

**Query No. 51**

**Subject: Recognition of late payment surcharge (LPSC) in accounts under Ind AS framework.<sup>1</sup>**

**A. Facts of the Case**

1. The Company (hereinafter referred to as ‘the Company’) is a domestic company registered under the erstwhile Companies Act, 1956. It has been notified as a state transmission utility by the Government of National Capital Territory (NCT) of Delhi. It is engaged in the business of operation and maintenance of transmission system in NCT. It is responsible to ensure development of intra-state power transmission system to facilitate intra-state transmission of electricity. The Company receives energy from various sources located within Delhi as well as outside Delhi and transmits this energy to various distribution entities through its transmission system on mutually agreed terms and conditions.

2. The Company has entered into bulk power transmission agreement (BPTA) with power distribution companies namely, T Ltd., BY Ltd. and BR Ltd. T Ltd. is now known as N Ltd.

3. In accordance with such Agreement, the Company is entitled to receive transmission/wheeling charges. The Company is further entitled to receive late payment surcharge (LPSC) from power distribution companies in case they make payment of wheeling charges to the Company beyond the due date stipulated in the Agreement. (A copy each of Bulk Power Transmission Agreement dated 09/10/2009 along with Annexure-A thereto having the heading ‘General Provisions Governing the Agreement’ entered into by the Company with BR Ltd. and BY Ltd. has been supplied separately by the querist for the perusal of the Committee).

In addition to the above, a copy each of Delhi Electricity Regulatory Commission (Terms and Conditions for Determination of Tariff) Regulations, 2017 and Delhi Electricity Regulatory Commission (SERC) (Terms and Conditions for Determination of Tariff) Regulations, 2022 has been supplied separately by the querist for the perusal of the Committee, which provides the mode and components of computation of tariff for transmission charges payable by distribution companies to transmission companies, i.e., the Company.

4. T Ltd./N Ltd. is making payment regularly. However, BY Ltd. and BR Ltd. (‘DISCOMs’ or ‘Distribution Companies’) have not been making payments regularly, attracting the levy of LPSC on delayed payments.

5. The querist has stated that the Company is maintaining records of the amount of LPSC receivable from DISCOMs as per its calculations in excel sheets. DISCOMs are recognising liability in respect thereof in their books of accounts as per their own calculations and are also deducting tax at source thereon but are not regularly paying the amount of LPSC remaining after deduction of tax at source to the Company. In other words, the DISCOMs are making delayed payment of wheeling charges and LPSC thereon.

6. The Company was recognising income of LPSC in its accounts only to the extent of the tax deducted at source (TDS) by DISCOMs. The source document for recognition of income to the extent of TDS was the amount getting reflected in Form 26AS of the Company issued

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<sup>1</sup> Opinion finalised by the Committee on 29.1.2024.

by the Income-tax Department. In other words, the Company was not recognising income in its accounts of gross LPSC minus TDS.

7. In financial year (F.Y.) 2015-16, F.Y. 2016-17, F.Y. 2017-18 and F.Y. 2018-19, the statutory auditors of the Company made qualification on this policy stating that not recognising LPSC income on accrual basis has led to understatement of income by INR 210 crore, INR 183.15 crore, INR 170.01 crore and INR 170.78 crore, respectively.

8. Qualifications raised in Independent Audit Report of F.Y. 2015-16 (reproduced herewith for the sake of ready reference on sample basis, as almost identical qualification has been made in other years), read as follows:

a) Qualified opinion of Independent Auditor for F.Y. 2015-16

“1. As per Accounting Policy No. 2.9(c), “The surcharge on late payment overdue sundry debtors for sale of energy/Wheeling Charges is not treated accrued due to uncertainty of its realisation and is, therefore, accounted for on receipt basis”. During the year 2015-16, the Company has recognised Rs. 233.55 lakhs as income equivalent to TDS deposited by the debtors (Refer Note No. 21). As per Accounting Standard 9, ‘Revenue Recognition’, revenue should be recognized if there is no uncertainty. *As debtors have deducted and deposited TDS, the income became certain and gross amount of Rs. 23335.5 lakhs should have been recognized instead of Rs. 2333.35 lakhs. Therefore, the profit of the company is understated by the Rs.21001.95 lakhs.”*

(Emphasis supplied by the querist.)

9. The Comptroller and Auditor General of India (CAG) audit team while carrying out supplementary audit for the above-mentioned financial years had never expressed any dissent with the qualification made by the statutory auditor in those years. As per the querist, it necessarily implies that CAG was in agreement with the then statutory auditors that non-recognition of LPSC in accounts by the Company amounted to understatement of income.

10. Further, the querist has stated that it is pertinent to mention here that for these financial years, Income-tax Department in its various assessment orders has held that LPSC not recognised in accounts was income accrued in the hands of the Company on accrual basis and imposed tax on unrecognised LPSC. Accordingly, for the various assessment years, huge additions have been made against the Company for unrecognised LPSC income in those years. Thus, Income-tax Department has drawn adverse inference on account of LPSC by way of making an addition in the assessment order made under section 143(3) for Assessment Year (A.Y.) 2016-17, A.Y. 2017-18 and A.Y. 2018-19 of the amount of LPSC not recognised in accounts as income.

11. In view of continuous audit observations of statutory auditors (agreed to by CAG as well, as it chose to not dissent with statutory auditors) and adverse view in the matter of Income-tax Department too, the Company decided to review its accounting treatment with regard to the recognition of LPSC in its accounts, keeping in view Indian Accounting Standard (Ind AS) 115, ‘Revenue from Contracts with Customers’, as notified by the Ministry of Corporate Affairs (MCA) under section 133 of the Companies Act, 2013.

