

Standardisation of Accounting Practices in Agriculture Sector in India



Agriculture accounting did not receive much attention around the world, particularly in India. There are many reasons for non-development of agriculture accounting, especially in the non-organised agriculture sector in India. Importance of agriculture accounting cannot be overlooked. Ind AS 41 Agriculture, Ind AS 16 Property, Plant and Equipment, and Ind AS 113 Fair Value Measurement throw light on agricultural accounting. There are numerous issues that require further research to standardise prudent accounting practice in 'agriculture accounting'. In this article, a simplified accounting system for small, marginal and medium farmers is suggested. Proposed 'farm accounting system' is based on 'statement of net worth' or 'statement of affairs'. Read on...

1. Introduction

1.1 ¹Agriculture is the backbone of the Indian economy, where roughly half of the work force is engaged in agriculture for its livelihood. On the other hand, an average Indian still spends almost half of his/her total expenditure on food. Accordingly, while being both a source of livelihood and food security for a vast majority of low income, poor and vulnerable sections of

society, this sector assumes crucial significance in the Indian economy.

- 1.2 The experience from BRICS countries indicates that a one percentage growth in agriculture is at least two to three times more effective in reducing poverty than the same growth emanating from non-agriculture sectors. Accordingly, over the period, it has been realised by the Government and it has given higher priority to agriculture sector in order to achieve the goals of reducing poverty and malnutrition as well as of inclusive growth. Since agriculture forms the resource base for a number of agro-based industries and agro-services, it is more meaningful to view agriculture not as farming alone but as a holistic value chain, which includes farming, wholesaling, warehousing (including logistics), processing and retailing.
- 1.3 In view of the above, the Central and State Governments from time to time come out with various schemes to educate the farmers, to create sufficient infrastructure for agriculture, to introduce new techniques of farming, *etc.*



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¹ <http://agricoop.nic.in>, Ministry of Agriculture, Government of India 2015

2. Objectives

Following are the objectives of presenting this paper-

1. To create awareness of agricultural accounting.
2. To introduce simplified accounting system for the use of small, marginal and medium farmer.
3. To understand conceptual differences of agricultural income under common parlance and the Income-tax Act.

3. Review of Concept of Development

Traditionally, in India, agricultural activities are carried out as a family ancestral routine and as a source of livelihood. Family members themselves provide labour input to carry out the activities. Majority of the population is having only small and marginal land holding and holding area is getting further decreased on account of its fragmentation. Farming operates mostly with barter exchange of goods and services. The farming conditions also differ from one location to the other. Farming activities are also dependent on nature, climatic conditions, government policies and are subject to uncertainties and daily market fluctuations.

3.1 Following are some of the reasons for non-development of agriculture accounting especially with non-organised agriculture sector in India –

1. Accounting requires maintenance of books of accounts and documents. Small farmers neither have a skill-set nor is there an environment or awareness to keep books and records.
2. Agricultural income is exempt from income tax.
3. No farmer is required to submit any financial statements to the government or banks or any other stakeholder. Banks grant loan on the basis of pre-determined fixed parameters.
4. The agriculture sector is not recognised like an industrial or business sector.
5. No separate cash/bank account for agricultural operations is maintained. All personal transactions as well as transactions relating to agricultural

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- activities are operated through common cash/bank account. Most of the farmers do not even have bank accounts.
6. Most of the transactions are on non-monetary basis i.e., barter or exchange of goods and services. In order to maintain books of accounts, it is necessary to translate the barter transactions into common unit of measurement i.e. monetary value. Valuation as regards the valuation of goods or services exchanged is thus, one of the hurdles for accounting.
7. Part of the farm produce and products are consumed by the farmer and his family members. These are required to be translated into monetary value, if not accurately, at least on approximate basis.
8. The farmer and his family members provide labour to the farm, in addition to the time devoted for management.
9. Farming operations are involved with uncertainties of weather, rain, flood, pests, continuous market fluctuations, government policies, *etc.*
10. Maintaining books of accounts (except farming corporations, government farms and companies involved with agricultural activities) is neither a legal requirement nor a customary practice in India.
11. Valuation of livestock, farm produce, feed, fodder, seeds, fertilisers, pesticides, standing crop, *etc.* is difficult on the part of a majority of uneducated or inadequately educated farmers.
12. Farmers carry out allied activities like dairy, poultry, sericulture, animal husbandry, piggery, aquaculture, apiculture, *etc.* Proper training is a must to maintain proper books of accounts and analyse activity-wise net results with recording of inter departmental transfers.
13. Farmer is not convinced that by maintaining books of accounts, he is in a position to take better managerial decision or change his earnings.
14. Year ending concept is yet to be accepted by the farmer. The Income-tax Act prescribes 31st March as uniform previous year. This cutoff date varies with farming season (Rabbi) which usually ends in April/May. Year-ending date to end with

