B.Com Honours

Semester II

Calicut University

Accounting Standards for Financial Reporting

Course Code: COM2MN103 • Module 4 Notes

1. Accounting Standards for Revenue and Depreciation

How a company reports revenue and accounts for the wear-and-tear of its physical assets determines its net profitability. This final module covers the revenue recognition standard (Ind AS 115 / IFRS 15), including its 5-step model, and details depreciation accounting (AS 6) and calculation methods.

Revenue from Contracts with Customers (Ind AS 115 / IFRS 15)

Ind AS 115 replaces old cash/accrual revenue recognition models with a unified **Five-Step Model**:

1. **Identify the Contract:** Establishing that an agreement exists between the business and the customer, specifying rights and payment terms.
2. **Identify Performance Obligations (PO):** Detailing the specific promises in the contract (e.g., delivering a laptop and providing 1 year of free IT support represent two separate POs).
3. **Determine the Transaction Price:** Figuring out the total cash expected from the customer, adjusting for discounts, rebates, or performance bonuses.
4. **Allocate Transaction Price:** Spreading the total price across the identified POs based on their individual standalone selling prices.
5. **Recognize Revenue:** Recognizing revenue only when (or as) the entity satisfies a performance obligation by transferring control of the goods or services.

Depreciation Accounting (AS 6 / Ind AS 16)

Depreciation is the systematic allocation of the depreciable amount of a physical asset over its useful life. It represents the wear-and-tear, obsolescence, and usage of Property, Plant, and Equipment (PPE).

- **Depreciable Asset:** An asset that has a limited useful life, is held by an enterprise for production or service, and is not held for resale. (Land is not a depreciable asset because it has an unlimited useful life).
- **Objectives:** Calculating true profit (depreciation is an operating cost), representing the true value of assets on the Balance Sheet, and retaining funds to replace the asset at the end of its

useful life.

Methods of Depreciation: SLM vs. WDV

Firms calculate depreciation using two main mathematical approaches:

1. Straight Line Method (SLM)

Depreciation is calculated as a fixed percentage of the original cost of the asset. The depreciation amount remains constant every year:

$$\text{Annual Depreciation} = \frac{\text{Original Asset Cost} - \text{Estimated Scrap Value}}{\text{Estimated Useful Life (Years)}}$$

2. Written Down Value Method (WDV)

Depreciation is calculated as a fixed percentage of the book value (written down value) of the asset at the start of each year. The depreciation amount declines every year:

$$\text{Depreciation for Year } n = \text{Book Value at start of Year } n \times \text{Depreciation Rate}$$

Key Difference: WDV is preferred by tax authorities (Income Tax Act, India) and is suitable for assets that lose value quickly or require high maintenance as they age (e.g., machinery, vehicles). SLM is suitable for simple, long-term assets (e.g., office furniture, patents).