12. While reviewing accounting treatment of LPSC, the Company observed that Clause No. 5 of the Bulk Power Transmission Agreement dated 09/10/2009 under the heading 'Transmission Charges Accounting' provides that the Company shall raise monthly bill towards transmission charges for use of its transmission system upon the power distribution companies on or before 10<sup>th</sup> day of the succeeding month in accordance with the tariff orders issued by DERC from time to time. Further, Clause No. A.4(c) of Annexure-A of the Agreement having the heading 'General Provisions Governing the Agreement' provides that the due date for payment of monthly bills by the distribution companies to the Company is one month from the date of presentation of the bill. Clause No A.4 (e) of the said annexure provides that in case the payment of bills of transmission charges is delayed beyond a period of one month from the date of presentation of bill, the transmission licensee may levy a late payment surcharge at the rate of 1.25% per month on the unpaid amount from the due date up to the actual date of payment. For the sake of convenience, the above stated clauses of the agreement and annexure thereto are reproduced here below:

#### **“5.0 TRANSMISSION CHARGES ACCOUNTING**

Monthly Bills towards Transmission Charges for use of the Transmission System shall be raised by the Company on or before 10th day of the subsequent month in accordance with the tariff orders issued by DERC from time to time. The required data for this purpose shall be furnished by State Load Dispatch Centre (SLDC) to the Company up to 7<sup>th</sup> of every month.

...

Payment of bills by the Beneficiary shall be governed by Clause A.4 of General provisions governing the Agreement (Annexure-A).

#### **A.4 PAYMENT, REBATE, LPSC ETC.**

...

(c) **Due Date:** One month from the date of presentation of bill.

(e) **Late Payment Surcharge (LPSC)**

In case the payment of bills of transmission charges is delayed beyond a period of one month from the date of presentation of bill, the Transmission Licensee may levy a late payment surcharge at the rate of 1.25% per month on the unpaid amount from the due date up to the actual date of payment.”

13. Further, Regulation No. 137 of the DERC (Terms and Conditions for Determination of Tariff) Regulations, 2017 (hereinafter referred to as 'Regulation 2017') too provides that in case the payment of any bill for charges/tariff, payable under the Regulation by the distribution company to transmission company, is delayed beyond a period of 60 days from the date of billing, late payment surcharge at the rate of 1.5% per month shall be levied by the transmission company. Similarly, Regulation No. 138 of the said Regulation provides for allowing of rebate by the transmission company to the distribution company in the event of payment by the distribution company within a period of 30 days of presentation of bills by the transmission company.

From a combined reading of Regulation No. 137 and 138, the Company came to the conclusion that the Regulation provides relief where payment is made before the due date (30 days of the presentation of bills) and imposes surcharge for late payment after such due date, implying that the late payment surcharge is compensatory in nature, with aim to recompense transmission company against delayed payments made by distribution company. For the sake of convenience, the Regulation No. 137 and 138 are reproduced here below:

“137. **Late Payment Surcharge**

In case the payment of any bill for charges payable under these regulations is delayed by a beneficiary of generating entity or long term transmission customer/DICs as the case may be, beyond a period of 60 days from the date of billing, a late payment surcharge at the rate of 1.50% per month shall be levied by the generating entity or the transmission licensee, as the case may be.

138. **Rebate**

For payment of bills of the generating entity and the transmission licensee through letter of credit on presentation or through any NEFT/RTGS within a period of 2 days of presentation of bills by the generating entity or the transmission licensee, a rebate of 2% shall be allowed.

Provided that in case payments are made on any day after 2 days and within a period of 30 days of presentation of bills by the generating entity or the transmission licensee, a rebate of 1% shall be allowed.”

14. From a perusal of the above referenced and discussed Agreement and Regulation, the Company observed that the terms for late payment from the day of presentation of bills to customers are expressly provided in the Agreement and Regulation, which are binding on both the distribution company as well as the Company, i.e., transmission company. Thus, it can be safely concluded that late payment surcharge recoverable by the Company gets its sanctity not only from its Agreement with the distribution companies but also by virtue of the Regulation. It necessarily implies that late payment surcharge partakes the character of contractual as well as statutory accrual in the hands of the Company.

15. The Company is a company registered under the erstwhile Companies Act, 1956 and therefore, by virtue of section 128 of the Companies Act, 2013, it is mandatorily required to maintain its accounts on accrual basis, which means that the Company is required to recognise income and expenses accruing or incurred in a particular year in that year itself, irrespective of whether such income has been received or expense has been paid in that year or not.

16. In this regard, the querist has stated that paragraph 6 of Ind AS 115 requires that an entity shall apply Ind AS 115 to a contract where a counter party to the contract is a customer. The Standard defines customer as a party who has contracted with an entity to obtain goods or services that are an output of the entity's ordinary activities in exchange for consideration. In view of this definition, the Company noticed that the DISCOMs are its customers with whom it has contracted in relation to its transmission services that are output of its ordinary activities in exchange for consideration in the form of transmission charges. Thus, it transpires that the recognition of LPSC by the Company in its account shall be governed by the provisions of Ind AS 115.

17. Paragraph 9 of Ind AS 115 requires that an entity shall account for a contract with a customer only when all of the following criteria are met:

- (a) the parties to the contract have approved the contract (in writing, orally or in accordance with other customary business practices) and are committed to perform their respective obligations;
- (b) the entity can identify each party's rights regarding the goods or services to be transferred;
- (c) the entity can identify the payment terms for the goods or services to be transferred;
- (d) the contract has commercial substance (i.e. the risk, timing or amount of the entity's future cash flows is expected to change as a result of the contract); and
- (e) it is probable that the entity will collect the consideration to which it will be entitled in exchange for the goods or services that will be transferred to the customer. In evaluating whether collectability of an amount of consideration is probable, an entity shall consider only the customer's ability and intention to pay that amount of consideration when it is due. The amount of consideration to which the entity will be entitled may be less than the price stated in the contract if the consideration is variable because the entity may offer the customer a price concession (see paragraph 52).

