Query No. 5

Subject: Accounting treatment of unamortised portion of grant from government/ government agencies under Ind AS framework.[1]

A. Facts of the Case

1. A company (hereinafter referred to as 'the Company'), a joint venture company with equal equity participation from the Government of India (GoI) and Government of National Capital Territory of Delhi (GNCTD), has been entrusted with the responsibility of construction and operation of the rail-based Mass Rapid Transit System (MRTS) for Delhi/NCR areas.

2. The grants received by the Company, all being in the nature of capital grant for long-term capital assets, can be categorised into two categories:

> *Grant I:* Grants received directly from the shareholders of the Company, i.e. GoI and GNCTD, as part of funding pattern/financing plan for execution of metro project, along with other modes of financing such as, equity, subordinate debt, JICA loan etc.
>
> *Grant II:* Grants received from other government agencies like Delhi Development Authority (DDA), Haryana Urban Development Authority (HUDA), Ghaziabad Development Authority (GDA), Government of Haryana (GoH), Government of Uttar Pradesh (GoUP), as part of funding pattern/financing plan for execution of metro project along with other modes of financing such as, equity, subordinate debt, JICA loan etc.

3. The querist has stated that since the grants are sanctioned by government/government agencies for the purpose of construction of metro projects, i.e. long-term capital assets, the same are in the nature of grant related to assets within the meaning of Indian Accounting Standard (Ind AS) 20, 'Accounting for Government Grants and Disclosure of Government Assistance'.

Accounting treatment being followed by the Company

4. Paragraphs 24 to 28 of Ind AS 20, 'Accounting for Government Grants and Disclosure of Government Assistance' provide two acceptable alternatives for presentation of grants related to assets in the balance sheet i.e. either by setting up the grant as deferred income or by deducting the grant in arriving at the carrying amount of the asset.

5. The Company has opted for the first alternative since beginning to date as per provisions of paragraph 26, wherein the Company recognises the grant as deferred income that is recognised in profit or loss on a systematic basis over the useful life of the asset.

6. The unamortised portion of grants being received by the Company in the nature of 'Grant-I' which are received directly from the shareholders in the nature of shareholders' contribution, are presented under the head 'Other Equity' on utilisation in construction of metro project.

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[1] Opinion finalised by the Committee on 24.4.2024.

7. The unamortised portion of grants in nature of 'Grant-II' which are received from other government/ government agencies, but are received as a part of the funding pattern/financing plan issued by shareholder(s), are also presented under the head 'Other Equity' on utilisation in construction of metro projects.

8. Accordingly, as per the querist, in both the scenarios mentioned at paragraphs 6 and 7 above, after capitalisation of related assets, unamortised portion of grant on such assets is recognised in profit or loss annually under the head 'Other Income' on pro-rata basis of depreciation calculated on the granted assets in line with the provisions of paragraph 26 of Ind AS 20.

Provisional Comment issued by the Comptroller and Auditor General of India (C&AG) during Supplementary Audit

9. During supplementary audit of financial statements of the Company for the financial year (F.Y.) 2022-23, the office of Comptroller & Auditor General of India (C&AG) issued a Provisional Comment which is reproduced below:

> "Balance Sheet
>
> Equity and Liabilities
>
> Equity – Other Equity – Deferred Income – Rs. 9,72,193.14 lakh (Note 14)
>
> The above amount represents value of unamortised portion of Government Grants received for various phases of the Company's Metro projects. As these Grants are not attributable to the shareholders, the same should not have been included under Other Equity.
>
> Inclusion of the same under Other Equity has resulted in overstatement of the same and understatement of Non-Current Liabilities by Rs. 9,72,193.14 lakh."

10. The reply given by the Company is as below:

The Company has given accounting treatment of grant in line with the provisions of Ind AS 20, which are explained below:

Paragraphs 24 to 27 of Ind AS 20, 'Accounting for Government Grants and Disclosure of Government Assistance' deals with presentation of grants related to assets, which are reproduced below:

> **"24 Government grants related to assets, including non-monetary grants at fair value, shall be presented in the balance sheet *either by setting up the grant as deferred income or by deducting the grant in arriving at the carrying amount of the asset.***
>
> *25* *Two methods* of presentation in financial statements of grants or the appropriate portions of grants related to assets are regarded as *acceptable alternatives.*
>
> 26 One method recognises the grant as deferred income that is recognised in profit or loss on a systematic basis over the useful life of the asset.

