Guidelines on Compliance with Accounting Standards (AS) by Banks

DBOD.No.BP. BC. 89 /21.04.018/2002-03
March 29, 2003

All Scheduled Commercial Banks
(excluding RRBs and LABs)

Dear Sir,

Guidelines on Compliance with Accounting Standards (AS) by Banks

The Reserve Bank of India has been continuously making efforts to ensure convergence of its supervisory norms and practices with the international best practices with a view to aligning standards adopted by the Indian banking system with global standards. In this direction, the Governor had announced in the Mid-Term Review of Monetary and Credit Policy for the year 2001-02, that it was necessary to put in place appropriate arrangements to identify compliance by banks, as also gaps in compliance, with the Accounting Standards (AS) issued by the Institute of Chartered Accountants of India (ICAI) and recommend steps to eliminate / reduce gaps. Accordingly, a Working Group was constituted under the Chairmanship of Shri N.D. Gupta, Former President of ICAI to recommend steps to eliminate / reduce gaps in compliance by banks with the Accounting Standards issued by ICAI. The Working Group had examined compliance by banks with the Accounting Standards 1 to 22 which were already in force for the accounting period commencing from April 1, 2001, as also Accounting Standards 23 to 28 which were to come into force for subsequent periods.

2. The Working Group has, in its report, observed that out of Accounting Standards which are already in force, viz. Accounting Standards 1 to 22, banks in India are generally complying with most of the Accounting Standards except for the following eight, leading to qualification in the financial statements.

Accounting Standard	Pertaining to
5	Net Profit or Loss for the period, prior period items and changes in accounting policies
9	Revenue Recognition
11	Accounting for the Effects of Changes in Foreign Exchange Rates
15	Accounting for Retirement Benefits in the Financial Statements of Employers
17	Segment Reporting
18	Related Party Disclosures
21	Consolidated Financial Statements
22	Accounting for Taxes on Income

The Statutory Central Auditors report on banks' non-compliance with some of the Accounting Standards in the Auditors' Reports attached to the balance sheets and the qualifications could affect the confidence of the users of the financial statements, viz., counter party banks, host country regulators of foreign branches of Indian banks, national and international rating agencies etc., in the integrity of the published results.

3. With a view to eliminating gaps in compliance with the Accounting Standards, the Working Group has made recommendations on the concerned Accounting Standards and detailed guidelines based thereon are furnished for the guidance of banks in the Annexure. The Working Group has not made recommendation on Accounting Standard 11 (Accounting for effects of changes in foreign exchange rates) since ICAI is in the process of revising Accounting Standard 11. Guidelines on Accounting Standard 21 (Consolidated financial

statements) have been issued separately vide our circular DBOD.No.BP.BC.72/21.04.018/2002-03 dated February 25, 2003.

4. ICAI which was represented on the Working Group has also agreed to furnish appropriate clarification on the Accounting Standards in question on the lines of the recommendations of the Group for the guidance of its members. RBI considers that with the issue of the guidelines as above and adoption of the prescribed procedures, there should normally be no need for any Statutory Auditor for qualifying balance sheet of the bank being audited for non-compliance with Accounting Standards. Hence, it is essential that both banks and the Statutory Central Auditors adopt the guidelines and procedures prescribed. Whenever specific difference in opinion arises among the auditors, the Statutory Central Auditors would take a final view. Persisting difference, if any, could be sorted out in prior consultation with RBI, if necessary.

5. Banks are advised to place these guidelines before the Board of Directors. Banks are further advised to ensure strict compliance with the standards with effect from the accounting year ending March 31, 2003.

6. Please acknowledge receipt.

Yours faithfully,
Sd/-
(C.R. Muralidharan)
Chief General Manager
Encls : as above

Annexure

Guidelines on Compliance with Accounting Standards by banks

On the basis of the recommendations of the Working Group on Compliance with Accounting Standards by banks, which was constituted by the Reserve Bank of India with Shri N. D. Gupta, the then President of the Institute of Chartered Accountants of India, as Chairman, the following guidelines are issued to banks by RBI with a view to eliminating the gaps in compliance by banks with the Accounting Standard issued by ICAI.