18. The querist has stated that insofar as the applicability of paragraphs 9(a), (b) and (c) is concerned, the Company has entered into a contract (BPTA) with DISCOMs customers in writing, identifying and ascertaining each party's right regarding the quantification of LPSC and payment terms for such LPSC. Thus, the parties to the contract have approved the contract in writing. Further, the recognition of LPSC by the DISCOM customers as expense in their books of account coupled with deduction of TDS at the rate of 10% of LPSC, entailing immediate outflow of 10% of LPSC from the hands of DISCOM customers to the exchequer on behalf of the Company establishes the customers' commitment to perform their respective obligation of payment of LPSC under the contract. Thus, conditions enumerated in paragraph 9(a), 9(b) and 9(c) get fully satisfied.

19. As per paragraph 9(d), it is clear that the contract has commercial substance since the amount of the Company's future cash flows is expected to enhance and thus, undergo a change as a result of the contract containing the clause of receipt of LPSC from DISCOMs customers. Thus, condition enumerated in paragraph 9(d) gets fully satisfied.

20. As per the querist, as far as the satisfaction of the conditions – DISCOMs'/customers' ability and intention to pay LPSC to evaluate the probability or collectability of LPSC – prescribed in paragraph 9(e) is concerned, the Company observed from audited accounts of DISCOMs, BR Ltd. and BY Ltd., as under:

- Audited accounts of BR Ltd. for F.Y. 2021-22 shows that it has to pay Rs. 7852.03 crore to its trade creditors including the Company and the source of payment thereof by BR Ltd. is receivable of Rs. 10855.93 crore on account of regulatory deferral account balances. Regulatory deferral account balances broadly represent amounts receivable by DISCOMs from the Government of NCT of Delhi and consumers of Delhi.
- The audited accounts of BR Ltd. further reveals positive current ratio of 1.39 and net worth or net owned funds of Rs. 5184.40 crore.
- Similarly, audited accounts of BY Ltd. for F.Y. 2021-22 shows that it has to pay Rs. 7170.45 crore to its trade creditors including the Company and the source of payment

thereof by BR Ltd. is receivable of Rs. 9744.43 crore on account of regulatory deferral account balances. The Company observed that regulatory deferral account balances broadly represents amounts receivable by DISCOMs from Government of NCT of Delhi and consumers of Delhi.

- The audited accounts of BY Ltd. further reveals positive current ratio of 1.33 and net worth or net owned funds of Rs. 2605.64 crore.
- Further, a perusal of the Tariff Order for F.Y. 2021-22 passed by the Delhi Electricity Regulatory Commission ('Commission' or 'DERC') reveals that in paragraph no. 5.5 of the Order, the Commission has approved surcharge @ 8% on the tariff for liquidating the regulatory assets of DISCOMs.
- Further, in paragraph no. 2.253 of the Order, the Commission has noted that it submitted before the Hon'ble Supreme Court in Civil Appeal of 2010 that surcharge of 8% shall liquidate the regulatory assets of DISCOMs within 6 to 8 years; as noted in paragraph no. 2.243 of the Order, the surcharge was introduced vide Tariff Order dated 13/07/2012.
- BR Ltd. and BY Ltd. have represented before the Hon'ble Supreme Court in WP(C) No. 104 and 105 of 2014 that the regulatory assets approved by the Commission for them upto F.Y. 2013-14 is Rs. 8156 crore.
- The dues from the DISCOMs are being continuously recovered every year by three different methods. These are by:
  - Direct payments received from DISCOMs.
  - By adjustment of Short Term Open Access (STOA) charges payable to DISCOMs by the Company.
  - By diversion of subsidy payable to DISCOMs to the Company directly by the GNCTD.
- Summary sheet of dues recoverable towards transmission charges and LPSC; and recoveries there against made by the Company from both the DISCOMs BR Ltd. and BY Ltd. during the last six financial years is given here below in tabular form for the sake of reference:

- **BY Ltd.**

(Rs. in crore)

Financial Year	Dues towards Transmission and Other Bills		Dues towards LPSC	
	Transmission Charges raised during year	Payment received during Year	LPSC accrued during Year	Payment received during year
(1)	(2)	(3)	(4)	(5)
2016-17	217.23	122.85	93.67	59.52
2017-18	226.77	(140.75)	100.22	(66.89)
2018-19	257.57	(163.65)	169.37	(98.59)
2019-20	209.92	(200.03)	158.85	(135.05)
2020-21	238.92	(129.84)	146	(71.7)
2021-22	223.47	(122.28)	185.91	(83.5)

- **BR Ltd.**

(Rs. in crore)

Financial Year	Dues towards Transmission and Other Bills		Dues towards LPSC	
	Transmission Charges raised during year	Payment received during Year		Transmission Charges raised during year
(1)	(2)	(3)	(4)	(5)
2016-17	401.77	(233.38)	142.99	(86.62)
2017-18	442.04	(245.81)	174.28	(112.61)
2018-19	451.47	(358.55)	252.33	(203.66)
2019-20	370.6	(418.98)	236.16	(212.83)
2020-21	459.79	(267.32)	222.19	(129.67)
2021-22	391.3	(284.69)	276.65	(167.9)

- Summary sheet of TDS deducted by DISCOMs against LPSC getting duly reflected in Form 26AS of the Company:

(Rs. in crore)

Financial Year	TDS deducted by DISCOMs against LPSC	
	BY Ltd.	BR Ltd.
2016-17	9.43	10.91
2017-18	6.6	12.3
2018-19	5.95	11.3
2019-20	9.17	12.52
2020-21	4.4	7.14
2021-22	9.3	10.84

- Summary Sheet of subsidy getting adjusted by GNCTD of DISCOMs and adjusted by the Company against wheeling charges bills and LPSC recoverable from DISCOMs:

(Rs. in crore)

Financial Year	BY Ltd.	BR Ltd.	Total
2014-15	238,500,000	484,000,000	722,500,000
2015-16	457,000,000	1,023,000,000	1,480,000,000
2016-17	840,000,000	1,450,000,000	2,290,000,000
2017-18	1,499,400,000	2,693,800,000	4,193,200,000
2018-19	1,192,200,000	1,731,300,000	2,923,500,000
2019-20	1,603,300,000	2,672,200,000	4,275,500,000
2020-21	1,263,600,000	2,111,100,000	3,374,700,000
2021-22	1,085,500,000	1,787,100,000	2,872,600,000
<b>Total</b>	<b>8,179,500,000</b>	<b>13,952,500,000</b>	<b>22,132,000,000</b>

