

Query No. 2

Subject: Classification of Lease Receivables.¹

A. Facts of the Case

1. A Corporation (hereinafter referred to as ‘the Corporation’ or ‘the Company’) is a Public Sector Undertaking (PSU) under the administrative control of the Ministry of Railways, with 86.36% of equity being held by the Government of India (GoI). The Corporation was set up as the dedicated financing arm of the Indian Railways for mobilising funds from domestic as well as overseas capital markets. It is also registered as Systemically Important Non-Deposit taking Non-Banking Financial Company (NBFC – ND-SI) and Infrastructure Finance Company (NBFC- IFC) with the Reserve Bank of India (RBI). In more than 30 years of its existence, the Corporation has played a significant role in supporting the expansion of the Indian Railways and related entities by financing a significant proportion of its annual plan outlay.

2. The primary objective of the Corporation is to meet the predominant portion of ‘Extra Budgetary Resources (EBR)’ requirement of the Indian Railways through market borrowings at the most competitive rates and terms. The Company’s principal business therefore is to borrow funds from the financial markets for acquisition/creation of assets which are then leased out to the Indian Railways under finance lease arrangements.

3. The querist has stated that the Company has adopted Companies (Indian Accounting Standards) Rules, 2015 (Ind AS) with the date of transition as 1st April 2017. All its leases, as a lessor, in the past have been classified as finance leases in accordance with the Ind AS 17 / Ind AS 116, ‘Leases’.

4. The financial statements of the Corporation are prepared in accordance with Division III to Schedule III of the Companies Act, 2013. The Corporation in accordance with Ind AS 17/Ind AS 116 read with Division III to Schedule III to the Companies Act, 2013 has been presenting ‘Lease Receivables’ from Ministry of Railways as part of ‘Receivables’ on the face of its Balance Sheet since inception of Ind AS from the date of Ind AS transition of 1st April 2017, the first Ind AS financial statements being for the year ended 31st March 2019.

5. Being a PSU, the Corporation is also subject to regular annual audit by the Comptroller and Auditor General of India (CAG). Since the adoption of Ind AS from financial year 2018-19, CAG has not made any observation on the aforesaid presentation. However, for the financial year 2021–22, it is observed that in accordance with Division III of Schedule III to the Companies Act, 2013, the said lease receivables should be presented as ‘Loans’ rather than ‘Receivables’. The Company submitted that its presentation of lease receivables as part of lease receivables is in accordance with Ind AS read with Division III of Schedule III of the Companies Act, 2013. CAG is not in agreement with the Company’s submission.

6. *Company’s submission in detail:*

According to the querist, the Company has rightly presented ‘Lease Receivables’ as part of ‘Receivables’. While it is understood, as observed by CAG also, that Division III of Schedule

¹ Opinion finalised by the Committee on 22.3.2023.

III to the Companies Act, 2013 requires 'Leasing' to be presented as part of 'Loans' on the 'Assets' side of the Balance Sheet, however, the Company relies on the following literature:

Conceptual Framework for Financial Reporting under Indian Accounting Standards issued by the Institute of Chartered Accountants of India:

The relevant paragraphs are as under:

- “1.2 The objective of general purpose financial reporting is to provide financial information about the reporting entity that is useful to existing and potential investors, lenders and other creditors in making decisions relating to providing resources to the entity. ...”
- “2.4 If financial information is to be useful, it must be relevant and faithfully represent what it purports to represent. The usefulness of financial information is enhanced if it is comparable, verifiable, timely and understandable.”
- “2.11 Information is material if omitting, misstating or obscuring it could reasonably be expected to influence decisions that the primary users of general purpose financial reports (see paragraph 1.5) make on the basis of those reports, which provide financial information about a specific reporting entity. In other words, materiality is an entity-specific aspect of relevance based on the nature or magnitude, or both, of the items to which the information relates in the context of an individual entity's financial report. ...”
- “7.1 A reporting entity communicates information about its assets, liabilities, equity, income and expenses by presenting and disclosing information in its financial statements.
- 7.2 Effective communication of information in financial statements makes that information more relevant and contributes to a faithful representation of an entity's assets, liabilities, equity, income and expenses. It also enhances the understandability and comparability of information in financial statements. Effective communication of information in financial statements requires:
 - (a) focusing on presentation and disclosure objectives and principles rather than focusing on rules;
 - (b) classifying information in a manner that groups similar items and separates dissimilar items; and
 - (c) aggregating information in such a way that it is not obscured either by unnecessary detail or by excessive aggregation.”
- “7.6 Effective communication in financial statements is also supported by considering the following principles:
 - (a) entity-specific information is more useful than standardised descriptions, sometimes referred to as 'boilerplate'; and
 - (b) duplication of information in different parts of the financial statements is usually unnecessary and can make financial statements less understandable.
- 7.7 Classification is the sorting of assets, liabilities, equity, income or expenses on the basis of shared characteristics for presentation and disclosure purposes.

