

Accounting Treatment of Import Duty and Voyage Expenses on Import of Dredger

The following is the brief version of an opinion given by the Expert Advisory Committee of the Institute in response to query sent by a member. This is being published for the information of readers.

A. Facts of the Case

1 A public sector undertaking under the Ministry of Transport, incorporated under the Companies Act, 1956, has the main objective of providing integrated dredging services to all major and minor ports, Indian Navy, fishing harbors and other maritime organisations.

2 During the year 2000-01, the company acquired one ocean going self-propelled Trailer Suction Hopper Dredger (hereinafter referred to as 'the dredger') from Holland. As per the contractual terms, the dredger was delivered at builder's yard at The Netherlands after completion of necessary inspection formalities and successful sea trials. As per the terms of the contract with the builder, the price of the dredger is ex-yard, the builder, and legally and contractually, the property in the dredger was passed on to the company on taking delivery at The Netherlands. The company's personnel manned the dredger on its maiden voyage to India. When the dredger was delivered at the builder's yard, it was complete in all respects and ready for its intended use, i.e., dredging.

3 After completion of the maiden voyage, the dredger

1. The Opinion is only that of the Expert Advisory Committee and does not necessarily represent the Opinion of the Council of the Institute.

2. The Compendium of Opinions containing the Opinions of Expert Advisory Committee has been published in 20 volumes which are available for sale at the Institute's office at New Delhi and its regional council offices at Mumbai, Chennai, Kolkata and Kanpur.

reached Chennai port in March 2001. The company paid an amount of Rs. 896.81 lakh towards customs duty at Chennai port. During the maiden voyage from The Netherlands to India, the company also incurred voyage expenses amounting to Rs.180 lakh.

4 The cost of the dredger was capitalised in the books of the company in the financial year 2000-01. While capitalising the same, the company has not included the voyage expenses as well as the customs duty paid in the cost of the asset and charged off the same to the profit and loss account. Similarly, the voyage expenditure on a dredger acquired during the previous year from the same builder at The Netherlands was also charged off to the profit and loss account during the current year.

5 The C&AG objected to this treatment stating that the voyage expenses and the customs duty should be included in the capital cost of the dredger. The comments issued by the C&AG in this respect are reproduced below:

“Balance Sheet
Application of Funds
Fixed Assets (Gross Block)(Schedule-IV)
Dredgers – Rs. 56,576.26 lakh

The above is understated by Rs.1205.47 lakh due to charging off of customs duty (Rs. 896.81 lakh) and transportation charges (Rs. 179.47 lakh) in respect of the dredger XVI and withdrawal of transportation charges of Rs. 129.19 lakh in respect of dredger XV capitalised in the previous year. This has resulted in understatement of depreciation by Rs. 17.80 lakh and profit for the year by Rs. 1187.67 lakh.”

6 The querist, has drawn the attention of the Committee to paragraph 9.1 of Accounting Standard (AS) 10, 'Accounting for Fixed Assets', issued by the Institute of Chartered Accountants of India, which states that 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". In the case of the company, the dredger was ready in all respects and ready for its intended use at the time the company took delivery of the dredger ex-builder's yard at The Netherlands after successful completion of all tests and trials stipulated in the relevant agreement with the builder. As per the querist, the cut off point for capitalisation of the cost of dredger is that point of time and voyage expenses and payment of customs duty arose subsequently. According to the querist, AS 10 clearly specifies capitalisation of the expenditure incurred upto the point when the asset is ready to be put to its intended use. The company had earlier negotiated with a German customer for a dredging contract employing this dredger at Germany.

7 The querist has further argued that as per paragraph 9.4 of AS 10, the expenditure incurred on start-up and commissioning of the project, including the expenditure incurred on test runs and experimental production, is usually capitalised as an indirect element of the construction cost. Further, as per paragraph 9.5 of AS 10, if the interval between the date a project is ready to commence commercial production and the date at which commercial production actually begins is prolonged, all expenses incurred during this period are charged to the statement of profit and loss. As per the querist, it is clear from the above that the intention of the Standard is that the expenditure incurred upto the period the asset is ready to be put to its intended use only, shall be treated as part of capital cost. According to the querist, in the case of the company, the dredger was ready to be put to its intended use when the dredger was taken delivery ex-builder's yard at The Netherlands, and therefore, any expenditure incurred thereafter shall not form part of the capital cost.

B. Query

8 The querist has sought the opinion of the Expert Advisory Committee as to whether the company should

capitalise the import duty and voyage expenses as a part of the cost of the dredger.

C. Points considered by the Committee

9 The Committee notes paragraph 9.1 of AS 10, which is reproduced below:

"9.1 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. Examples of directly attributable costs are:

- (i) site preparation;
- (ii) initial delivery and handling costs;
- (iii) installation cost, such as special foundations for plant; and
- (iv) professional fees, for example fees of architects and engineers.

The cost of a fixed asset may undergo changes subsequent to its acquisition or construction on account of exchange fluctuations, price adjustments, changes in duties or similar factors."

10 The Committee notes from the above that import duties and initial delivery and handling costs should be capitalised as a part of the cost of an item of a fixed asset. The Committee also notes that despite the company's negotiations with a German customer for employing the dredger at Germany, the dredger was actually brought and put to use in India. Accordingly, the Committee is of the view that the import duties and voyage expenses incurred to bring the dredger to India from The Netherlands should be capitalised as a part of the cost of the dredger.

D. Opinion

11 On the basis of the above, the Committee is of the opinion that the customs duty paid and voyage expenses incurred in respect of the maiden voyage of the dredger from The Netherlands to India should be included in the cost of the dredger.