- Thus, every year, substantive payments are being recovered from the DISCOMs and are being adjusted against the LPSC due from the DISCOMs. In view of these facts, it is apparent that payments on account of LPSC are continuously being recovered and hence it cannot be said that payments are not being received from the DISCOMs.
- Thus, the Company noticed that the DISCOMs have the ability to pay because the Commission has admitted that the DISCOMs are entitled to recovery of regulatory assets resulting into automatic inference of capacity to pay of DISCOMs to the Company out of such regulatory assets, and more particularly, substantive payments are being recovered by the Company from the DISCOMs and are being adjusted against the LPSC dues.

21. As per DISCOMs' intention to pay is concerned:

- The year-end balance and ledger account confirmation signed by the Company and DISCOMs, BR Ltd. and BY Ltd. and provided by them to the Company, show that the DISCOMs have confirmed that they have to pay late payment surcharge to the Company.
- As per the latest communication received consisting of accounts statement submitted by BR Ltd. and BY Ltd., they have adjusted the payment made by them against the LPSC first and principal later, showing their intent to pay the LPSC.
- The DISCOMs are recognising LPSC as expense in their books and deducting TDS thereon at the applicable rate as per their understanding.
- The Government of NCT of Delhi (GNCTD), which holds 100% ownership rights over the Company exercises significant influence over BR Ltd. and BY Ltd. too by way of holding 49% voting power in those two companies.
- BR Ltd. and BY Ltd. at various times *have suo-moto* submitted plans to liquidate their dues towards principal and LPSC. They have submitted Onetime settlement offer to the Company vide their offer dated 2/7/2022.
- DERC has conducted hearing for the reconciliation of the dues payable by BR Ltd. and BY Ltd. to the Company so as to make a roadmap as to how the dues of the Company can be expeditiously liquidated.
- Thus, the Company noticed that the DISCOMs, BR Ltd. and BY Ltd. have confirmed their liability towards late payment surcharge demanded by the Company from DISCOMs.

22. As per the querist, considering the above reproduced paragraph 9 of the Ind AS 115, delayed payment of dues by customer is not a relevant factor for determination of the timing of recognition of LPSC.

23. On the basis of the above, the Company formed the view that the late payment surcharge in the extant case should be recognised as income in accounts, and accordingly, the Company decided to change its accounting policy with regard to recognition of LPSC in its accounts.

24. Accordingly, the Company changed its accounting policy with respect to recognition of LPSC in accounts in consonance with Ind AS 115 and in alignment with the opinion of statutory auditors and CAG, and it expected removal of qualification in its accounts by the auditors made in auditor's reports for the financial years ending upto 31.03.2019. However, the statutory auditors in F.Y. 2020-21 changed their earlier stand and objected to treatment of change in accounting policy by the Company and stated that the change in accounting policy

is contrary to the provisions of Ind AS 115 as there has been continuous default by the DISCOMs towards payment of LPSC charges and there is significant uncertainty as to its recoverability. As per the independent audit report, the change in the accounting policy has resulted in profit for the year before tax expense being overstated by INR 337.64 crores in F.Y. 2020-21.

As per the querist, the language of Ind AS 115 has not undergone any change in F.Y. 2020-21 as compared to the earlier years.

25. When there is no change in the contents of Ind AS 115 in F.Y. 2020-21 as compared with earlier years, wherein the statutory auditors and CAG gave qualified opinion with respect to non-recognition of LPSC by the Company in its accounts for financial years ending upto 31.03.2019, then, according to the querist, it means that the statutory auditors and CAG in those years were of the opinion that there was no uncertainty with regard to recoverability of LPSC by the Company from DISCOMs.

26. Qualification made in independent audit report of F.Y. 2021-22 reads as follows:

*Qualified opinion of Independent Auditor for F.Y. 2021-22*

“Refer Note no. 23 (b) regarding accounting of Late Payment Surcharge Charges (LPSC) on accrual basis w.e.f. 01.04.2020 which were earlier accounted on cash basis. Consequent to the above change in accounting policy w.e.f. 01.04.2020, INR 46280.94 lakhs on account of LPSC charges pertaining to financial year 2021-22 has been recognised as other operating revenue in these financial statements (Refer Note 23).

The above change in accounting policy is contrary to the provisions of Ind AS 115. There has been continuous default by the DISCOMs towards payment of these LPSC charges and there is significant uncertainty as to its recoverability, however, no provision for these doubtful debts has been made in these financial statements. The DISCOMs from whom these LPSC charges are receivable have quantified a sum of INR 20146.14 lakhs as payable on account of LPSC on which TDS of INR 2014.61 lakhs has been deducted by them. The impact of this difference on subsequent reconciliation with the concerned DISCOMs cannot be ascertained presently.

Further, the above change has been made effective from F.Y. 2020-21 and LPSC charges receivable for F.Y. 2019-20 and earlier years have not been accounted for in these financial statements. The above recognition of LPSC on accrual basis has resulted in Profit for the year before tax expense being overstated by INR 46280.94 lakhs, Trade Receivables overstated by INR 44266.33 and current tax assets being overstated by INR 2014.61 lakhs.”

27. On the basis of the above qualification expressed by the statutory auditor in F.Y. 2021-22, the CAG of India in its supplementary report stated that the accounts of the Company do not present true and fair view and it was not proper on the part of auditor to have provided the assurance that accounts presented a true and fair view. Pursuant to representation made by the Company before CAG of India, the CAG of India vide letter dated 05.06.2023 has advised the Company to obtain opinion of the Expert Advisory Committee of the Institute of Chartered Accountants of India.

