Difference in Definition:**

6.1.1 Definition of PPE- IFRS for SMEs defines PPE as tangible assets that are held by an entity: for use in the production or supply of goods or services; for rental to others; or for administrative purposes; and are expected to be used during more than one period(IASB, 2009, page-92).Indian GAAP does not use the term Property Plant and Equipment instead uses the term Fixed Assets. Fixed Assets are defined as assets held with the intention of being used for the purpose of producing or providing goods or services and not held for sale in the normal course of business(MCA 2006, AS 10).

**Analysis:** IFRS for SMEs definition and existing AS 10 definition have differences. The important difference is property given on rent is covered under the PPE in IFRS for SMEs but AS 10 is silent on accounting treatment of property given on Rent. Also as per IFRS for SMEs PPE are expected to be used for more than one period but in Indian Accounting Standard it is not so.

**6.1.2 Definition of Fair Value-** AS per IFRS for SMEs “Fair value” is the amount for which an asset could be exchanged, or a liability settled, between knowledgeable, willing parties in an arm’s length transaction (IASB, 2009, page-19). On the other hand AS 10 on Fixed Assets uses the word “Fair market value” in place of “Fair value”. It defines Fair market value as the price that would be agreed to in an open and unrestricted market between knowledgeable and willing parties dealing at arm’s length who are fully informed and are not under any compulsion to transact (MCA 2006, AS 10).

Property, plant and equipment whose fair value cannot be measured reliably without undue cost or effort are treated as PPE as per Section 17 of IFRS for SMEs. However if land or a building, or part of a building, or both whose fair value can be measured reliably without undue cost or effort on an ongoing basis (known as investment property) are accounted for in accordance with section 16 of IFRS for SMEs at fair value through profit or loss. It is treated as investment property and not PPE if it held by owner or by the lessee under a finance lease to earn rentals or for capital appreciation or both, rather than for: (a) use in the production or supply of goods or services or for administrative purposes, or (b) sale in the ordinary course of business (IASB, 2009, page-92).

**Analysis:** Although AS-10 uses the word “Fair Market Value” in place of “Fair Value” as used in IFRS for SMEs the definition under AS-10 is similar to definition of “Fair Value” in IFRS for SMEs. In AS-10 and IFRS for SMEs fair value/fair market value is price between knowledgeable willing parties in an arm’s length transaction. However one important distinction between IFRS for SMEs and AS-10 definition of fair value is that in IFRS for SMEs it is the price for which an asset could be exchanged or liability settled but in AS 10 it price that would be agreed to in an open and unrestricted market. In IFRS for SMEs land or a building, or part of a building, or both can be treated under Investment property or PPE depends upon reliability of measuring fair value without undue cost or effort. If fair value of land or a building, or part of a building, or both can be measured reliably without undue cost or effort on an ongoing it will be treated as Investment property and Section 16 of the IFRS for SMEs will be applicable if it is not use in the production or supply of goods or services or for administrative purposes, or not held for sale in the ordinary course of business. In AS-10 there is no such distinction in accounting treatment of land or building or both. There is no concept of investment property in Indian GAAP.

**6.2 Difference in Recognition:** In IFRS for SMEs general asset recognition criteria apply. PPE is recognised if future economic benefits attributable to the asset are probable and the cost of the asset can be measured reliably. Spare parts and servicing equipment are usually carried as inventory and recognised in profit or loss as consumed. However, major spare parts and stand-by equipment are PPE when an entity expects to use them during more than one period. Similarly, if the spare parts and servicing equipment can be used only in connection with an item of property, plant and equipment, they are considered property, plant and equipment. There are some items of property, plant and equipment may require replacement at regular intervals (e.g the roof of a building). An entity shall add to the carrying amount of an item of property, plant and equipment the cost of replacing part of such an item when that cost is incurred if the replacement part is expected to provide incremental future benefits to the entity.

In AS 10, recognition criteria have been dealt under the head Identification of Fixed Assets. It has not dealt specially with recognition criteria. Spare parts and service parts stand-by equipment and servicing equipment are normally capitalised. Machinery spares are usually charged to the profit and loss statement as and when consumed.

**Analysis:** AS10 does not specially deal with recognition criteria but it provide guidance on recognition of spare parts, service parts, stand-by equipment and service equipment which are normally capitalised and similar to guidance given in IFRS for SMEs. Also AS10 does not deals with major inspection for faults regardless of whether parts of items are replaced or not. IFRS for SMEs provides for capitalisation of expenses for major inspections.