farming season is more problematic in case of perennial irrigation farms.

15. Literature on the subject of accounting in local languages is not available.
 16. Agriculture cess or revenue is not collected by the government on the basis of quantum of agricultural income.
 17. Crop/trees insurance is yet to be popularised in agriculture sector. To compensate losses on account of calamities beyond the control of a farmer by insurance companies, past track record is required to be ascertained.
 18. Accounting practices in India require to be standardised.
- 3.2 Agriculture accounting in India, therefore, is not even at an infant stage and is yet to grow. Educational illiteracy and inadequate earnings by a majority of small and medium farmers can also be considered as a real cause to this issue. It is, however, necessary for the understanding of the farmer himself and society at large, a take off in this connection is a must.

4. Accounting Standards for Agricultural Sector

- 4.1 Agriculture accounting did not receive much attention around the world, particularly in India.
- 4.2 In April 2001, the International Accounting Standards Board (IASB) adopted IAS 41, *Agriculture*, as part of International Financial Reporting Standards (IFRS). In December 2003, the IASB revised IAS 41.
- 4.3 In June 2014, the IASB amended the scope of IAS 16 *Property, Plant and Equipment*, to include bearer plants. Bearer plants related to agricultural activity were previously within the scope of IAS 41. The IASB decided that bearer plants should be accounted for in the same way as property, plant and equipment in IAS 16, because their operation is similar to that of manufacturing. However, the produce growing on bearer plants would remain within the scope of IAS 41².
- 4.4 The Institute of Chartered Accountants of India (ICAI), being the highest accounting body in India, formulates accounting standards (AS)

through its Accounting Standards Board (ASB) established in April 1977.

- 4.5 The Accounting Standards, as recommended by the ICAI, had been notified by the Ministry of Corporate Affairs, Central Government in consultation with the National Advisory Committee on Accounting Standards (NACAS) in the year 2006³ under the Companies (Accounting Standards) Rules, 2006 as a part of the Companies Act. At present, 29 Accounting Standards (ASs) are notified by the Ministry of Corporate Affairs (MCA) under the Companies Act. However, there is no specific AS dealing with the agriculture accounting.
- 4.6 After converging IFRS based standards, ICAI converged 39 IFRSs in the form of Ind AS with carve-outs as approved by the NACAS and notified as second set of accounting standards in India by MCA under recently introduced Companies (Indian Accounting Standards) Rules, 2015 as a part of the Companies Act, 2013 effective from 1st April 2015 to certain notified companies. Ind AS comprise of standard on 'Agriculture' as Ind AS 41⁴.

5. Importance of Agriculture Accounting

Agriculture accounting's importance can be viewed with the below listed reasons:

- 5.1 Joint stock companies (engaged in agricultural activity viz. tea plantations, rubber plantations, coffee plantations, orchards, cash crops, etc.) are required to maintain books of accounts under the Companies Act.
- 5.2 Net agricultural income is required to be ascertained in order to ascertain income tax liability (with aggregation procedure) in case of certain taxpayers like individuals, HUF and association of persons or body of individuals.
- 5.3 Agricultural income derived outside India in case of residents is subject to income tax in India.
- 5.4 The farmer himself will be in a position to know his fair profitability or surplus and financial position.
- 5.5 Farmer may be in a position to take better managerial decision in light of past performance.
- 5.6 National income can be calculated with better accuracy.