## B. Query

28. In view of the above, opinion of the Expert Advisory Committee of the Institute of Chartered Accountants of India is sought as to whether the accounting policy of the Company to recognise LPSC income in the accounts on accrual basis yearly at the rate of LPSC approved by the DERC in terms of statutory DERC Regulations (1.50% per month) and recoverable from DISCOMs is consistent with the Ind AS 115 and correct accounting policy.

## C. Points considered by the Committee

29. The Committee notes that the basic issue raised in the query relates to recognition of late payment surcharge (LPSC) in the financial statements of the Company. 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, accounting for transmission/wheeling charges, accounting in the books of DISCOMs, accounting under previous GAAP, appropriateness of the qualification/opinion issued by the Statutory Auditor, applicability of Ind AS 114, 'Regulatory Deferral Accounts', accounting for one-time settlement offer made by DISCOM, measurement of late payment surcharge, accounting for rebate to customers, appropriateness of accounting for change made effective from F.Y. 2020-21 with respect to LPSC receivable for F.Y. 2019-20 and earlier years, detailed aspects of impairment of receivables and application of Ind AS 109, application (if any) of Ind AS 8, 'Accounting Policies, Changes in Accounting Estimates and Errors', etc. The Committee wishes to point out that the opinion expressed hereinafter is in the context of Indian Accounting Standards, notified under the Companies (Indian Accounting Standards) Rules, 2015 as amended from time to time. Further, the Committee has examined the issue only from accounting perspective and not from any tax (GST or income-tax) or legal perspective including Supreme Court judgements or other applicable legal enactments, Assessment Orders, legal interpretation of agreements between the Company and other parties, legal interpretation of Delhi Electricity Regulatory Commission (Terms and Conditions for Determination of Tariff) Regulations, 2017, Delhi Electricity Regulatory Commission (Terms and Conditions for Determination of Tariff) Regulations, 2022 etc.

30. The Committee notes that a contract with customer should first meet the criteria as per paragraph 9 of Ind AS 115, before recognition of revenue under that contract as per the requirements of Ind AS 115. Therefore, in the extant case, at first, the Committee examines the contract with its customers, BR Ltd. and BY Ltd. in the context of uncertainty with regard to recoverability/collectability under the requirements of Ind AS 115 (viz., paragraph 9(e), which appears to be the main contention of the auditors against the revenue recognition policy of the Company) presuming that other criteria as per paragraph 9 are met. In this regard, the Committee notes the following requirements of Ind AS 115 and the 'Basis for Conclusions' of International Financial Reporting Standard (IFRS) 15 (which is corresponding international standard of Ind AS 115), issued by the International Accounting Standards Board (IASB):

### *Ind AS 115*

**“9 An entity shall account for a contract with a customer that is within the scope of this Standard only when all of the following criteria are met:**

- (a) the parties to the contract have approved the contract (in writing, orally or in accordance with other customary business practices) and are committed to perform their respective obligations;**

- (b) **the entity can identify each party's rights regarding the goods or services to be transferred;**
- (c) **the entity can identify the payment terms for the goods or services to be transferred;**
- (d) **the contract has commercial substance (ie the risk, timing or amount of the entity's future cash flows is expected to change as a result of the contract); and**
- (e) **it is probable that the entity will collect the consideration to which it will be entitled in exchange for the goods or services that will be transferred to the customer. In evaluating whether collectability of an amount of consideration is probable, an entity shall consider only the customer's ability and intention to pay that amount of consideration when it is due. The amount of consideration to which the entity will be entitled may be less than the price stated in the contract if the consideration is variable because the entity may offer the customer a price concession (see paragraph 52)."**

"13 If a contract with a customer meets the criteria in paragraph 9 at contract inception, an entity shall not reassess those criteria unless there is an indication of a significant change in facts and circumstances. For example, if a customer's ability to pay the consideration deteriorates significantly, an entity would reassess whether it is probable that the entity will collect the consideration to which the entity will be entitled in exchange for the remaining goods or services that will be transferred to the customer."

*Basis for Conclusions of IFRS 15*

"BC42 The boards included the criterion in paragraph 9(e) of IFRS 15 (which acts like a collectability threshold) because they concluded that the assessment of a customer's credit risk was an important part of determining whether a contract is valid. Furthermore, the boards decided to include this criterion as a consequence of their decision that customer credit risk should not affect the measurement or presentation of revenue (see paragraphs BC259-BC265).

BC43 The boards decided that a collectability threshold is an extension of the other requirements in paragraph 9 of IFRS 15 on identifying the contract. In essence, the other criteria in paragraph 9 require an entity to assess whether the contract is valid and represents a genuine transaction. The collectability threshold is related to that assessment because a key part of assessing whether a transaction is valid is determining the extent to which the customer has the ability and the intention to pay the promised consideration. In addition, entities generally only enter into contracts in which it is probable that the entity will collect the amount to which it will be entitled.

BC44 ... the boards observed that in most transactions, an entity would not enter into a contract with a customer in which there was significant credit risk associated with that customer without also having adequate economic protection to ensure that it would collect the consideration. Consequently, the boards decided that there would not be a significant practical effect of the different meaning of the same term because the population of transactions that would fail to meet the criterion in paragraph 9(e) of IFRS 15 would be small.

BC45 In determining whether it is probable that an entity will collect the amount of consideration to which the entity will be entitled, an entity might first need to determine the amount of consideration to which the entity will be entitled. This is because, in some circumstances, the amount of consideration to which an entity will be entitled may be less than the price stated in the contract. This could be because the entity might offer the customer a price concession (see paragraph 52 of IFRS 15) or because the amount of consideration to which an entity will be entitled varies for other reasons, such as the promise of a bonus. In either of those circumstances, an entity considers whether it is probable that the entity will collect the amount of consideration to which it will be entitled when the uncertainty relating to that consideration is resolved. The entity assesses whether it is probable of collecting that amount by considering both of the following:

- (a) the ability (ie the financial capacity) of the customer to pay the amount of consideration to which the entity will be entitled in exchange for the goods or services transferred.
- (b) the customer's intention to pay that amount. The boards observed that an assessment of the customer's intention would require an entity to consider all of the facts and circumstances, including the past practice of that customer or customer class. The boards noted that this assessment should be made on the assumption that the amount will be due (ie the corresponding performance obligation will be satisfied and the consideration is not subject to further variability that might affect the entity's entitlement to that consideration).”