**6.3 Difference in Initial Measurement:** As per IFRS for SMEs, costs directly attributable to acquiring the asset and the costs necessary to bring such an asset to working condition for its intended use are to be recognised. Start-up and pre-production costs must not be capitalised unless they are necessary part of bringing the asset to its working condition. The following costs are also included in the initial measurement of the asset:

- Its purchase price, including legal and brokerage fees, import duties and non-refundable purchase taxes, after deducting trade discounts and rebates.
- Any costs directly attributable to bringing the asset to the location and condition necessary for it to be capable of operating in the manner intended by management. These can include the costs of site preparation,
- Initial delivery and handling, installation and assembly, and testing of functionality. the initial estimate of the costs of dismantling and removing the item and restoring the site on which it is located, the obligation for which an entity incurs either when the item is acquired or as a consequence of having used the item during a particular period for purposes other than to produce inventories during that period (IASB, 2009, page-93).

In AS 10 the cost of an item of fixed asset comprises its purchase price, including import duties and other non-refundable taxes or levies and any directly attributable cost of bringing the asset to its working condition for its intended use; any trade discounts and rebates are deducted in arriving at the purchase price (MCA 2006, AS 10).

**Analysis:** Indian AS 10 is Similar to IFRS for SMEs except that IFRS for SMEs exclude some type of cost from cost like costs of opening a new facility, costs of introducing a new product or service, costs of conducting business in a new location or with a new class of customer etc but AS 10 does not give guidance on the same. As per IFRS for SMEs borrowing cost are not part of fixed assets but as per AS-16 on Borrowing cost relating to an assets that necessarily takes a substantial period of time to get ready for its intended use or sale (known as qualifying assets) and directly attributable to the acquisition, construction or production of a qualifying assets should be capitalised. Section 25 of IFRS for SMEs dealt separately with borrowing cost and it should be treated as expenses in profit and loss account in the period in which they have incurred.

**6.4 Difference in Accounting for Exchange of Assets :** As per IFRS for SMEs an item of property, plant or equipment may be acquired in exchange for a non-monetary asset or assets, or a combination of monetary and non-monetary assets. An entity shall measure the cost of the acquired asset at fair value unless (a) the exchange transaction lacks commercial

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substance or (b) the fair value of neither the asset received nor the asset given up is reliably measurable (IASB, 2009, page-94).

In AS 10 exchange of Assets for another assets is dealt under the head non-monetary consideration. As per AS 10 when a fixed asset is acquired in exchange for another asset, its cost is usually determined with reference to the fair market value of the consideration given. It may be appropriate to consider also the fair market value of the asset acquired if this is more clearly evident (MCA 2006, AS 10).

**Analysis:** Both IFRS for SMEs and AS 10 give weightage to fair value of the assets for the purpose of measuring the cost of assets acquired in exchange of another assets. As per AS 10 when a fixed asset is acquired in exchange for shares or other securities in the enterprise, it is usually recorded at its fair market value, or the fair market value of the securities issued, whichever is more clearly evident. IFRS for SMEs deals with not only one asset purchase against other assets, but even an item of PPE may be acquired in exchange for non-monetary assets or assets or combination of both. AS 10 provide guidance for fixed assets acquired for another assets and does not specially mentioned monetary and non-monetary assets.

**6.5 Difference in Measurement at Initial Recognition :** As per IFRS for SMEs the cost of an item of property, plant and equipment is the cash price equivalent at the recognition date. If payment is deferred beyond normal credit terms, the cost is the present value of all future payments.

As per AS 10 the gross book value of a fixed asset should be either historical cost or a revaluation computed in accordance with this Standard (MCA 2006, AS 10).

**Analysis:** IFRS for SMEs provide guidance that in case assets is acquired lower than purchase price than also cash price equivalent is considered as cost of the project. However AS 10 deals with only historical or revaluation cost of the Assets. Hence in IFRS for SMEs PPE reflects more correct price than Indian AS 10.

**6.6 Difference in Measurement after Initial Recognition :** As per IFRS for SMEs an entity shall measure all items of PPE after initial recognition at cost less any accumulated depreciation and less any accumulated impairment losses. An entity shall recognise the costs of day-to-day servicing of an item of property, plant and equipment in profit or loss in the period in which the costs are incurred (IASB, 2009, page-94).