27 The other method deducts the grant in calculating the carrying amount of the asset. The grant is recognised in profit or loss over the life of a depreciable asset as a reduced depreciation expense."

(Emphasis supplied by the querist.)

11. The Company has opted for the first alternative wherein government grants are being reflected as deferred income that is being recognised in profit or loss on a systematic basis over the useful life of the asset.

12. Presentation of deferred income under 'Non-Current Liabilities' as suggested by C&AG would not be correct, since deferred income is not in the nature of liability. Liability has been defined under paragraphs 4.26 and 4.27 of 'Conceptual Framework for Financial Reporting under Indian Accounting Standards (Ind AS)' as given below:

"4.26 A liability is a *present obligation* of the entity to transfer an economic resource as a result of past events.

4.27 *For a liability to exist, three criteria must all be satisfied:*

(a) the entity has an obligation;

(b) the *obligation is to transfer an economic resource;* and

(c) the obligation is a present obligation that exists as a result of past events".

(Emphasis supplied by the querist.)

13. In case of the Company, as per sanction orders of various phases of MRTS projects, grants are received as part of funding pattern as one of the main sources of promoter contribution for execution of project and utilised only for the purpose they are sanctioned.

14. Grants are usually sanctioned for a particular project/corridor and capitalised to the related assets. An amount equivalent to depreciation on related assets is recognised in profit or loss in accordance with paragraph 26 of Ind AS 20 and unamortised portion is shown as 'Deferred Income' under the head 'Other Equity'.

15. Depiction of unamortised portion of grant under 'Non-Current Liabilities' would indicate that the unamortised portion of grant is returnable to the grantor. Whereas, in fact, the residual unamortised portion of grant, which has been already utilised for construction of assets, is attributable to the promotor's funds and not required to be returned back at any point of time. Therefore, the presentation made by the Company for disclosure of unamortised portion of grants, which have already been utilised, under the head 'Other Equity' is correct.

Hence, the Company is correctly accounting for and disclosing the grant in line with the laid down procedure under Ind AS 20 and also in the absence of any specific provision in Schedule III of the Companies Act, 2013 for accounting treatment of grants.

As explained above, since the inclusion of grants under the head 'Other Equity' is in order, there is no overstatement of 'Other Equity' and no understatement of 'Non-Current Liabilities'.

This practice is consistently followed by the Company in earlier years also.

16. It is assured that the complete issue relating to accounting treatment of grant under other equity will be referred to the Expert Advisory Committee of the Institute of Chartered Accountants of India (ICAI) for its expert opinion.

In view of above explanations, it was requested by the Company to the C&AG to drop the Provisional Comment.

17. The querist has stated that there is no specific provision in Schedule III to the Companies Act, 2013 for accounting treatment and disclosure of deferred grants. The grants received by the Company are mainly for execution of metro projects. The unutilised portion of grant is accounted for as liability in the books. On utilisation of the grant funds, the same is accounted for as deferred grant under the head 'Other Equity' till its amortisation. Hence, the unamortised portion of grant represents the *funds which have already been utilised in execution of metro projects.* Therefore, the question of refund of utilised funds does not arise. (Emphasis supplied by the querist.)

B. Query

18. In view of the above, opinion of the Expert Advisory Committee is sought on the following issues:

(i) Whether the accounting treatment of deferred grant being made by the Company as per paragraphs 6 to 8 is correct.

(ii) If not, what should be the correct accounting treatment?

C. Points considered by the Committee

19. The Committee notes that the basic issue raised in the query relates to accounting treatment of funds received by the Company from government/government agencies. The Committee has, therefore, considered only this issue and has not examined any other issue that may arise from the Facts of the Case, such as accounting for funds received from other financing modes such as equity share capital, subordinate debt, JICA loan etc., accounting for funds received as reimbursement of cost of metro tickets for spectators and volunteers in commonwealth games 2010 (as observed from one of the communication shared by the querist with the Committee), accounting for various expenses incurred by the Company on the metro project, accounting for assets acquired for the project from the funds received, presentation as per Schedule III to the Companies Act, 2013, etc. Further, the opinion hereinafter has been expressed in the context of Indian Accounting Standards notified under the Companies (Indian Accounting Standards) Rules, 2015, as amended from time to time and is purely from accounting perspective and not from the perspective of legal interpretation of grant sanction documents, etc.