The Committee notes from the above that the collectability threshold as per paragraph 9(e) is an extension of other criteria of paragraph 9 of Ind AS 115 and is related to assessment of whether the contract/transaction is valid and represents genuine transaction. Further, in genuine or valid transaction, normally, the customer would have the ability and the intention to pay the promised consideration as the entities generally only enter into contracts in which it is probable that the entity will collect the amount to which it will be entitled. Also, in most transactions, an entity would not enter into a contract with a customer in which there was significant credit risk associated with that customer without also having adequate economic protection to ensure that it would collect the consideration.

Further, with regard to assessment of customer's credit risk in terms of 'ability to pay' and 'intention to pay', the Committee notes that it has been informed by the querist that BR Ltd. and BY Ltd. have disclosed balances due to the Company as trade creditors in their financial statements and have also disclosed Rs. 10855.93 crore and Rs. 9744.43 crore respectively as receivable from the Government (in form of regulatory deferral accounts from the State Government and its customers). Further, substantive dues from the DISCOMs are being continuously recovered every year through direct payments received from DISCOMs, by adjustment of Short Term Open Access (STOA) charges payable to DISCOMs by the Company and by diversion of subsidy payable to DISCOMs to the Company directly by the GNCTD. The Committee is of the view that these factors indicate that BR Ltd. and BY Ltd. have the ability (financial capacity) to pay and also have the intention to pay the amount, which is also supported by the past practice of payment. Therefore, relying on the facts provided by the querist, the Committee is of the view that the condition under paragraph 9(e) of Ind AS 115 with regard to collectability of consideration is satisfied in the extant case; and the Company should account for contract with DISCOMs as per the requirements of Ind AS

115 and accordingly, recognise revenue as per the following requirements of Ind AS 115 (which are based on accrual basis and not cash or receipt basis of accounting):

**“31 An entity shall recognise revenue when (or as) the entity satisfies a performance obligation by transferring a promised good or service (ie an asset) to a customer. An asset is transferred when (or as) the customer obtains control of that asset.”**

Thus, the revenue is to be recognised on satisfaction of performance obligation by transferring good or service to the customer and not on receipt of cash or consideration from the customer.

31. With regard to accounting for LPSC, the Committee further notes the following requirements of Ind AS 115 and the ‘Basis for Conclusions’ of International Financial Reporting Standard (IFRS) 15 (which is corresponding international standard of Ind AS 115), issued by the International Accounting Standards Board (IASB):

*Ind AS 115*

**“Determining the transaction price**

**47 An entity shall consider the terms of the contract and its customary business practices to determine the transaction price. The transaction price is the amount of consideration to which an entity expects to be entitled in exchange for transferring promised goods or services to a customer, excluding amounts collected on behalf of third parties (for example, some sales taxes). The consideration promised in a contract with a customer may include fixed amounts, variable amounts, or both.**

48 The nature, timing and amount of consideration promised by a customer affect the estimate of the transaction price. When determining the transaction price, an entity shall consider the effects of all of the following:

- (a) variable consideration (see paragraphs 50–55 and 59);
- (b) constraining estimates of variable consideration (see paragraphs 56–58);
- (c) the existence of a significant financing component in the contract (see paragraphs 60–65);
- (d) non-cash consideration (see paragraphs 66–69); and
- (e) consideration payable to a customer (see paragraphs 70–72).”

**“The existence of a significant financing component in the contract**

60 In determining the transaction price, an entity shall adjust the promised amount of consideration for the effects of the time value of money if the timing of payments agreed to by the parties to the contract (either explicitly or implicitly) provides the customer or the entity with a significant benefit of financing the transfer of goods or services to the customer. In those circumstances, the contract contains a significant financing component. A significant financing component may exist

regardless of whether the promise of financing is explicitly stated in the contract or implied by the payment terms agreed to by the parties to the contract.

- 61 The objective when adjusting the promised amount of consideration for a significant financing component is for an entity to recognise revenue at an amount that reflects the price that a customer would have paid for the promised goods or services if the customer had paid cash for those goods or services when (or as) they transfer to the customer (ie the cash selling price). An entity shall consider all relevant facts and circumstances in assessing whether a contract contains a financing component and whether that financing component is significant to the contract, including both of the following:
- (a) the difference, if any, between the amount of promised consideration and the cash selling price of the promised goods or services; and
  - (b) the combined effect of both of the following:
    - (i) the expected length of time between when the entity transfers the promised goods or services to the customer and when the customer pays for those goods or services; and
    - (ii) the prevailing interest rates in the relevant market.
- 62 Notwithstanding the assessment in paragraph 61, a contract with a customer would not have a significant financing component if any of the following factors exist:
- (a) the customer paid for the goods or services in advance and the timing of the transfer of those goods or services is at the discretion of the customer.
  - (b) a substantial amount of the consideration promised by the customer is variable and the amount or timing of that consideration varies on the basis of the occurrence or non-occurrence of a future event that is not substantially within the control of the customer or the entity (for example, if the consideration is a sales-based royalty).
  - (c) the difference between the promised consideration and the cash selling price of the good or service (as described in paragraph 61) arises for reasons other than the provision of finance to either the customer or the entity, and the difference between those amounts is proportional to the reason for the difference. For example, the payment terms might provide the entity or the customer with protection from the other party failing to adequately complete some or all of its obligations under the contract.
- 63 As a practical expedient, an entity need not adjust the promised amount of consideration for the effects of a significant financing component if the entity expects, at contract inception, that the period between when the entity transfers a promised good or service to a customer and when the customer pays for that good or service will be one year or less.
- 64 To meet the objective in paragraph 61 when adjusting the promised amount of consideration for a significant financing component, an entity shall use the

discount rate that would be reflected in a separate financing transaction between the entity and its customer at contract inception. That rate would reflect the credit characteristics of the party receiving financing in the contract, as well as any collateral or security provided by the customer or the entity, including assets transferred in the contract. An entity may be able to determine that rate by identifying the rate that discounts the nominal amount of the promised consideration to the price that the customer would pay in cash for the goods or services when (or as) they transfer to the customer. After contract inception, an entity shall not update the discount rate for changes in interest rates or circumstances (such as a change in the assessment of the customer's credit risk).

