

Query No. 18

Subject: Accounting treatment of capital work-in-progress (CWIP) held on behalf of Government of India (GoI) and funds received from the GoI.¹

A. Facts of the Case

1. A company (hereinafter referred to as the 'company') was incorporated on 18th July, 2014 under the Companies Act, 2013 as a public sector undertaking (PSU) fully owned by the Government of India (GoI) under the administrative Ministry of Road Transport & Highways (MoRTH) with authorised capital of Rs.10 crore. It has started functioning in September 2014 with the objective to develop national highways (NH) and other infrastructure at fast pace in the North East and strategic areas of the country sharing international borders. The company has been entrusted the task of developing and improving road connectivity in length of 10,000 km including the international trade corridor in the North Eastern region of India on behalf of the GoI. The company has formulated a vision to become an instrument for creation and management of infrastructure of the highest standard while contributing significantly towards nation building. Being a professional company, its mission is to design and develop infrastructure projects in a time bound, most efficient and transparent manner with maximum benefits to all the stakeholders. The company has adopted a business model that relies on outsourcing of a number of activities including design, construction and supervision of national highways, rather than undertaking all such activities through its own employees. This has thus helped the company in maintaining a lean organisational structure to facilitate faster operational decision-making. Within a short period, the company has set up its corporate office and twelve offices in Assam, Arunachal Pradesh, Jammu and Kashmir, Manipur, Nagaland, Tripura, Uttarakhand, Mizoram, Meghalaya, Sikkim, A & N Islands and Nepal for monitoring and supervising the NH projects entrusted to it.

2. The querist has stated that infrastructure is an important component in the development of any economy, more so, in case of India because of its demographic profile. Infrastructure projects have large capital requirements and also long gestation periods. A typical highways project has a construction period of two-three years, during which it does not generate any cash flows.

3. The querist has further stated that the Government of India (GoI) through Notification entrusted the company the job of construction and development of the highways and other infrastructure projects. The ownership of land acquired for the same remains vest with the GoI. Presently, the company is executing the national highways and other infrastructure projects on behalf of the Government of India (GoI) out of the funds provided by MoRTH and entitled to receive agency commission as per the defined rate on the expenditure incurred. The national highways stretches entrusted to the company are at different stages of planning and development and are likely to be completed in next couple of years.

4. According to the querist, since the company has been incorporated only in mid 2014, it started its activities of the project effectively from the financial year 2015-16 as per the financial model adopted. The financial model includes that all the funds for the execution of the roads and infrastructure projects are being financed by the Government of India on the basis of yearly budget allocations and released to the company on yearly basis. The company, out of the funds received from the GoI for the project execution, regularly

¹ Opinion finalised by the Committee on 10.11.2017 and 11.11.2017.

spends the amount and has been generating asset as defined by the MoRTH. Accordingly, upto 31.03.2016, Rs. 2819 crore have been released to the company by the GoI and capital work-in-progress (CWIP) of Rs. 1579 crore has been generated.

5. Therefore, the major activities of the company are to build the roads and infrastructure on behalf of the GoI. Other than that, the company has to incur the establishment expenditure towards payment of salary, rent and other establishment expenses, which are nominal in nature, and are being paid out of the agency commission being received against project executions and some interest income.

6. The querist has stated that considering the above financial model and activities of the company, it may be appreciated that a prudent and accepted accounting policy and disclosure procedures are required for accounting for work-in-progress generated and cumulative fund received from the MoRTH in the books of account. Since the financial impact of these activities are substantial in nature as compared to the other activities of the company, these two financial heads require a proper disclosure in the final accounts and financial statement of the company. So far as the accounting standards of the Institute of Chartered Accountants of India (ICAI) are concerned, there is no such clarity to disclose these items in the financial statements. If these two heads are not depicted in the financial statement considering that the company is not the owner of the work-in-progress and funds, then it may not be justified in respect to the transparency and true & fair view of balance sheet. The querist has separately provided a copy of specimen contract made entered in with third parties wherein the contract is entered in the name of "The President of India through the Ministry of Road Transport & Highways, Government of India".

B. Query

7. Therefore, the querist has requested the Expert Advisory Committee of the ICAI to advise the company, the report policy to be adopted to disclose the following heads in the books of account:

- (i) Work-in-progress generated out of the funds provided by the GOI and corresponding work-in-progress generated on behalf of the GOI.
- (ii) Cumulative amount of funds released to the company by the MoRTH for project as per the yearly budgetary allocation.