² IAS 41 *Agriculture* issued by the International Accounting Standard Board 2015

³ Notification dated 07.12.2006 on the Companies (Indian Accounting Standards) Rules 2006 issued by the Ministry of Corporate Affairs, Government of India.

⁴ Notification dated 16.2.2015 on the Companies (Indian Accounting Standards) Rules 2015 issued by the Ministry of Corporate Affairs, Government of India.

- 5.7 State and Central governments will be in a better position to frame agricultural policies in the national interest.
- 5.8 Farmer will be in a better position to ascertain his income from allied activities to agriculture.

6. Accounting Practices and Proposing Revised System for Agriculture Accounting

- 6.1 Only joint stock companies, government farms and state farming corporations are maintaining books of accounts and prepare financial statements for the benefit of concerned stakeholders.
- 6.2 In addition, few progressive farmers in India having cash crops, orchards, plantations with perennial irrigation facilities might be maintaining books of accounts in some way or other in the form of diary or register (not necessarily systematic book-keeping).
- 6.3 Most of the developed countries have levied tax on agriculture income. Maintaining books of accounts with large farming area, favourable climatic conditions, better capital investment, *etc.* is not a problem for corporate farming or co-operative farming or farmer with larger area under cultivation.
- 6.4 In India, an accounting system is required to be introduced, propagated, and published in local and simplified languages to develop skill-set in this connection.
- 6.5 Accounting system to be followed by the farmers as is visualised may be categorised in two parts—
1. Small, marginal, medium farmer (even farmer with large holding)—Simplified Accounting System (may be called as 'Farm Accounting')
 2. Other corporate entities, State farming corporations (even progressive farmer can follow this system) may be called as 'Double Entry of Full Proof Book-Keeping System'.

6.6 Farm accounting for small, marginal and medium farmers

A system must have the following features to catch the **SPEED**—

- S** = Simple
P = Practical
E = Effective
E = Economical
D = Duplicable

The system is based on maintaining minimum records and books of accounts. This may also be referred as 'Accounts from Incomplete Records'.

A simplified 'farm accounting' is based on 'statement of net worth' or 'statement of affairs'. 'Statement of net worth' is a statement of agricultural assets and liabilities as on a particular date by estimating the values. This statement is required to be prepared at the beginning and at the end of the accounting year. Accounting year for farming operations must end with cropping season (Rabbi Season which usually ends in April/May). However, with perennial irrigation, usually three crops are also taken by a farmer viz. Kharif Crop, Rabbi Crop and small duration vegetable crop. In case of perennial irrigation, there is a continuing farming process throughout the period for cash crops, orchards and plantations. Even the end of Rabbi Season varies in different locations of India. With these deliberations, it is assumed that a uniform year ending date viz. 31st March may be taken as cut-off date for farm accounting purposes.

6.6.1 The study⁵ conducted by Mr. C. H. Shah on the farm in Kodinar Taluka in the State of Gujarat can be considered as an indicator. He has classified agricultural inputs as under—

1. Land
2. Labour
3. Livestock
4. Manure, Fertilisers, Pesticides, Insecticides, Fungicides, Weedicides, *etc.*
5. Seed
6. Implements

1. Land: Land is a vital and most important physical asset of a farm. Land includes expenditure on its development also. Many times, land under cultivation is taken on rental basis (barter) under the share cropping arrangement. In the sharing arrangement, the farmer cultivates the

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⁵ Monograph on Accounting for Agricultural Operations, The Institute of Chartered Accountants of India – Research Committee in 1983, New Delhi.

land belonging to the landlord and the cultivator pays rent for the farm in the form of a share in the final produce.

Open well or bore well dug (other than machinery and electricals installed) in a land may be considered as an integral part and parcel of land and hence, may be capitalised with land. Land is usually considered as non-depreciable asset and may be considered for impairment as and when necessary.