20. At the outset, the Committee notes that both GoI and GNCTD are owners of the Company and the funds have been contributed by them in various forms viz. equity, subordinate debt, loans etc. Further, in case of Grant I, though it is being argued by the querist that the funds are received as part of funding pattern as one of the main sources of promoter contribution for execution of project, these are being considered as government grant related

to assets. Further, the auditor is also considering them as government grant. Similarly, in case of Grant II, it is being argued that the funds are received from other government/ government agencies as a part of the funding pattern/financing plan issued by shareholder(s); however, these are also being accounted for as government grants related to asset. In this regard, the Committee wishes to point out that as per paragraph 2(c) of Ind AS 20, the Standard does not deal with government participation in the ownership of the entity. Therefore, if the Government provides funds to an entity, acting in its capacity as owner of the entity, the same cannot be accounted for as government grants as per Ind AS 20. Accordingly, it is important to understand the nature of these two types of funds/grants being received from the government/government agencies.

21. In this regard, the Committee notes the following from various communications submitted by the querist in relation to release of grant:

Letter dated 25th July, 2019 of Ministry of Housing and Urban Affairs, GoI for release of grant to the Company towards extension of Metro (presumably in case of Grant I):

> "I am directed to refer to the Company's letter No…. to convey the sanction of the President to the release of Grant of Rs. 120,00,00,000/- (Rupees One Hundred Twenty crore only) towards extension of State Metro….
>
> 2. The amount is sanctioned subject to the following terms and conditions:-
>
> i) …
>
> ii) This amount shall be utilized by the Company for the purpose for which it has been sanctioned and cannot be diverted for any purpose other than that for which it is now released.
>
> iii) In case the Company is unable to utilize the grant for the purpose for which it is sanctioned, the unutilized portion shall be refunded to Government forthwith.
>
> iv) The Company will provide Utilization Certificate in form GFR 19A that the Grant has been utilized for the purpose for which it has been sanctioned within twelve months of the close of this financial year.
>
> 3. The expenditure involved will be debited to the Major Head 2217 – Urban Development, 80 – General (Sub Major Head), 80.001 – Direction and Administration (Minor Head), 05 – Grants to 'the Company' (Sub-Head), 05.00.35 – Grants-in-aid for creation of capital assets against Demand No. 56 for the year 2019-20."
>
> "7. This sanction has been entered at Sl. No. 34 of the 'grant-in-aid' register in respect of the Company for the year 2019-20."

Letter dated 15th March 2012 of Delhi Development Authority for release of funds (presumably in case of Grant II)

> "III. … the amount spent should be furnished to DDA as soon as possible after the close of the financial year.
>
> IV. The Company should maintain a report of the permanent and semi-permanent assets acquired wholly or mainly out of the DDA funds… Such assets should not be disposed of, encumbered or utilized for purposes other than those for which the

amount was given without the prior sanction of DDA. Should the Company cease to exist at any time, such assets properties shall revert to the DDA.

V. The grants to the Company shall be governed by the provisions of GFRs 2005."

The Committee notes from the above letters related to release of funds that the funds have been received with a condition to use them specifically for the construction or acquisition of metro project or some permanent/semi-permanent assets and cannot be diverted for any purpose other than that for which these are released. It is also noted that in one of the above letters it is also stipulated that in case the Company is unable to utilize the grant for the purpose for which it is sanctioned, the unutilized portion shall be refunded to Government forthwith. Thus, these funds are transferred with conditions/restrictions, fulfilment of which is mandatory for retaining the funds. It is also evident from the above communication that the funds have been granted under the head 'Grants-in-aid' or are governed by the provisions of General Financial Rules (GFRs) applicable to grants. Thus, the Committee is of the view that the funds released by the Government/government agencies through above-mentioned letters are in the nature of government grants. In this context, the Committee notes the definition of 'Government grants' as provided in Ind AS 20, 'Accounting for Government Grants and Disclosure of Government Assistance' as follows:

"*Government grants* are assistance by government in the form of transfers of resources to an entity in return for past or future compliance with certain conditions relating to the operating activities of the entity. …"

22. Further, with regard to the nature of such grants and accounting treatment thereof, the Committee notes the following requirements from Ind AS 20:

***"Grants related to assets* are government grants whose primary condition is that an entity qualifying for them should purchase, construct or otherwise acquire long-term assets. Subsidiary conditions may also be attached restricting the type or location of the assets or the periods during which they are to be acquired or held."**

"12 Government grants shall be recognised in profit or loss on a systematic basis over the periods in which the entity recognises as expenses the related costs for which the grants are intended to compensate."