Although it is not specially mentioned in AS 10 regarding measurement after initial recognition at cost less any accumulated depreciation and any accumulated impairment losses, but it is current practise of SMEs in India. Also in AS 10 provides for guidance on “Improvement and Repairs” only. Subsequent expenditure related to fixed asset that represents improvements are capitalised; and expenses relating to repairs ought to be charged to the profit and loss statement.

**Analysis:** It is similar to IFRS for SMEs which provides for the costs of day-to-day servicing of an item of PPE to be charged in profit or loss account. As per AS10 the cost of an addition or extension to an existing asset which is of a capital nature and which becomes an integral part of the existing asset is usually added to its gross book value. Any addition or extension, which has a separate identity and is capable of being used after the existing asset is disposed

of, is accounted for separately. Only expenditure that increases the future benefits from the existing asset beyond its previously assessed standard of performance is included in the gross book value, e.g., an increase in capacity. IFRS for SMEs is silent on the issue.

**6.7 Difference in Disclosure Requirements :**As per IFRS for SMEs, an entity shall disclose the following for each class of Property, Plant and Equipment- the measurement bases used for determining the gross carrying amount, the depreciation methods used, the useful lives or the depreciation rates used, the gross carrying amount and the accumulated depreciation (aggregated with accumulated impairment losses) at the beginning and end of the reporting period, a reconciliation of the carrying amount at the beginning and end of the reporting period showing separately:(i) additions (ii) disposals

(iii) acquisitions through business combinations (iv) transfers to investment property if a reliable measure of fair value becomes available (v) impairment losses recognised or reversed in profit or loss in accordance with Section 27 of IFRS for SMEs, depreciation and other changes. The entity shall also disclose the following:

- (a) the existence and carrying amounts of property, plant and equipment to which the entity has restricted title or that is pledged as security for liabilities.
- (b) the amount of contractual commitments for the acquisition of property, plant and equipment(IASB, 2009, page-97).

**Analysis:** AS10 is similar to IFRS for SMEs but it does not provide guidance on disclosure regarding restricted title or pledged as security for liability. Also AS 10 is silent on disclosure of contractual commitments for the acquisition of Fixed Assets.

**7. STATISTICAL ANALYSIS :**

With the aim of identifying the gap to be faced by Indian SMEs if IFRS for SMEs is adopted in India, an analysis with character of comparison between IFRS for SMEs on PPE and AS 10 on Accounting for fixed Assets was carried out. We have coded every items of PPE of IFRS for SMEs. If the same item is present in AS 10 we have assigned value 1, and if it is not present we have assigned value 0 in AS 10. IFRS for SMEs has been taken as yardstick for this comparison and most of the countries have already adopted this and in our objective we have attempted to study the gap to be faced by Indian SMEs if IFRS for SMEs is implemented in India.

In order to achieve the proposed comparison, we considered that the best analysis, in the case of this type of approach, is represented by the non-parametric correlation and the degree of association between two or more than two considered variables. The most frequently used method in Accounting Standard literature, when an analysis at the level of national accounting regulations is aimed is Jaccards' association coefficients. The Jaccard coefficient is defined as the size of the intersection divided by the size of the union of the sample sets:

$$J(A,B)= \frac{|A \cap B|}{|A \cup B|} \dots\dots\dots(1)$$

The Jaccard distance is complementary to the Jaccard coefficient and measures the dissimilarities. It is obtained by dividing the difference of the sizes of the union and the intersection of two sets by the size of the union:

$$J_g(A,B) = 1 - J(A,B) = \frac{|A \cup B| - |A \cap B|}{|A \cup B|} \dots \dots \dots (2)$$

In order to achieve a quantification of the degree of similarity between the IFRS for SMEs on PPE and AS 10 on Fixed Assets, there was developed an empirical analysis with character of comparison. Based on the methodology of previous studies dealing with formal harmonization, there was identified a series of elements regarding financial reporting. The two considered coefficients offer the possibility of quantifying both the degree of association and the degree of dissimilarity between different sets of accounting standards taken into consideration for analysis. So as to dimension the association or compatibility level between two or more accounting systems, the formula for the Jaccards' coefficients is as follows:

$$S_{ij} = \frac{a}{a+b+c} \dots \dots \dots (3)$$

or

$$D_c = \frac{b+c}{a+b+c} \dots \dots \dots = 1 - S_{ij} \dots \dots \dots (4)$$

where,

$S_{ij}$  represents the degree of similarity between the two sets of analyzed accounting regulations;