2. **Labour:** The labour employed on a farm may be either family labour or hired labour. Hired labour may be temporary or permanent and may be paid in cash or kind. The opportunity cost of family labour can be assessed on the basis of man-day inputs and categories of labour. The hired labour cost may be ascertained on the basis of labour-pay register with cash and exchange column (filled with quantity of produce shared with laborer) and additional column for conversion in monetary value. These registers may be maintained on daily basis closed monthly.
3. **Livestock:** Livestock is usually the major physical asset of a farm, especially for a small, marginal and medium farmer. Progressive farmers have, nowadays, reduced livestock and replaced it with tractors, implements and other mechanic equipment. Livestock may be used for dairy or for draught purpose.
4. **Manure, Fertilisers, Pesticides, Insecticides, Fungicides and Weedicides, etc.:** Consumption of these items is an important input to the farm. Manure may be either farm yard manure (dung of livestock or compost manure in a farm) or

chemical fertiliser. Use of other inputs of pesticides, insecticides, fungicides, weedicides, etc. is increasing day by day. These are however, normally purchased items.

5. **Seeds:** The seeds used on a farm may be either purchased seeds or farm grown seeds. With the invention of high yielding varieties, the relative proportion of purchased seeds is increasing in recent times.
6. **Implements:** This includes tractors, water pumps, bullock carts, ploughs, sowing implements, and harvesting implements, etc. These implements are for long lasting use and are in the nature of fixed assets.

7. Detailing the Steps for Ascertainment of Income from Agricultural Activities under the Proposed System

Step 1—Prepare a Statement of Net Worth at the beginning of the year [A Statement of Net Worth prepared at the end of earlier year to be considered]

Estimate the value of assets and liabilities on the basis suggested below—

Assets:

Land: May be taken at market value (including open well/bore well)

Sheds and Farm House: Cost less depreciation

Livestock: Estimated market value

Implements: At cost less depreciation based on life of the asset

Stock of Manure, Fertilisers, Pesticides, Insecticides, Fungicides, and Weedicides, etc.: At cost

Cash on Hand: At actuals

Balance at Bank: At actuals (subject to pending cheques deposited and cheques issued)

Advance to Labors: At actuals

Farm Yielded Seed: Estimated market value

Purchased Seed: At cost

Other Advances: Actuals

Other Assets: Estimated value

Receivable: At actuals

Liabilities:

Bank Loan: Outstanding balance as per bank statement

Personal Loans (For Agriculture): At actuals

Wages Payable to Laborers: Estimated basis

Bill Payable to Supplier: At actuals

Other Payables: At actuals

Opening Capital = Assets – Liabilities

The opportunity cost of family labour can be assessed on the basis of man-day inputs and categories of labour. The hired labour cost may be ascertained on the basis of labour-pay register with cash and exchange column (filled with quantity of produce shared with labourer) and additional column for conversion in monetary value.

Step 2 – Prepare a Statement of Net Worth at the end of the year.

Estimate the value of assets and liabilities at the end of the year.

Closing Capital = Assets – Liabilities

Step 3–Find out Farmers Drawings and Consumption of Farm Produce.

- Bank withdrawals for personal use [not for farm operation payments]

- Bank payments for personal use

- Bank payments for personal asset [not for farm asset payments]

- Consumption of farm produce by family (on estimated basis)

Step 4: Find out Personal Deposits (including cheque deposits).

Step 5: Find out value of Labour and Management by farmer and his family members on estimated basis.

Step 6: Find out increase in Market Value of Land during the year.

Step 7: Find out Net Result for the year with Reconciliation.

Reconciliation	Step Ref.	Amount (₹)	Amount (₹)
Closing Capital as on 31 st March	2	
Add: Farmer's Drawings and Consumption of Farm Produce by family	3	
Less: 1. Farmer's Personal deposits	4	
2. Farmer's Family Labour and Management	5	
3. Increase in Value of Land [Not considered as part of Surplus/ (Deficit)]	6
Closing Adjusted Capital as on 31 st March		
Less: Opening Capital as on 1 st April	1	
∴ Net Surplus/(Deficit) for the year		

7.1. Advantages of Proposed System:

1. Easy to understand.
2. Net Surplus/(Deficit) is ascertainable.

3. Minimum records required to be maintained.

4. If transactions are routed through bank account, there will be more accurate and reliable result.

5. Simple to operate.

6. Fair value concept introduced.

7.2 If figures in opening and closing net worth are worked out with accuracy and reliability and with maintenance of additional registers, one can prepare 'Income and Expenditure Account'.