2. These guidelines pertains to the following Accounting Standards (AS) which are already operational:

AS 5, AS 9, AS 15, AS 17, AS 18, AS 22, AS 23, AS 25, and AS 27.

3. Banks should place these guidelines before the Board of Directors and ensure strict compliance with effect from the accounting year ending March 31, 2003.

4. Accounting Standard 5 - Net Profit or Loss for the period, prior period items and changes in Accounting policies.

4.1 Gist of the Accounting Standard

The objective of this Standard is to prescribe the classification and disclosure of certain items in the statement of profit and loss so that all enterprises prepare and present such a statement on a uniform basis. Accordingly, this Standard requires the classification and disclosure of extraordinary and prior period items, and the disclosure of certain items within profit or loss from ordinary activities. It also specifies the accounting treatment for changes in accounting estimates and the disclosures to be made in the financial statements regarding changes in accounting policies. This Standard deals with, among other matters, the disclosure of certain items of net profit or loss for the period. These disclosures are made in addition to any other disclosures required by other Accounting Standards.

4.2 Reasons for qualification

4.2.1 Qualification in respect of Accounting Standard 5 should normally arise due to error or omission on the part of banks in accounting for income/ expenditure in the previous years, which are rectified during the current year and due to non-disclosure of such prior period items separately in the P& L account for the current year.

4.2.2 Qualifications arise mainly due to change in accounting estimates and not due to error or omission by the banks. The banks do not disclose the details of such items separately in the relevant year's profit & loss account since the format of the profit & loss account for banks is prescribed under Form B of the Third Schedule to the Banking Regulation Act, 1949, which does not provide any matching head of item for making such disclosures.

4.3 Action to be taken by banks / Auditors.

4.3.1 Paragraph 4.3 of Preface to the Statements on Accounting Standards states that Accounting Standards are intended to apply only to items which are material. Since materiality is not objectively defined, it has been decided that all banks should ensure compliance with the provisions of the Accounting Standard in respect of any item of prior period income or prior period expenditure which exceeds one percent of the total income/ total expenditure of the bank if the income/ expenditure is reckoned on a gross basis or one percent of the net profit before taxes or net losses as the case may be if the income is reckoned net of costs.

4.3.2 Since the format of the profit and loss accounts of banks prescribed in Form B under Third Schedule to the Banking Regulation Act 1949 does not specifically provide for disclosure of the impact of prior period items on the current year's profit and loss, such disclosures, wherever warranted, may be made in the Notes on Accounts to the balance sheet of banks.

5. Accounting Standard 9 - Revenue Recognition

5.1 Gist of the Accounting Standard

This Standard deals with the bases for recognition of revenue in the statement of profit and loss of an enterprise. The Standard is concerned with the recognition of revenue arising in the course of the ordinary activities of the enterprise from the sale of goods, the rendering of services, and the use by others of enterprise resources yielding interest, royalties and dividends. This Standard requires that revenue from sales or service transactions should be recognised when the requirements as to performance set out in paragraphs 11 and 12 of the Standard are satisfied, provided that at the time of performance it is not unreasonable to expect ultimate collection. If at the time of raising of any claim it is unreasonable to expect ultimate collection, revenue recognition should be postponed. This Standard requires that revenue arising from the use by others of enterprise resources yielding interest, royalties and dividends should only be recognised when no significant uncertainty as to measurability or collec-

tability exists. The Standard also prescribes the bases for recognition of these revenues. This Standard requires that in addition to the disclosures required by Accounting Standard 1 on 'Disclosure of Accounting Policies' (AS 1), an enterprise should also disclose the circumstances in which revenue recognition has been postponed pending the resolution of significant uncertainties.

