

Query No. 44

Subject: Classification of accrued interest on short term FDR/flexi deposits of 3 months or less.¹

A. Facts of the Case

1. A company (hereinafter referred to as ‘the Company’) is a Public Sector Undertaking (PSU) under the aegis of Ministry of Housing & Urban Affairs, Government of India established in the year 1960 as a construction arm of Government of India. The Company has achieved Navratna status in the year 2014. The Company as a group has four operational subsidiaries and several joint ventures under its umbrella. The Company operates into three business segments (a) Project Management Consultancy (PMC); (b) Real Estate and (c) Engineering, Procurement and Construction (EPC).

Under PMC segment, the Company executes cost plus contracts obtained on either nomination basis or through competitive bidding. The projects are executed by contractors appointed by the Company through transparent tendering process.

Under Real Estate segment, the Company works as a developer, procures land, gets the works executed by entering into contractual engagements with contractors and the project is sold in pre-construction and post construction stages. Marketing is done by the Company only.

Under EPC segment, the Company takes contract at fixed prices and the work is executed through sub-contractors.

2. Indian Accounting Standards (Ind AS) were introduced on the Company w.e.f. 01.04.2016. The accounts of the financial year (F.Y.) 2016-17 were prepared in accordance with Ind AS along with comparatives of F.Y. 2015-16 and opening balance sheet of 01.04.2015.

3. ‘Cash and cash equivalents’ is not defined in Ind AS Schedule III however, according to Ind AS 7, ‘Statement of Cash Flows’, cash is defined to include cash on hand and demand deposits with banks. Cash equivalents are defined as short-term, highly liquid investments that are readily convertible to known amounts of cash and which are subject to an insignificant risk of changes in value.

4. *As per paragraph 7 of Ind AS 7, ‘Statement of Cash Flows’:*

“Cash equivalents are held for the purpose of meeting short-term cash commitments rather than for investment or other purposes. For an investment to qualify as a cash equivalent it must be readily convertible to a known amount of cash and be subject to an insignificant risk of changes in value. Therefore, an investment normally qualifies as a cash equivalent only when it has a short maturity of, say, three months or less from the date of acquisition. Equity investments are excluded from cash equivalents unless they are, in substance, cash equivalents, for example in the case of preference shares acquired within a short period of their maturity and with a specified redemption date.”

¹ Opinion finalised by the Committee on 27.12.2023.

The Company presently presented 'Investment in Flexi Deposit & Fixed Deposit' having maturity three months or less from the date of acquisition as cash and cash equivalents along with any interest accrued on the same.

5. The querist has stated that the Company's fixed deposit and flexi deposits are made with banks which generally provide relaxation to the Company from the pre-mature cancellation charges (a copy of communication received from banks in this regard has been supplied separately by the querist for the perusal of the Committee). Further, the amount of accrued interest is only Rs. 4.63 crore which is only 0.28% on total cash and cash equivalents of Rs. 1,652.78 crore as on March 31, 2023.

6. The querist has also mentioned that Bank has accrued/paid the accrued interest amount in the Company's fixed and flexi deposit account or provided statement of accrued interest with principal amount of flexi/fixed deposit (a copy of the sample deposit statement, issued by the bank has been supplied by the querist for the perusal of the Committee). On the basis of such statement, the Company accounted for the accrued interest on flexi/fixed deposit and presented the same along with underlying asset, i.e., flexi/fixed deposit having original maturity of three months or less under 'Cash and Cash Equivalents' considering there will be no significant change in the value of 'Cash and Cash Equivalents' on account of pre-mature redemption of FDR/flexi deposit.

It is observed that different practices are being adopted across the industries.

B. Query

7. In view of the above, the opinion of Expert Advisory Committee has been sought as to whether the Company may continue to present accrued interest on short-term FDR/flexi deposits having original maturity of 3 months or less alongwith the underlying FDR/flexi deposits under 'Cash and Cash Equivalents' or any other treatment is required as per applicable Ind AS.