- 65 An entity shall present the effects of financing (interest revenue or interest expense) separately from revenue from contracts with customers in the statement of profit and loss. Interest revenue or interest expense is recognised only to the extent that a *contract asset* (or receivable) or a contract liability is recognised in accounting for a contract with a customer.”

*Basis for Conclusions of IFRS 15*

“BC232 The boards also decided to remove the term ‘time value of money’ from the discussion about adjustments for financing components, to reflect their decision that the focus is on whether the payment terms provide the customer or the entity with a significant benefit of financing. This is because the term ‘time value of money’ is a broader economic term that may suggest that it is necessary to adjust the promised amount of consideration in circumstances other than when the cash sales price may differ from the contractual payments. In addition, the boards decided to refine the factors in paragraph 61 of IFRS 15 that an entity should consider when deciding whether a contract includes a significant financing component. Those factors require evaluation of:

- (a) the difference, if any, between the amount of promised consideration and the cash selling price of the promised goods or services. If the entity (or another entity) sells the same good or service for a different amount of consideration depending on the timing of the payment terms, this generally provides observable data that the parties are aware that there is a financing component in the contract. This factor is presented as an indicator because in some cases the difference between cash selling price and the consideration promised by the customer is due to factors other than financing (...).
- (b) the combined effect of (1) the expected length of time between when the entity transfers the promised goods or services to the customer and when the customer pays for those goods or services and (2) the prevailing interest rates in the relevant market. Although the boards decided that the difference in timing between the transfer of goods and services and payment for those goods and services is not determinative, the combined effect of timing and the prevailing interest rates may provide a strong indication that a significant benefit of financing is being provided.”

“BC234 The boards also observed that for many contracts, an entity will not need to adjust the promised amount of customer consideration because the effects of the financing component will not materially change the amount of revenue that

should be recognised in relation to a contract with a customer. In other words, for those contracts, the financing component will not be significant. During their redeliberations, the boards clarified that an entity should consider only the *significance* of a financing component at a contract level rather than consider whether the financing is *material* at a portfolio level. The boards decided that it would have been unduly burdensome to require an entity to account for a financing component if the effects of the financing component were not material to the individual contract, but the combined effects for a portfolio of similar contracts were material to the entity as a whole.”

“BC239 The boards considered whether the discount rate used to adjust the promised amount of consideration for the effects of a significant financing component should be a risk-free rate or a risk-adjusted rate. A risk-free rate would have been observable and simple to apply in many jurisdictions and it would have avoided the costs of determining a rate specific to each contract. However, the boards decided that using a risk-free rate would not result in useful information, because the resulting interest rate would not have reflected the characteristics of the parties to the contract. In addition, the boards noted that it would not necessarily have been appropriate to use any rate explicitly specified in the contract because the entity might offer 'cheap' financing as a marketing incentive and, therefore, using that rate would not have resulted in an appropriate recognition of profit over the life of the contract. Consequently, the boards decided that an entity should apply the rate used in a financing transaction between the entity and its customer that does not involve the provision of goods or services because that rate reflects the characteristics of the party receiving financing in the contract. That rate also reflects the customer's creditworthiness, among other risks.”

#### **“Presentation of the effect of a significant financing component**

BC244 As a result of the boards’ decision on the existence of a significant financing component (...), a contract with a customer that has a significant financing component would be separated into a revenue component (for the notional cash sales price) and a loan component (for the effect of the deferred or advance payment terms). Consequently, the accounting for a trade receivable arising from a contract that has a significant financing component should be comparable to the accounting for a loan with the same features. Consider the following example: Customer A purchases a good on credit and promises to pay CU1,000 in three years. The present value of this trade receivable is CU751. Now consider Customer B who borrows CU751 from a bank with a promise to pay CU1,000 in three years. Customer B uses the loan to purchase the same good as Customer A. Economically, those transactions are the same, but, in the absence of the requirements in IFRS 15 to account for a significant financing component, the form of the transaction would determine whether an entity would recognise revenue of CU751 or CU1,000 (ie on a discounted or an undiscounted basis). For this reason, paragraphs 60–65 of IFRS 15 require a contract with a financing component that is significant to the contract to be separated, which results in the same revenue recognition for both transactions.”

“BC246 The boards decided that an entity should present the effect of the financing (ie the unwinding of the discount) separately from revenue from contracts with customers, as interest revenue or interest expense, rather than as a change to the

measurement of revenue. This is because contracts with financing components that are significant have distinct economic characteristics—one relating to the transfer of goods or services to the customer and one relating to a financing arrangement—and those characteristics should be accounted for and presented separately.”

From the above, the Committee notes that revenue from contracts with customers is based on transaction price, which is the amount of consideration to which an entity expects to be entitled in exchange for transferring promised goods or services to a customer. The nature, timing and amount of consideration promised by a customer affect the estimate of the transaction price. Ind AS 115 provides that while determining the transaction price, an entity shall adjust the promised amount of consideration for the effects of the time value of money if the timing of payments agreed to by the parties to the contract (either explicitly or implicitly) provides the customer or the entity with a significant benefit of financing the transfer of goods or services to the customer. The objective of such adjustment is to recognise revenue at an amount that reflects the price that a customer would have paid for the promised goods or services if the customer had paid cash for those goods or services when (or as) they transfer to the customer (ie the cash selling price). The Committee also notes that the Standard requires an entity to consider all relevant facts and circumstances in assessing whether a contract contains a financing component and whether that financing component is significant to the contract, including: (a) the difference, if any, between the amount of promised consideration and the cash selling price of the promised goods or services; and (b) the combined effect of: (i) the expected length of time between when the entity transfers the promised goods or services to the customer and when the customer pays for those goods or services; and (ii) the prevailing interest rates in the relevant market.