Such characteristics include—but are not limited to—the nature of the item, its role (or function) within the business activities conducted by the entity, and how it is measured.

- 7.8 Classifying dissimilar assets, liabilities, equity, income or expenses together can obscure relevant information, reduce understandability and comparability and may not provide a faithful representation of what it purports to represent.

Classification of assets and liabilities

- 7.9 Classification is applied to the unit of account selected for an asset or liability (see paragraphs 4.48–4.55). However, it may sometimes be appropriate to separate an asset or liability into components that have different characteristics and to classify those components separately. That would be appropriate when classifying those components separately would enhance the usefulness of the resulting financial information. ...”

Ind AS 8, Accounting Policies, Changes in Accounting Estimates and Errors

The relevant paragraphs are as under:

- “7 When an Ind AS specifically applies to a transaction, other event or condition, the accounting policy or policies applied to that item shall be determined by applying the Ind AS.”**
- “10 In the absence of an Ind AS that specifically applies to a transaction, other event or condition, management shall use its judgement in developing and applying an accounting policy that results in information that is:**
- (a) relevant to the economic decision-making needs of users; and**
 - (b) reliable, in that the financial statements:**
 - (i) represent faithfully the financial position, financial performance and cash flows of the entity;**
 - (ii) reflect the economic substance of transactions, other events and conditions, and not merely the legal form;**
 - (iii) are neutral, ie free from bias;**
 - (iv) are prudent; and**
 - (v) are complete in all material respects.**
- 11 In making the judgement described in paragraph 10, management shall refer to, and consider the applicability of, the following sources in descending order:**
- (a) the requirements in Ind ASs dealing with similar and related issues; and**
 - (b) the definitions, recognition criteria and measurement concepts for assets, liabilities, income and expenses in the *Conceptual Framework for Financial Reporting under Indian Accounting Standards (Conceptual Framework)* issued by the Institute of Chartered Accountants of India.”**

The relevant paragraphs are as under:

“7 ...

Material:

Information is material if omitting, misstating or obscuring it could reasonably be expected to influence decisions that the primary users of general purpose financial statements make on the basis of those financial statements, which provide financial information about a specific reporting entity.

Materiality depends on the nature or magnitude of information, or both. An entity assesses whether information, either individually or in combination with other information, is material in the context of its financial statements taken as a whole. ...

Assessing whether information could reasonably be expected to influence decisions made by the primary users of a specific reporting entity's general purpose financial statements requires an entity to consider the characteristics of those users while also considering the entity's own circumstances.”

“15 Financial statements shall present a true and fair view of the financial position, financial performance and cash flows of an entity. Presentation of true and fair view requires the faithful representation of the effects of transactions, other events and conditions in accordance with the definitions and recognition criteria for assets, liabilities, income and expenses set out in the *Conceptual Framework for Financial Reporting under Indian Accounting Standards (Conceptual Framework)* issued by the Institute of Chartered Accountants of India (ICAI). The application of Ind ASs, with additional disclosures when necessary, is presumed to result in financial statements that present a true and fair view.”

“29 An entity shall present separately each material class of similar items. An entity shall present separately items of a dissimilar nature or function unless they are immaterial except when required by law.

30 Financial statements result from processing large numbers of transactions or other events that are aggregated into classes according to their nature or function. The final stage in the process of aggregation and classification is the presentation of condensed and classified data, which form line items in the financial statements. If a line item is not individually material, it is aggregated with other items either in those statements or in the notes. An item that is not sufficiently material to warrant separate presentation in those statements may warrant separate presentation in the notes.

30A When applying this and other Ind ASs an entity shall decide, taking into consideration all relevant facts and circumstances, how it aggregates information in the financial statements, which include the notes. An entity shall not reduce the understandability of its financial statements by obscuring material information with immaterial information or by aggregating material items that have different natures or functions.”

“45 An entity shall retain the presentation and classification of items in the financial statements from one period to the next ...”

“54 The balance sheet shall include line items that present the following amounts:

...

(h) trade and other receivables;

...

55 An entity shall present additional line items (including by disaggregating the line items listed in paragraph 54), headings and subtotals in the balance sheet when such presentation is relevant to an understanding of the entity’s financial position.”