$D_{ij}$  represents the degree of dissimilitude or diversity between the two sets of analyzed accounting regulations;

a – the number of elements which take the 1 value for both sets of regulations;

b – the number of elements which take the 1 value within the j-set of regulations and the 0 value for the i-set of regulations;

c – the number of elements which take the 1 value within the i-set of regulations and the 0 value for the j-set of regulations (Strouahlet al (2009), page-623).

The final result of degree of comparability of IFRS for SMEs on PPE and AS 10 Accounting for Fixed Assets are given in Table-1 below:-

**Table-1: Empirical Results of Degree of Comparability between IFRS for SMEs on PPE and AS 10 on Accounting for Fixed Assets.**

Particulars	$S_{ij}$ = DEGREE OF SIMILARITY between IFRS for SMEs and AS 10	$D_{ij}$ = DEGREE OF DISSIMILARITY between IFRS for SMEs and AS 10
Requirements as per IFRS for SMEs and AS 10	51.52%	48.48%

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The above result shows that provisions in AS 10 are 51.52% similar to IFRS for SMEs and there is difference of 48.48% between those two pronouncements.

### **8. CHALLENGES BEFORE SMEs:**

The major challenges before the SMEs in India will be to overcome the 48.48% differences with IFRS for SMEs if they have to adopt the international standard. Also there are some items on which provision/guidance are available on AS-10 but IFRS for SMEs is silent on the same. If we have to make the AS-10 similar to IFRS for SMEs, these provisions need to be modified. This will be one of the major challenges before the regulator.

Fair value measurement is another area where SMEs will face the challenge. Although fair market value is defined in AS-10 but it is not used for initial recognition and mainly used in case of non-monetary consideration i.e. Assets exchanged for another Assets. In IFRS for SMEs if land or a building, or part of a building, or both whose fair value can be measured reliably without undue cost or effort on an ongoing basis (known as investment property ) will be accounted for in accordance with section 17 of IFRS for SMEs at fair value through profit or loss. SMEs in India will face challenges in following the concept of fair value of the assets as it is still not well developed practice in India. There will be cost of implementing/following the fair value measurement and most of the SMEs with limited resources will find it very challenging.

The very basic purpose of Financial Statements of SMEs is different from public limited companies, as owner himself is involved in day to day administration of the enterprise and main user of the SMEs financial statements are Income tax authority, Financial Institutions, Banks etc. The SMEs owner may not be interested to change the existing financial reporting practise to international standard as it will lead to more and transparent disclosure of many information, which are not disclosed at present. This will be another reason that Indian SMEs may not be ready to move to IFRS for SMEs.

### **9. FINDINGS & CONCLUSION:**

We can conclude that there are substantial differences between IFRS for SMEs on PPE and AS 10:Accounting for Fixed Assets, particularly in the area of fair value measurement, borrowing cost capitalisation, treatment of inspection cost, measurement at cost, disclosure practise etc. IFRS for SMEs requirements are 51.52% similar to AS 10 and there is difference of 48.48% between IFRS for SMEs and AS-10. However, it may be expected that the challenges posed by the IFRS for SMEs can be coped up by the SMEs in India in course of time. Adoption of the IFRS for SMEs in India is essential to empower our SMEs to face the competition in the world so far as global accounting and reporting practices are concerned.

### **10. LIMITATION OF THE STUDY:**

The study is based on data collection done mainly from the secondary data sources such as official website of accounting body of the country, IASB web site, news articles, journals, papers and various other websites. The source of information for the empirical analysis was also the information gathered by closely analyzing the regulations mentioned above which were accordingly codified and assayed by using some statistical methods. The primary

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sources were not used in the study and result may be different if so used. There is a scope for further study in the subject by doing research using primary data. Moreover AS 10 is meant for both SMEs and Non-SMEs, whereas the IFRS under our study is meant for SMEs only. So comparison may not have level playing field. But the purpose of our study was to assess from where the SMEs in India will have start when the IFRS for SMEs is adopted in India.

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