C. Points considered by the Committee

8. The Committee notes that the basic issues raised by the querist relate to accounting treatment of work-in-progress generated out of the funds provided by the GOI and generated on behalf of the GoI and accounting treatment of the amount of funds released to company by the MoRTH (GoI) for project as per the yearly budgetary allocation in the books of account of the company. Therefore, the Committee has considered only these issues and has not considered any other issue that may arise from the Facts of the Case, such as, accounting for agency commission received by the company and any expenditure incurred by the company out of such commission, etc. Further, the opinion expressed, hereinafter, is purely from accounting perspective and not from any legal perspective. At the outset, the Committee wishes to point out that since the querist has referred to financial year 2015-16 in the Facts of the Case, the opinion expressed hereinafter is from the perspective of the Accounting Standards notified under the Companies (Accounting Standards) Rules, 2006 and not from the perspective of Indian Accounting Standards (Ind ASs) notified under the Companies (Indian Accounting Standards) Rules, 2015.

9. At the outset, the Committee notes from the Facts of the Case that the Government

of India (GoI) through Notification entrusted the company the job of construction and development of the highways and other infrastructure projects, but the ownership of land acquired for the same remains vested with the GoI only. Further, the company is executing the national highways and other infrastructure projects on behalf of Government of India (GoI) and all the funds for execution of these projects are being financed by the GoI on the basis of yearly budget allocations. Moreover, the company is only entitled to receive agency commission as per the defined rate on the expenditure incurred. Hence, the Committee is of the view that it would not be incorrect to consider the company as an agent of the Government of India for execution of the said project and not a contractor for construction of the project. The Committee also notes paragraph 4 of AS 7, notified under the 'Rules', which states that "for the purposes of this Standard, construction contracts include, contracts for the rendering of services which are directly related to the construction of the asset, for example, those for the services of project managers and architects;" therefore, on the basis of facts available with the Committee such as agency commission being paid, the contract with the third parties are made in name of the Government of India, it is evident that the principles of AS 7 are applicable to the extent of revenue earned by the company for such arrangements viz. agency commission in the extant case.

10. With regard to the issue raised, the Committee notes the term 'asset' as defined in paragraph 49(a) of the 'Framework for the Preparation and Presentation of Financial Statements', issued by the Institute of Chartered Accountants of India as follows:

"(a) An *asset* is a resource controlled by the enterprise as a result of past events from which future economic benefits are expected to flow to the enterprise."

From the above, the Committee is of the view that so far as the company is concerned, the project assets do not meet the definition of 'asset'. This is because the future economic benefits from the project assets are not expected to flow to the company as it is specifically mentioned by the querist that the company is not the owner of the work-in-progress and the funds received from the GoI. The project assets are not even funded by the company; rather these are funded by the GoI. Accordingly, the project assets or work-in-progress during the project execution should not be recognised by the company in its books of account.

11. As regards the issue raised by the querist relating to the accounting treatment of funds received by the company from the MoRTH (GoI), the Committee is of the view that these funds are received by the company not for its own activities; rather for execution of the project on behalf of the GoI and therefore, these are of the nature of 'asset held in trust'. Accordingly, the asset and liability in respect thereof should be recognised in the books of account of the company. As and when the expenditure is incurred, the 'asset held in trust' should be credited with corresponding debit to the related liability. Further, considering the nature of company's role in the extant case, the company may, if it so desires, disclose in the notes forming part of accounts, project assets/capital work-in-progress and project liabilities with an appropriate disclosure of their nature.

D. Opinion

12. On the basis of the above, the Committee is of the following opinion on the issues raised in paragraph 7 above:

- (i) The work in progress generated out of the fund provided by MoRTH (GOI) and corresponding work in progress generated on behalf of GOI should not be recognised in the books of account of the company, as discussed in paragraph

10 above. However, considering the nature of company's role in the extant case, the company may, if it so desires, disclose in the notes forming part of accounts, project assets/capital work-in-progress with an appropriate disclosure of their nature.

- (ii) As regards the cumulative amount of funds released to the company by MoRTH (GoI) for project as per the yearly budgetary allocation, the Committee is of the view that these funds are received by the company not for its own activities; rather for execution of the project on behalf of the GoI and therefore, these are of the nature of 'asset held in trust'. Accordingly, the asset and liability in respect thereof should be recognised in the books of account of the company. As and when the expenditure is incurred, the 'asset held in trust' should be credited with corresponding debit to the related liability, as discussed in paragraph 11 above.