7.3. Limitations

1. No full-fledged double entry system.

2. Difficult to arrive at a summary of income and expenses (Head wise).

3. Departmental profit cannot be ascertained (like poultry, dairy, sericulture, etc.).

4. Lesser accuracy/reliability.

5. Publicity for accounting system is required in local language.

6. Training to farmers will help in implementation of the system.

7.4 *Farm Accounting for Corporate, Government Farms, State Farming Corporations. (Including progressive farmers, who can follow the system):*

These entities or individuals can maintain under double entry book keeping system with primary books and secondary books as ledger under full-fledged accounting system like any other commercial organisation under 'accrual system of accounting'.

Note: This system is not elaborated in detail, as accounts will be maintained like any other commercial or business entity.

8. Critical Issues Pertaining To "Agriculture Accounting"

8.1 Following critical issues require further research to standardise prudent accounting practice in 'agriculture accounting':

1. Treatment of land development expenses.

2. Treatment of expenditure on 'Green Manure' having benefit for more than two years.

3. Treatment of expenditure on 'Arhar Dal' raised to maintain fertility of land.

4. How to treat initial expenditure like sugar cane plantation (which will remain as first crop, Dubar and Ratoon) over a period of three years.

5. Treatment of expenditure on open well/bore well.

6. Valuation of standing crop [whether to consider event occurring after balance sheet date].
7. Expenditure on long live and late yield trees like teak, orchards, rubber trees, coconut, *etc.*
8. Valuation of livestock.
9. Whether allied activities like dairy, poultry, sericulture, animal husbandry, piggery, sericulture, aquaculture, *etc.*, along with farming operations are part and parcel of agricultural income?
10. Whether income from nursery plantation is agricultural income?
11. Whether agricultural land should be depreciated in view of reduction in the agriculture produce over a period of time?

9. Tax Implications of Agriculture Income

9.1 Section 2(1A) of the Income-tax Act⁶ defines *agriculture* income as-

- (a) Any rent or revenue derived from land which is situated in India and is used for agricultural purpose.
- (b) Any income derived from such land by agricultural operations including processing of the agricultural produce, raised or received as rent in kind so as to render it fit for market, or sale of such produce.
- (c) Income attributable to a farm house subject to the condition that the building is situated in the immediate vicinity of the land and the same is used as dwelling house, store house or other out building and the land is assessed to land revenue or a local rate or alternatively, the building is situated on or in the immediate vicinity of land which (though not assessed to land revenue) is situated in rural area.

9.2 Rural area for the above purpose is any area outside the jurisdiction of a municipality or cantonment board having a population of 10,000 or more and which does not fall within notified distance from the local limits:

Population:

More than 10,000 – up to 1,00,000 : 2 km

More than 1,00,000 – up to 10,00,000 : 6 km

More than 10,00,000 : 8 km

9.3 Section 10(1) exempts agricultural income from income tax. The reason for exemption is that the Constitution of India gives exclusive power to the State legislature to make laws with respect

to taxes on agricultural income. However, in case of some tax payers, agricultural income is taken into consideration for aggregation with taxable income and determination of tax liability.

9.4 For disintegrating a composite business income which is partly agricultural and partly non-agricultural, the Income Tax Rules provide a base–

Sr. No.	Income	Agricultural Income	Non Agricultural Income	Rule Ref.
1.	Growing and Manufacturing of Tea in India	60%	40%	8
2.	Growing and Manufacturing of Rubber	65%	35%	7A
3.	Growing and Curing of Coffee	75%	25%	7B(1)
4.	Growing, Curing, Roasting and Grounding of Coffee	60%	40%	7B(1A)
5.	Other Composite Income	Market Value of Agricultural Produce	Balance Income	7

9.5 The scheme of aggregation of agricultural income with non agricultural income for rate purpose is applicable only in the case of –

- Individuals
- Hindu Undivided Families
- Associations of Persons, or Bodies of Individuals
- Artificial Juridical Persons

It applies only when the aforesaid assessee has non-agricultural income of an amount exceeding ₹5,000 and non agriculture income exceeds the basic exemption limit as is applicable for respective assessment year.