"Presentation of grants related to assets

24 Government grants related to assets, including non-monetary grants at fair value, shall be presented in the balance sheet either by setting up the grant as deferred income or by deducting the grant in arriving at the carrying amount of the asset.

25 Two methods of presentation in financial statements of grants or the appropriate portions of grants related to assets are regarded as acceptable alternatives.

26 One method recognises the grant as deferred income that is recognised in profit or loss on a systematic basis over the useful life of the asset.

27 The other method deducts the grant in calculating the carrying amount of the asset. The grant is recognised in profit or loss over the life of a depreciable

asset as a reduced depreciation expense.”

From the above, the Committee notes that grants that are related to assets are those whose primary condition is that an entity qualifying for them should purchase, construct or otherwise acquire long-term assets. Since, in the extant case, the grant has been received for construction/acquisition of metro project/assets, the same is grant related to assets. The Committee further notes that as per the requirements of Ind AS 20, there are two methods of presentation of grants related to assets. As per one method of presentation under paragraph 26 of Ind AS 20, which has been adopted by the Company in the extant case, such grants may be presented in the balance sheet by setting up the grant as deferred income, which is recognised as income on a systematic basis over the useful life of the asset.

In this context, the Committee notes from the Facts of the Case that the unutilised portion of grant is accounted for as liability in the books. On utilisation of the grant funds, the same is accounted for as ‘deferred grant’ under the head ‘Other Equity’ till its amortisation and the deferred grant is being amortised and transferred to income over the life of the relevant assets in proportion to depreciation on those assets. In this regard, the Committee wishes to point out that as per the requirements of Ind AS 20, grants are recognised in profit or loss on a systematic basis over the periods in which the entity recognises as expenses the related costs for which the grants are intended to compensate. In case of grants related to assets, the expenses which are recognised in the profit or loss are depreciation expenses (on the relevant depreciable assets), which are considered as the related costs for the purpose of recognition of grant over the period. Thus, irrespective of the utilisation of grant in the construction or acquisition of assets, till these assets are not depreciated, the grants yet to be amortised are presented as ‘deferred income’ under the head ‘liability’ (and not as ‘other equity’) in the Balance Sheet as it represents the portion of grants for which the related conditions of the grant are yet to be fulfilled and may have to be refunded. Therefore, the unamortised portion represents unfulfilled obligations on the part of the entity receiving the grant. In this context, the Committee notes that as per the Conceptual Framework for Financial Reporting under Indian Accounting Standards (Ind AS), issued by the ICAI, “‘Equity’ is the residual interest in the asset of the entity after deducting all its liabilities”, which is not transferred to or recognised subsequently in the profit or loss; whereas liability represents a present obligation of the entity, the reduction of which may give rise to recognition of income in view of the definition of ‘Income’ in the aforesaid Conceptual Framework which includes ‘decreases in liabilities’ as income. Since the unamortised grant or deferred income does not represent any residual interest in the net assets; rather represents unfulfilled obligations as afore-mentioned, these should be presented as a ‘liability’ and not as ‘equity’ in the financial statements. It is only on commencement of depreciation on related asset, the amortisation or recognition of deferred income as income will commence.

Therefore, grants received in the extant case should be accounted for as deferred income under an appropriate head of ‘Liabilities’ and the same should be amortised or recognised as income in the Statement of Profit and Loss over the useful life of the asset in proportion to the depreciation.

D. Opinion

23. On the basis of the above, the Committee is of the following opinion on the issues raised in paragraph 18 above:

(i) and (ii) Since the grants received from GoI/GNCTD are grants related to assets, the same should be presented in the balance sheet by setting up the grant as 'deferred income' under the head 'liability' (if an entity selects that option under paragraph 26 of Ind AS 20) and not as 'other equity' in the Balance Sheet and the same should be recognised as income on a systematic basis over the useful life of the asset, as discussed in paragraphs 21 and 22 above. Therefore, the accounting treatment of deferred income being presented as 'Other Equity' by the Company is not correct.

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