



Ind AS 118 and Gross Profit: A New Reporting Consideration for Indian Companies

From nature-based reporting to management judgment in expense presentation

In our earlier article, [“Ind AS 118 and the Changing Face of Income Statement Reporting”](#), we discussed the broader changes proposed by Ind AS 118 and their implications for presenting and communicating of financial performance. While Ind AS 118 has not yet been notified in India, the Exposure Draft proposes an effective date of 1 April 2027, broadly aligned with IFRS 18’s effective date for annual reporting periods beginning on or after 1 January 2027.

The proposed standard also introduces a renewed focus on presenting operating expenses. In doing so, it raises an interesting question for Indian companies: under what circumstances might gross profit emerge as a reported subtotal within the financial statements?

Gross Profit in Indian Financial Reporting

Gross profit is one of the most widely recognised indicators of business performance globally. It is commonly reported by companies that separately present revenue and cost of sales, particularly in sectors such as manufacturing, retail and consumer products. Investors often use gross profit and gross margin to understand pricing, cost structures, product mix and the extent to which revenue covers the direct costs of generating that revenue.

Yet gross profit has historically been uncommon on financial statements prepared under Ind AS. Indian companies typically present expenses through line items such as employee benefits expense, depreciation and amortization, finance costs and other operating expenses. While this provides useful information about the nature of resources consumed, it does not ordinarily identify cost

of sales as a distinct category. Consequently, gross profit does not naturally emerge as a reported subtotal.

The proposed introduction of Ind AS 118 may require companies to revisit this long-established reporting convention.

Nature-Based Expense Presentation in India

Historically, global IFRS reporting permitted operating expenses to be presented either by nature or by function, depending on which approach provided more useful information to users of financial statements. As a result, reporting practices evolved differently across industries and jurisdictions.

The Indian position developed differently. The existing requirements of Ind AS 1, together with the format prescribed by Schedule III to the Companies Act, 2013, resulted in a predominantly nature-based presentation of operating expenses. Most companies therefore reported expenses through captions such as employee benefits expense, depreciation and amortization, finance costs and other expenses rather than by business function.

The relative absence of gross profit from Indian financial reporting is therefore not accidental. It largely reflects how expense presentation developed within the Indian reporting framework.

What Changes Under Ind AS 118

The proposed Ind AS 118 introduces a different approach to the presentation of operating expenses. Rather than prescribing a nature-based presentation, the standard requires entities to present operating expenses in a manner that provides the most useful, structured summary of expenses using characteristics of:

- the nature of expenses;
- the function of expenses; or
- a combination of both approaches.

Importantly, this is not intended to be a free accounting policy choice. In determining the appropriate presentation, entities are expected to consider:

- the principal drivers of profitability;
- how the business is managed and reported internally;
- prevailing industry practice; and
- whether allocations to functions can be made without introducing arbitrary or unreliable judgements.

Where expenses cannot be meaningfully allocated, presentation by nature may remain more appropriate. The standard also recognizes that a mixed presentation may sometimes provide the most useful information.

The significance of the change therefore lies less in the availability of functional presentation and more in the requirement for management to actively evaluate which presentation provides the most useful information about the business.

Where Gross Profit Fits Into the Discussion

Gross profit is not a separate reporting choice under Ind AS 118. Rather, it often results from a broader decision about how to present operating expenses. Where management concludes that a functional presentation provides the most useful information and separately identifies cost of sales as a functional expense category, gross profit naturally emerges as a reported subtotal. Conversely, where expenses continue to be presented by nature, gross profit would generally not arise.

The introduction of Ind AS 118 should therefore not be viewed as requiring entities to report gross profit. Rather, it introduces a framework under which entities are expected to assess how operating expenses should be presented.

The outcome of that assessment is likely to vary across industries and business models. For some entities, particularly in manufacturing, retail and consumer-facing sectors, cost of sales may be a principal driver of profitability, and a functional presentation may provide meaningful information about business performance. For others, particularly where employee costs, technology costs or other operating expenses are more significant drivers of performance, presentation by nature may continue to provide more useful information.

A mixed presentation may also emerge in practice, particularly where some operating expenses can be meaningfully allocated by function while others cannot. Accordingly, there is unlikely to be a single answer for every industry or every company.

How Management Should Approach the Assessment

The assessment of whether operating expenses should be presented by nature, by function, or through a mixed approach is closely linked to how management views and evaluates performance. Where measures such as gross margin, cost of sales or delivery margins already feature prominently in internal reporting, a functional presentation may appear intuitive. For others, performance may be monitored largely through expense categories such as employee costs, technology costs or operating overheads, making a nature-based presentation equally relevant.

Industry practice may also influence the discussion. Where investors and analysts routinely evaluate companies using gross margin-based measures, questions may naturally arise about whether the existing presentation still provides the most useful information. At the same time, peer reporting alone is unlikely to determine the answer. The presentation ultimately needs to reflect the entity's economics, operating model and reporting environment.

An equally important consideration is whether expenses can be allocated to functions in a robust and supportable manner. A functional presentation may appear conceptually attractive, but its usefulness depends on the quality of the underlying allocation methodologies. The discussion becomes more complex when significant categories of expenditure, such as employee costs, technology expenditure, occupancy costs and corporate overheads, support multiple activities and cannot be attributed directly to a single function.

As companies evaluate the alternatives, the discussion may gradually move beyond the face of the financial statements. Questions on data availability, allocation methodologies, system capabilities, and governance processes may become increasingly relevant, particularly where significant categories of expenditure support multiple activities. The assessment is ultimately not about selecting a preferred presentation format. It is about determining which presentation best explains of the entity's performance.

Implementation Considerations

Information availability may differ significantly between companies. While some organizations already maintain cost centers, allocation methodologies and management reports that support a functional view of performance, others may need to consider whether existing reporting structures provide the required information consistently and supportably.

Where a functional or mixed presentation is being evaluated, additional consideration may be needed for cost centers, allocation methodologies, reporting hierarchies, and the availability of underlying data. The discussion may become particularly relevant where significant categories of expenditure support multiple functions simultaneously.

Additional complexity may arise from the requirement to disclose specified expenses by nature even where expenses are presented by function. Consequently, companies may need to retain visibility over both functional and nature-based information within their reporting processes.

Looking Ahead

Indian financial reporting has historically benefited from a relatively consistent approach to presenting operating expenses. Ind AS 118 may gradually shift the discussion from reporting convention towards management judgment.

Some sectors may continue to favor nature-based presentation, while others may conclude that a functional presentation provides greater insight into business performance. Industry practices are also likely to evolve over time as companies evaluate investor expectations, peer reporting and implementation practicality.

Given the requirement for comparative information and the possibility of system and process changes, early assessment may provide meaningful benefits even before the standard becomes effective.

Concluding Thoughts

Gross profit may become more visible in Indian financial reporting under Ind AS 118, but its appearance is neither automatic nor mandatory.

Ind AS 118 introduces a broader assessment regarding how operating expenses should be presented. For many entities, the outcome may remain a nature-based presentation. Others may conclude that a functional or mixed presentation provides more useful information about the drivers of profitability. The conclusion reached may differ across industries, business models and operating environments.

In that sense, the significance of Ind AS 118 extends beyond the possible appearance of a gross profit subtotal. It requires an active evaluation of whether long-established reporting practices continue to provide the most useful information to users of financial statements.



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