Section 10(1) exempts agricultural income from income tax. The reason for exemption is that the Constitution of India gives exclusive power to the State legislature to make laws with respect to taxes on agricultural income. However, in case of some tax payers, agricultural income is taken into consideration for aggregation with taxable income and determination of tax liability.

⁶ The Income-tax Act, 1961 2015 Edition, Ministry of Finance, Government of India.

- 9.6 Procedure for Computation of Tax –
1. Compute net agricultural income.
 2. Aggregate net agricultural income with non-agricultural income and compute tax liability (before surcharge and education cess) on aggregated income.
 3. Compute tax liability (before surcharge and education cess) on net agricultural income plus basic exemption limit (charged 'nil' rate).
 4. Tax liability (before surcharge and education cess) = Tax liability in Step No. 2 above – Tax liability in Step No. 3 above.
 5. Final tax liability = Tax liability in Step 4 above + Surcharge (if applicable) + Education cess
- 9.7 Agricultural income as referred in Section 2 (1A) is to be computed on the same basis as is adopted for computation of income chargeable under the head 'Profit and Gains of Business or Profession' or 'Income From Other Sources' or 'Income From House Property', as the case may be.
- 9.8 Loss incurred in agriculture is allowed to be set off against gains from agriculture for not more than subsequent eight years. No set off is however allowed in respect of assessee's share in agriculture loss of an association of persons or body of individuals.
- 9.9 Any tax on agricultural income (if any) by State Government is allowed as deduction.
- 9.10 Where the net result of computation of agriculture income is a loss, the loss will be disregarded for aggregation with non-agricultural income.
- 9.11 The net agricultural income of the assessee will be rounded off to the nearest multiple of ₹10.
- 9.12 Considering the above referred provisions of the Income-tax Act, the following income is not an agricultural income though it may be connected with agricultural land–
1. Income from dairy farming.
 2. Income from poultry farming.
 3. Income from the activities like aquaculture, sericulture, wormiculture, apiculture, ferry boats *etc.*
 4. Income from sale of agriculture land.
 5. Income from rearing of animals (livestock).
Income from sales of produce from horticulture and floriculture is part of agriculture income.

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In order to develop unorganised agriculture sector with proper perspective through allocation of public funds and compensate farmers for their farm yield with fair market values, it is necessary to understand the financial performance and financial position of farmers in India at root level. For this purpose, government has to take a base of income derived by farmers from agricultural activities.

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10. Justifying the Premises

In order to develop unorganised agriculture sector with proper perspective through allocation of public funds and compensate farmers for their farm yield with fair market values, it is necessary to understand the financial performance and financial position of farmers in India at root level. For this purpose, government has to take a base of income derived by farmers from agricultural activities. Farmer as an individual has neither the skill set nor resources to have an elaborate accounting system. With the simplified accounting system as proposed in this paper, the authors hope that farmers will begin with new era of agriculture accounting and develop sustainability of the agricultural sector in the times to come.

11. Conclusion

- 11.1 It may be concluded that agriculture sector has always played a pivotal role in the Indian economy. This sector continues to provide employment and livelihood for majority of the population. Over the period, the accounting practices in non-organised part of agriculture sector have not been evolved to the required extent. Emerging new accounting policies and practices at par in organised sector with international practices will certainly improve the quality of agriculture accounting.
- 11.2 It is being felt that in the initial phase, there may be some issues in implementing new Ind AS to agriculture sector. However, over the period these issues will also get resolved and accounting for this sector will result into reflecting true and fair view of the financial position and financial performance of this sector. Similarly small, marginal and medium farmers will begin ascertainment of agricultural income with the simplified system proposed in this paper to develop his own sustainability. ■