Ind AS 116, ‘Leases’

The relevant paragraphs are as under:

“67 At the commencement date, a lessor shall recognise assets held under a finance lease in its balance sheet and present them as a receivable at an amount equal to the *net investment in the lease*.”

Guidance Note on Division III - Schedule III to the Companies Act, 2013 for NBFC that is required to comply with Ind AS

“4.1 Every Non-Banking Financial company as defined in the Companies (Indian Accounting Standards) (Amendment) Rules, 2016 to which Indian Accounting Standards apply, shall prepare its financial statements in accordance with this Schedule or with such modification as may be required under certain circumstances.”

General instructions for preparation of financial statements of a non-banking financial company (NBFC) that is required to comply with Indian Accounting Standards (Ind AS)

“...

2. Where compliance with the requirements of relevant Act, Regulations, Guidelines or Circulars issued by the relevant regulator from time to time including Indian Accounting Standards (Ind AS) (except the option of presenting assets and liabilities in accordance with current, noncurrent classification as provided by relevant Ind AS) as applicable to the NBFCs require any change in treatment or disclosure including addition, amendment, substitution or deletion in the head or sub-head or any changes inter se, in the financial statements or statements forming part thereof, the same shall be made and the requirements under this Schedule shall stand modified accordingly.

...

7. Financial Statements shall disclose all material items, i.e., the items if they could, individually or collectively, influence the economic decisions that users make on the basis of the financial statements. Materiality depends on the size or nature of the item or a combination of both, to be judged in the particular circumstances.

...

Note: *This Schedule sets out the minimum requirements for disclosure on the face of the Financial Statements, i.e., Balance Sheet, Statement of Changes in Equity for the period, the Statement of Profit and Loss for the period (The term ‘Statement of Profit and Loss’ has the same meaning as ‘Profit and Loss Account’) and Notes. Cash flow statement shall be prepared, where applicable, in accordance with the requirements of the relevant Indian Accounting Standard.*

Line items, sub-line items and sub-totals shall be presented as an addition or substitution on the face of the Financial Statements when such presentation is relevant to an understanding of the NBFC’s financial position or performance or to cater to categories of NBFC’s as prescribed by the relevant regulator or sector-specific disclosure requirements or when required for compliance with the amendments to the relevant statutes or under the Indian Accounting Standards.”

To summarise, the gist of the aforesaid literature is as under:

- Financial statements should faithfully present the information
- Financial statements should be relevant, reliable and consistent
- ‘Form’ or ‘boiler plate’ presentation should be avoided. Schedule III is a ‘form’ or ‘boiler plate’
- Materiality is one of the key factors in arriving at a judgement
- Information should not be obscured
- Nature of entity’s business is also important for presentation
- Ind AS 1 (generally) and Ind AS 116 (specifically paragraph 67) require lease receivables to be presented as part of receivables
- Schedule III (see instruction 2) permits departure from requirements from Schedule III if Ind AS requires such departure

(Emphasis supplied by the querist.)

7. It may also be noted that the Corporation is primarily a leasing company. It is not a loan company (which is a very small portfolio). If the lease receivables are presented as part of ‘Loans’, in that case it would prima facie, appear to a general investor that the Company is a loan company. The material information is obscured. Presenting lease receivables on the face of the Balance Sheet immediately and at the first glance itself, establishes the Company as a leasing company. Therefore, in the firm opinion and judgement of the Company, the presentation of ‘Lease Receivables’ as part of ‘Receivables’ on the face of its Balance Sheet complies, in all respects, the requirements of the aforesaid literature, reproduced in detail.

B. Query

8. The Expert Advisory Committee of the Institute of Chartered Accountants of India is requested to give its opinion as to:

- (i) whether the presentation of ‘Lease Receivables’ as part of ‘Receivables’ on the face of the Company’s Balance Sheet is in accordance with applicable Ind ASs read with Division III of Schedule III to the Companies Act, 2013.

- (ii) If not, then what is the correct presentation?

C. Points considered by the Committee

9. The Committee notes that the basic issue raised by the querist relates to the presentation of 'Lease Receivables' in the financial statements. The Committee has, therefore, examined only this issue and has not examined any other issue that may arise from the Facts of the Case, such as, recognition and measurement of lease receivables, impairment of lease receivables, classification of lease as finance lease, detailed aspects of accounting under Ind AS 116, accounting as per Ind AS 17, accounting treatment on transition to Ind AS 116 from Ind AS 17, classification of lease receivables as current/non-current, accounting for prior period errors (if any) under Ind AS 8, 'Accounting Policies, Changes in Accounting Estimates and Errors', etc. Further, the Standards referred to in the opinion are Indian Accounting Standards, notified under the Companies (Indian Accounting Standards) Rules, 2015.