5.2. Reasons for qualification

Auditors of a few banks had qualified the accounts for non-compliance with this Accounting Standard because the banks had not followed the accrual basis of recognising income in respect of certain items of income which, wherever necessary, are required to be split over two or more accounting periods due to the nature of the transaction.

5.3. Action to be taken by banks / Auditors

5.3.1 Paragraph 4.3 of Preface to the Statements on Accounting Standards states that Accounting Standards are intended to apply only to items which are material. Since materiality is not objectively defined, it has been decided that an item of income may not be considered to be material if it does not exceed one percent of the total income of the bank if the income is reckoned on a gross basis or one percent of the net profit (before taxes) if the income is reckoned net of costs. If any item of income is not considered to be material as per the above norms, it may be recognised when received.

5.3.2 Non-recognition of income by the banks in case of non-performing advances and non-performing investments, in compliance with the regulatory prescriptions of the RBI, should not attract a qualification by the statutory auditors as this would be in conformity with provisions of the standard, since it recognises postponement of recognition of revenue where collectibility of the revenue is significantly uncertain.

6. Accounting Standard 15 - Accounting for Retirement Benefits in the Financial Statements of Employers.

6.1 Gist of the Accounting Standard

This Standard deals with accounting for retirement benefits in the financial statements of employers. This Standard applies to retirement benefits in the form of provident fund, superannuation/pension and gratuity provided by an employer to employees, whether in pursuance of requirements of any law or otherwise. It also applies to retirement benefits in the form of leave encashment benefit, health and welfare schemes and other retirement benefits, if the predominant characteristics of these benefits are the same as those of provident fund, superannuation/pension or gratuity benefit, i.e. if such a retirement benefit is in the nature of either a defined contribution scheme or a defined benefit scheme as described in this Standard. This Standard does not apply to those retirement benefits for which the employer's obligation cannot be reasonably estimated, e.g., ad hoc ex-gratia payments made to employees on retirement. As per the Standard, the cost of retirement benefits to an employer results from receiving services from the employees who are entitled to receive such benefits. Consequently, the cost of retirement benefits is accounted for in the period during which these services are rendered. Accounting for retirement benefit cost only when employees retire or receive benefit payments (i.e., as per pay-as-you-go method) does not achieve the objective of allocation of those costs to the periods in which the services were rendered. The Standard requires that in respect of retirement benefits in the form of provident fund and other defined contribution schemes, the contribution payable by the employer for a year should be charged to the statement of profit and loss for the year. In respect of gratuity benefit and other defined benefit schemes, the Standard lays down that the accounting treatment will depend on the basis of type of arrangement, which the employer has chosen to make.

6.2 Reasons for qualification

The financial statements of a few banks have attracted qualification by the auditors for not complying with this Accounting Standard because the banks had not provided for the liability arising out of leave encashment on retirement. These banks were adopting the 'pay as you go' method whereby the cost of the retirement benefit is recognised only at the time of retirement when payments are made to the employees instead of accounting for the liability on an actuarial basis.

6.3 Action to be taken by banks / Auditors.

6.3.1 Banks are required to account for the liability arising out of leave encashment on retirement on an accrual basis. As the Standard does not provide for any transition period to enterprises that are yet to achieve full compliance it would be unavoidable for the statutory auditors to make a qualification until the Accounting Standard has been fully complied with. With a view to ensuring that the qualification by the auditor does not

arise banks, which are yet to fully comply with the Standard, are required to provide for the accrued liability for leave encashment on retirement as on 31st March 2003 by charging the same to their profit and loss account for the year ending on that date. However, considering the financial implication of accounting for the past requirements in the current year's income, banks have the option to charge the liability for leave encashment on retirement accrued up to 31st March 2002 to the revenue reserves. Banks may disclose the change in accounting policy in the appropriate schedule relating to 'Significant changes in Accounting Policies' / 'Principal Accounting Policies'.