C. Points considered by the Committee

8. The Committee notes that the basic issue raised by the querist relates to the presentation of accrued interest on short term FDR/flexi deposits of 3 months or less in the financial statements (balance sheet) prepared as per the requirements of Schedule III to the Companies Act, 2013. The Committee has, therefore, considered only this issue and has not considered any other issue that may arise from the Facts of the Case, such as, presentation of accrued interest in the Statement of Cash Flows as per the requirements of Ind AS 7, materiality of the accrued interest as per the requirements of Ind AS, accounting for different business segments of the Company i.e. (a) Project Management Consultancy (PMC); (b) Real Estate and (c) Engineering, Procurement and Construction (EPC), accounting and presentation of deposits with banks or investments with maturity of more than three months, etc. Further, the opinion expressed hereinafter is purely from accounting perspective and not from legal perspective. Furthermore, the Committee wishes to point out that the Accounting Standards referred to in the Opinion are the Indian Accounting Standards, notified under the Companies (Indian Accounting Standards) Rules, 2015, as revised or amended from time to time.

9. The Committee notes that Division II of Schedule III to the Companies Act, 2013 (hereinafter referred to as 'Ind AS Schedule III') requires the following items to be presented under non-current assets and current assets on the face of the Balance Sheet:

“Current assets

(a) ...

(b) Financial Assets

...

(iii) Cash and cash equivalents

(iv) Bank balances other than (iii) above

...”

The Committee further notes the following requirements of Guidance Note on Division II - Ind AS Schedule III to the Companies Act 2013, issued by the Institute of Chartered Accountants of India (January 2022 Edition):

“8.1.16. Cash and Bank Balances

(i) Cash and cash equivalents shall be classified as:

(a) Balances with banks (of the nature of cash and cash equivalents);

(b) Cheques, drafts on hand;

(c) Cash on hand;

(d) Others (specify nature).

(ii) Bank balances other than cash and cash equivalents as above, shall be disclosed below cash and cash equivalents on the face of the Balance Sheet

...

Cash and cash equivalents is not defined in Ind AS Schedule III however, according to *Ind AS-7 Statement of Cash Flows*, Cash is defined to include cash on hand and demand deposits with banks. Cash Equivalents are defined as short term, highly liquid investments that are readily convertible into known amounts of cash and which are subject to an insignificant risk of changes in value.

Ind AS 7 further explains that an investment normally qualifies as a cash equivalent only when it has a short maturity of, say, three months or less from the date of acquisition. This would include term deposits with banks that have an original maturity of three months or less...”

10. From the above, the Committee is of the view that the cash equivalents are short-term, highly liquid investments with maturity of normally three months or less that are readily convertible to a known amount of cash and which are subject to an insignificant risk of changes in value. The Committee notes from this that the critical criteria in the definition of cash equivalents are that these are ‘convertible to known amounts of cash’ and ‘subject to an insignificant risk of changes in value’. As per first criterion mentioned above, the amount of cash that will be received must be known at the time of the initial investment. Further, the

second criterion requires assessment of potential value changes due to various risks, including interest penalty due to early redemption.

In this context, the Committee notes from the Facts of the Case that the flexi deposits and FDRs (along with interest component) in the extant case are having a maturity of less than 3 months from the date of acquisition. Thus, these are short-term, highly liquid investments with maturity of normally three months or less.

With regard to criterion of 'convertible to known amounts of cash', the Committee notes that since in the extant case, the interest rates are fixed, the amounts of principal and interest expected to be received are known at the inception of the investment. Accordingly, the investments are convertible to known amounts of cash, Further, it is noted from the copy of the sample deposit statement, issued by the bank (which has been supplied by the querist for the perusal of the Committee), that the balance appearing in the bank statement of the Company's fixed deposit account is inclusive of the accrued interest.

With regard to the second criterion relating to 'subject to an insignificant risk of changes in value', it is noted from the facts supplied by the querist that in the extant case, either there is 'nil' pre-closure/premature penalty/cancellation charges or the banks have waived off such charges. Further, from the facts of the case, there does not appear to be any other factor leading to significant change in the value of balances in fixed/flexi deposits along with interest accrued thereon in the extant case. Thus, the terms and conditions under which the deposits have been made appear to indicate that the amounts to be obtained are subject to insignificant change in value.

Therefore, the Committee is of the view that balances in fixed/flexi deposits along with interest accrued and credited thereon meet the definition of cash equivalents. Accordingly, as per the requirements of Ind AS Schedule III, these should be presented as 'cash and cash equivalents' in the balance sheet.

D. Opinion

11. On the basis of the above, the Committee is of the opinion on the query raised in paragraph 7 above that accrued interest amount for the Company's fixed & flexi deposit account meets the definition of 'cash and cash equivalent' as per the requirements of Ind AS Schedule III and should be presented as 'cash and cash equivalents' in the balance sheet, as discussed in paragraph 10 above.