The Committee also notes from the Facts of the Case that the Company is a Non-banking Financial Company and therefore, the Ind ASs are applicable to the Company from the financial year 2018-19 and the financial statements shall be presented in accordance with Division III of Schedule III to the Companies Act, 2013.

10. With regard to the presentation of the 'Lease Receivables' the Committee notes that Division III of Schedule III to the Companies Act, 2013 requires the head 'Loans' under the head 'Financial Asset' on the 'Assets' side of the balance sheet to be sub-classified as under:

Loans	
(A)	
(i) Bills Purchased and Bills Discounted	
(ii) Loans repayable on Demand	
(iii) Term Loans	
(iv) Leasing	
(v) Factoring	
(vi) Others (to be specified)	
Total (A)- Gross	

Further, the Committee notes the following paragraphs of the 'Guidance Note on Division III - Schedule III to the Companies Act, 2013 for NBFC that is required to comply with Ind AS (Revised January, 2022 Edition)':

"8.1 Assets

On the face of the Balance Sheet, Division III to Schedule III requires the following items to be presented under financial assets and non-financial assets:

Financial assets

- (a) Cash and cash equivalents
- (b) Bank Balance other than included in (a) above
- (c) Derivative financial instruments

- (d) Receivables
 - (I) Trade Receivables
 - (II) Other Receivables
- (e) Loans
- (f) Investments
- (g) Other Financial assets (to be specified)
- ...

“Financial Assets

...

8.1.5 Loans

An NBFC shall disclose the following in the Notes under the head ‘Loans’:

- (i) Bills purchased and bills discounted
- (ii) Loans repayable on demand
- (iii) Term Loans
- (iv) Leasing
- (v) Factoring
- (vi) Others (to be specified, example of ‘Others’ could be Intercompany Deposits, Staff loans, loans to related parties, etc.)

...

For finance lease receivables, an entity shall apply the presentation and disclosure requirements under Ind AS 116 in addition to the requirements of Division III to Schedule III. The disclosure requirements of Ind AS 107 would also apply to such receivables.

...”

“8.1.12.8 For assets given on lease, an entity shall apply the presentation and disclosure requirements under Ind AS 116 in addition to the requirements of Ind AS Schedule III.”

From the above, the Committee notes that Division III of Schedule III to the Companies Act, 2013 specifically requires to present financial assets relating to ‘Leasing’, viz., lease receivables under ‘Loans’ under the head ‘Financial Assets’ in the Balance Sheet. Further, the Guidance Note states that presentation and disclosure requirements under Ind AS 116, Division III to Schedule III to the Companies Act, 2013 and disclosure requirements of Ind AS 107 for finance lease receivables should also be applied by the entity.

In this regard, the Committee notes that apart from the above requirements, Schedule III and Ind AS 107 do not specify any other requirements with regard to presentation of lease receivables. As regard to the requirements under paragraph 67 of Ind AS 116, the Committee is of the view that the same only requires to present net investment in lease as a receivable in the balance sheet. Therefore, the disclosure of lease receivables under ‘Loans’ as per the requirements of Schedule III cannot be considered in contradiction to or as departure from the requirements of Ind AS. Accordingly, the Committee is of the view that the Company should

present the lease receivables under 'Loans' as per the requirements of Schedule III to the Companies Act, 2013.

As far as nature of business of the Company is concerned, the Committee notes from the Facts of the Case that the Company's principal business is to borrow funds from the financial markets for acquisition /creation of assets which are then leased out to the Indian Railways under finance lease arrangements. Thus, in substance, the Company is providing finance to Indian Railways for acquisition/construction of asset. Therefore, considering the nature of business of the Company also, presentation of 'Lease Receivables' under 'Loans' under the head 'Financial Assets' appears to be appropriate. Further, other disclosure requirements, such as, maturity analysis of lease receivables as per Ind AS 116, etc. should also be complied with.

D. Opinion

11. On the basis of the above, the Committee is of the following opinion on the issues raised by the querist in paragraph 8 above:

- (i) The presentation of 'Lease Receivables' as part of 'Receivables' on the face of the Company's Balance Sheet is not in accordance with applicable Ind ASs read with Division III of Schedule III to the Companies Act, 2013.
- (ii) 'Lease Receivables' should be presented under 'Loans' under the head 'Financial Assets' in the Balance Sheet, as discussed in paragraph 10 above. Further, other disclosure requirements, such as maturity analysis of lease receivables as per Ind AS 116, etc. should also be complied with.