7. Accounting Standard 17 - Segment Reporting

7.1 Gist of the Accounting Standard

The Standard establishes principles for reporting financial information, about the different types of products and services an enterprise produces and the different geographical areas in which it operates. As per the Standard, for reporting the financial information, business and geographical segments are required to be identified. It provides that one basis of segmentation is primary and the other is secondary, with considerably less information required to be disclosed for secondary segments. It contains requirements for identifying reportable segments and lays down disclosures required for reportable segments for primary segment reporting format of an enterprise as well as the disclosures required for secondary reporting format of the enterprise. It also addresses several other segment disclosure matters.

7.2 Reasons for qualification

Banks were not able to adopt the Accounting Standard due to lack of clarity for identifying the business segments and geographical segments as also the absence of uniform disclosure formats as relevant to banks.

7.3 Action to be taken by banks / Auditors

7.3.1 In view of very large branch network and the existing level of MIS and computerisation of public sector banks and the difficulties on account of collection and compilation of details of segment-wise position of assets, liabilities, income, expenses and other information, as an interim measure, it has been decided to recommend a suitable simplified disclosure format which all banks would be in a position to comply with as a first step towards compliance with Accounting Standard 17. However, this does not dispense with the need to provide more disclosures in future after developing an appropriate MIS for the purpose. Hence, banks should initiate measures to move towards greater disclosures within a defined time period.

7.3.2 In view of the above and with a view to adapt the disclosure format prescribed in Appendix III to the Accounting Standard to suit banks it has been decided that banks should uniformly adopt the disclosure format furnished in Attachment 1 of these guidelines. This format indicates the minimum disclosure requirements under this Accounting Standards and banks are allowed the discretion to enhance the disclosure levels.

7.3.3 Banks are advised to adopt the following while complying with the Accounting Standard.

- The business segment should ordinarily be considered as the primary reporting format and geographical segment would be the secondary reporting format.
- The business segments will be 'Treasury', 'Other banking operations' and 'Residual operations'.
- 'Domestic' and 'International' segments will be the geographic segments for disclosure.
- Banks may adopt their own methods, on a reasonable and consistent basis, for allocation of expenditure among the segments.

8. Accounting Standard 18 - Related Party Disclosures

8.1 Gist of the Accounting Standard

This Standard is applied in reporting related party relationships and transactions between a reporting enterprise and its related parties. This Standard requires that name of the related party and nature of the related party relationship where control exists should be disclosed irrespective of whether or not there have been transactions between the related parties. The Standard requires that where control does not exist, certain disclosures have to be made by the reporting enterprise if there have been transactions between related parties, during the existence of a related party relationship. As per the Statement, items of a similar nature may be disclosed in aggregate by type of related party.

8.2 Reasons for qualification

Many banks had not complied with this Accounting Standard due to the following reasons and had, there-

fore, invited qualifications of their financial statements:

- Compliance with the above Accounting Standard would infringe upon their obligation to maintain confidentiality of their customers' accounts.
- Banks were not sure who were their related parties, including key management personnel.
- Absence of a disclosure format relevant to banks.

8.3 Action to be taken by banks / Auditors

8.3.1 In view of the above banks are advised to adopt the following while ensuring compliance with the Accounting Standards

- Related Parties: To begin with, related parties for a bank are its parent, subsidiary(ies), associates/ joint ventures, Key Management Personnel (KMP) and relatives of KMP. KMP are the whole time directors for an Indian bank and the chief executive officer for a foreign bank having branches in India. Relatives of KMP would be on the lines indicated in Section 45 S of the R.B.I. Act, 1934.
- Disclosure format: The illustrative disclosure format recommended by the ICAI as a part of General Clarification (GC) 2/2002 has been suitably modified to suit banks. The illustrative format of disclosure by banks for the AS is furnished in Attachment 2.
- Nature of disclosure: The name and nature of related party relationship should be disclosed, irrespective of whether there have been transactions, where control exists within the meaning of the Standard. Control would normally exist in case of parent-subsidiary relationship. The disclosures may be limited to aggregate for each of the above related party categories and as indicated in Attachment 2, these would pertain to the year-end position as also the maximum position during the year.
- Position of nationalised banks: The Accounting Standards is applicable to all nationalised banks. Paragraph 9 of the Accounting Standards exempts state controlled enterprises i.e., nationalised banks from making any disclosures pertaining to their transactions with other related parties which are also state controlled enterprises. Thus nationalised banks need not disclose their transactions with the subsidiaries as well as the RRBs sponsored by them. However, they will be required to disclose their transactions with other related parties.
- Secrecy provisions: If in any of the above category of related parties there is only one related party entity, any disclosure would tantamount to infringement of the bank secrecy clause. In terms of para 5 of Accounting Standards 18, the disclosure requirements do not apply in circumstances when providing such disclosures would conflict with the reporting enterprise's duties of confidentiality as specifically required in terms of statute, by regulator or similar competent authority. In terms of Paragraph 6 of this Accounting Standard, in case a statute or regulator governing an enterprise prohibits the enterprise from disclosing certain information which is required to be disclosed, non-disclosure of such information would not be deemed as non-compliance with the Accounting Standards. It is clear from the above that on account of the judicially recognized common law duty of the banks to maintain the confidentiality of the customer details, they need not make such disclosures. In view of the above, where the disclosures under the Accounting Standards are not aggregated disclosures in respect of any category of related party i.e., where there is only one entity in any category of related party, banks need not disclose any details pertaining to that related party other than the relationship with that related party.
- Since public sector banks have a large network of branches, these banks should immediately devise an appropriate MIS to support the above disclosures.

9. Accounting Standard 22 - Accounting for Taxes on Income

9.1 Gist of the Accounting Standard

This Standard is applied in accounting for taxes on income. This includes the determination of the amount of the expense or saving related to taxes on income in respect of an accounting period and the disclosure of such an amount in the financial statements. The Standard requires that tax expense for the period, comprising current tax and deferred tax, should be included in the determination of the net profit or loss for the period. As per the Standard, deferred tax should be recognised for all the timing differences, subject to the consideration of prudence in respect of deferred tax assets as specified in the Standard. The Standard requires that current tax should be measured at the amount expected to be paid to (recovered from) the taxation authorities, using the applicable tax rates and tax laws. Deferred tax assets and liabilities should be measured using the tax rates and tax laws that have been enacted or substantively enacted by the balance sheet date. The

Standard also prescribes requirements in respect of re-assessment of unrecognised deferred tax assets and review of deferred tax assets. The Standard also provides transitional provisions to deal with the deferred tax balance that has accumulated prior to the adoption of the Standard.

9.2 Reasons for qualifications

Banks have expressed difficulties in complying with the Accounting Standard since creation of Deferred Tax Liability (DTL) or Deferred Tax Asset (DTA) would put them in a position by virtue of which they would be restrained due to certain statutory / regulatory requirements.

- Creation of a deferred tax liability (transition DTL) by debit to revenue reserves for the accumulated effect as on 1st April 2001 would affect banks' Capital to Risk Weighted Assets Ratio (CRAR) adversely unless such DTL is treated as Tier 1 capital.
- DTA created in compliance with Accounting Standards 22 would be in the nature of an intangible asset. Hence creation of a deferred tax asset might affect bank's ability to declare dividends in view of the provisions of Section 15(1) of the BR Act whereby banking companies are prohibited from paying dividend on their shares until all their capitalised expenses including preliminary expenses, accumulated losses and any other expenditure not represented by tangible assets have been completely written off.

9.3 Action to be taken by banks / Auditors

9.3.1 Adoption of AS 22 may give rise to creation of either a deferred tax asset (DTA) or a deferred tax liability (DTL) in the books of accounts of banks and creation of DTA or DTL would give rise to certain issues which have a bearing on the computation of capital adequacy ratio and banks' ability to declare dividends. In this regard it is clarified as under:

- DTL created by debit to opening balance of Revenue Reserves on the first day of application of the Accounting Standards 22 or to Profit and Loss account for the current year should be included under item (vi) 'others (including provisions)' of Schedule 5 - 'Other Liabilities and Provisions' in the balance sheet. The balance in DTL account will not be eligible for inclusion in Tier I or Tier II capital for capital adequacy purpose as it is not an eligible item of capital.
- DTA created by credit to opening balance of Revenue Reserves on the first day of application of Accounting Standards 22 or to Profit and Loss account for the current year should be included under item (vi) 'others' of Schedule 11 'Other Assets' in the balance sheet.
- Creation of DTA results in an increase in Tier I capital of a bank without any tangible asset being added to the banks' balance sheet. Therefore, in terms of the extant instructions on capital adequacy, DTA, which is an intangible asset, should be deducted from Tier I Capital.

10. Accounting Standard 23 - Accounting for Investments in Associates in Consolidated Financial Statements

10.1 Gist of the Accounting Standard

This Accounting Standard sets out principles and procedures for recognising, in the consolidated financial statements, the effects of the investments in associates on the financial position and operating results of a group. The Standard defines associate as an enterprise in which the investor has significant influence and which is neither a subsidiary nor a joint venture of the investor. The Standard requires that an investment in an associate should be accounted for in consolidated financial statements under the equity method subject to certain exceptions. As per the Standard, the equity method is a method of accounting whereby the investment is initially recorded at cost, identifying any goodwill/capital reserve arising at the time of acquisition. The carrying amount of the investment is adjusted thereafter for the post-acquisition change in the investor's share of net assets of the investee. The consolidated statement of profit and loss reflects the investor's share of the results of operations of the investee. The Standard lays down the requirements in respect of the application of the equity method.

10.2 Action to be taken by banks / Auditors

10.2.1 This Accounting Standard has become effective for accounting periods commencing on or after April1, 2002.

10.2.2 It is observed that there could be certain doubts as to whether conversion of debt into equity in an enterprise by a bank by virtue of which the bank holds more than 20% will result in a investor-associate relationship for the purpose of Accounting Standards 23.

The term associate has been defined as an enterprise in which the investor has significant influence and which is neither a subsidiary nor a joint venture of the investor. Significant influence is the power to participate in the financial and/ or operating policy decisions of the investee but not control over those policies. Such an influence may be gained by share ownership, statute or agreement. As regards share ownership, if an investor holds, directly or indirectly through subsidiaries 20% or more of the voting power of the investee, it is presumed that the investor has significant influence, unless it can be clearly demonstrated that this is not the case. Conversely, if the investor holds, directly or indirectly through subsidiaries less than 20% of the voting power of the investee, it is presumed that the investor does not have significant influence, unless such influence can be clearly demonstrated. A substantial or majority ownership by another investor does not necessarily preclude an investor from having significant influence.

10.2.3 From the above it is clear that though a bank may acquire more than 20% of voting power in the borrower entity in satisfaction of its advances it may be able to demonstrate that it does not have the power to exercise significant influence since the rights exercised by it are protective in nature and not participative. In such a circumstance, such investment may not be treated as investment in associate under this Accounting Standard. Hence the test should not be merely the proportion of investment but the intention to acquire the power to exercise significant influence.

11. Accounting Standard 25 - Interim Financial Reporting

11.1 Gist of Accounting Standard

This Standard prescribes the minimum content of an interim financial report and the principles for recognition and measurement in a complete or condensed financial statements for an interim period. As per the Standard, a statute governing an enterprise or a regulator may require an enterprise to prepare and present certain information at an interim date which may be different in form and/or content as required by this Standard. In such a case, the recognition and measurement principles as laid down in this Standard are applied in respect of such information, unless otherwise specified in the statute or by the regulator. The Standard defines interim financial report as a financial report containing either a complete set of financial statements or a set of condensed financial statements (as described in this Standard) for an interim period. As per the Standard, an interim financial report should include, at a minimum, condensed balance sheet; condensed statement of profit and loss; condensed cash flow statement; and selected explanatory notes. In respect of recognition and measurement, the Standard requires that an enterprise should apply the same accounting policies in its interim financial statements as are applied in its annual financial statements, except for accounting policy changes made after the date of the most recent annual financial statements that are to be reflected in the next annual financial statements. However, the frequency of an enterprise's reporting (annual, half-yearly, or quarterly) should not affect the measurement of its annual results. To achieve that objective, measurements for interim reporting purposes should be made on a year-to-date basis.

11.2 Action to be taken by banks / Auditors

11.2.1 This Accounting Standard is effective from the accounting periods commencing on or after 1st April 2002. Where an enterprise is required to or elects to prepare and present an interim financial report comprising either a complete set of financial statements or a set of condensed financial statements for an interim period, it should comply with this Standard.

11.2.2 The disclosures required to be made by listed banks in terms of the listing agreements would not tantamount to interim reporting as envisaged under the Accounting Standard. Hence, the Accounting Standard is not mandatory for the quarterly reporting prescribed for listed banks. However, the recognition and measurement principles laid down in this Standard would have to be complied with in respect of such quarterly reports.

11.2.3 Appendix 3 to the Standard clarifies that it is not necessary to do a fresh actuarial valuation for each interim period and instead the proportionate estimate of the liability based on the actuarial valuation done at the end of the previous financial year may be used, adjusted for significant market fluctuations since that time and for significant curtailments, settlements or other significant one-time events.

11.2.4 The half yearly review prescribed by RBI for public sector banks, in consultation with SEBI, vide circular DBS. ARS. No. BC 13/ 08.91.001/ 2000-01 dated 17th May 2001 is extended to all banks (both listed and unlisted) with a view to ensure uniformity in disclosures. Banks may adopt the format prescribed by the RBI for the purpose.

12 AS 27 - Financial Reporting of Interests in Joint Ventures

12.1 Gist of the Accounting Standard

This Standard is applied in accounting for interests in joint ventures and the reporting of joint venture assets, liabilities, income and expenses in the financial statements of venturers and investors, regardless of the structures or forms under which the joint venture activities take place. This Standard identifies three broad types of joint ventures, namely, jointly controlled operations, jointly controlled assets and jointly controlled entities. This Standard requires, inter alia, that in its consolidated financial statements, a venturer should report its interest in a jointly controlled entity using proportionate consolidation subject to certain exceptions. The Standard defines proportionate consolidation as a method of accounting and reporting whereby a venturer's share of each of the assets, liabilities, income and expenses of a jointly controlled entity is reported as separate line items in the venturer's financial statements.

12.2 Action to be taken by banks / Auditors

12.2.1 This Standard, which is effective from 1st April 2002, sets out the principles and procedures for accounting for interests in joint ventures and reporting of joint venture assets, liabilities, income and expenses in the financial statements of the ventures and the investors. In respect of separate financial statements of an enterprise, this standard is mandatory in nature from the above date. In respect of consolidated financial statements of an enterprise, this standard is mandatory in nature where the enterprise prepares and presents the consolidated financial statements in respect of accounting periods commencing on or after 1st April 2002.

12.2.2 It is clarified that though paragraph 27 of the Accounting Standard prescribes that for the purpose of solo financial statements, investment in jointly controlled entities is to be accounted as per Accounting Standard 13, such investment is to be reflected in the solo financial statements of banks as per guidelines prescribed by RBI since Accounting Standard 13 does not apply to banks.

12.2.3 In view of the above, this Accounting Standard applies in case of jointly controlled entities only where banks are required to present consolidated financial statements, whereby the investment in JVs should be accounted for as per provisions of the Standard. However, in respect of joint ventures in the form of joint controlled operations and jointly controlled assets, the Accounting Standard is applicable for both solo financial statements as well as consolidated financial statements.

12.2.4 RRBs sponsored by banks would be treated as associates and therefore the provisions of the Accounting Standard would not apply. The investment in RRBs will however, be accounted in the consolidated financial statements as per the provisions of Accounting Standard 23. ■