Moreover, as per the ‘Basis for Conclusions’ of IFRS 15, if the entity sells the same good or service for a different amount of consideration depending on the timing of the payment terms, this generally provides observable data that the parties are aware that there is a financing component in the contract and this factor is considered as an indicator of financing component. However, the entity should also evaluate all relevant facts and circumstances considering the requirements of Ind AS 115 while determining whether the contract contains a significant financing component. Further, as a practical expedient, an entity need not adjust the promised amount of consideration for the effects of a significant financing component if the entity expects, at contract inception, that the period between when the entity transfers a promised good or service to a customer and when the customer pays for that good or service will be one year or less.

32. In this context, the Committee notes the relevant clause from Bulk Power Transmission Agreement (BPTA) and regulation 137 of DERC (Terms and Conditions for Determination of Tariff) Regulations, 2017, which provide as follows:

*Bulk Power Transmission Agreement*

**“5.0 TRANSMISSION CHARGES ACCOUNTING**

Monthly Bills towards Transmission Charges for use of the Transmission System shall be raised by the Company on or before 10th day of the subsequent month in accordance with the tariff orders issued by DERC from time to time. The required data for this purpose shall be furnished by State Load Dispatch Centre (SLDC) to the Company up to 7th of every month.

...

Payment of bills by the Beneficiary shall be governed by Clause A.4 of General provisions governing the Agreement (Annexure-A).”

“**A.4 PAYMENT, REBATE, LPSC ETC.**

...

(c) **Due Date:** One month from the date of presentation of bill.

...

(e) **Late Payment Surcharge (LPSC)**

In case the payment of bills of transmission charges is delayed beyond a period of one month from the date of presentation of bill, the Transmission Licensee may levy a late payment surcharge at the rate of 1.25% per month on the unpaid amount from the due date up to the actual date of payment.”

*DERC (Terms and Conditions for Determination of Tariff) Regulations, 2017*

“137. In case the payment of any bill for charges payable under these regulations is delayed by a beneficiary of generating entity or long term transmission customer/DICs as the case may be, beyond a period of 60 days from the date of billing, a late payment surcharge at the rate of 1.50% per month shall be levied by the generating entity or the transmission licensee, as the case may be.”

From the above, the Committee notes that the terms for late payment from the due date of payment are expressly provided in the BPTA or Tariff Regulations, which is binding on both the buyer as well as the Company. The Committee further notes that delayed payment charges are charges to the customers who have not paid the bill by due date; and that such charges are defined in terms of percentage *per annum*, which indicates that the same is directly linked with the passage of time and the quantum of the same depends on timing of payment by the customers and outstanding amount. Thus, the amount of consideration varies due to difference in timing of payments (as the consideration will increase with increase in timing of payment). Therefore, considering the requirements of Ind AS 115 reproduced above, the Committee is of the view that the LPSC is of the nature of financing component and if such component is significant at the contract level, considering the facts and circumstances of the Company and the above-reproduced requirements of Ind AS 115, the Company should separate the same from its transaction price (and consequentially from revenue). However, considering the requirements of paragraph 63 of Ind AS 115 reproduced above, as a practical expedient, if the Company expects, at contract inception, that the period between when it transfers the promised good or service to a customer and when the customer pays for that good or service will be one year or less, it need not make adjustments for the effects of significant financing component while recognising revenue. Accordingly, the Committee is of the view that in the extant case, if the financing component in a contract is significant and the practical expedient is either not applied or the Company expects the period between the transfer of promised good or service to the customers is more than one year, the same shall not be considered as a part of the ‘Revenue’ of the Company. Furthermore, the Company should present the effect of the financing separately from revenue from contracts with customers, as interest income classified within ‘Other Income’.

The Committee further notes that as per the requirements of paragraph 64 of Ind AS 115, when adjusting the promised amount of consideration for a significant financing component, the Company should use the discount rate that would be reflected in a separate financing transaction between it and its customer at contract inception. Thus, the Company should determine the transaction price or cash selling price by adjusting the promised amount of consideration using that discount rate and should recognise revenue and a receivable for that amount. The Company should account for the receivable and interest thereon in accordance with the requirements of Ind AS 109, 'Financial Instruments' (which are based on accrual basis of accounting).

Further, considering that the requirements of paragraph 9(e) of Ind AS 115 relating to collectability of consideration were satisfied at the inception of the contract, as discussed above, the receivables (relating to transaction price and interest thereon) so recognised should be tested for impairment subsequently for uncertainty about collection, as per the following requirements of Ind AS 109:

**“5.5.1 An entity shall recognise a loss allowance for *expected credit losses* on a financial asset that is measured in accordance with paragraphs 4.1.2 or 4.1.2A, a lease receivable, a *contract asset* or a loan commitment and a financial guarantee contract to which the impairment requirements apply in accordance with paragraphs 2.1(g), 4.2.1(c) or 4.2.1(d).”**

“5.1.3 Despite the requirement in paragraph 5.1.1, at initial recognition, an entity shall measure trade receivables at their transaction price (as defined in Ind AS 115) if the trade receivables do not contain a significant financing component in accordance with Ind AS 115 (or when the entity applies the practical expedient in accordance with paragraph 63 of Ind AS 115).”

**“5.5.3 Subject to paragraphs 5.5.13–5.5.16, at each reporting date, an entity shall measure the loss allowance for a financial instrument at an amount equal to the *lifetime expected credit losses* if the credit risk on that financial instrument has increased significantly since initial recognition.”**

**“5.5.5 Subject to paragraphs 5.5.13–5.5.16, if, at the reporting date, the credit risk on a financial instrument has not increased significantly since initial recognition, an entity shall measure the loss allowance for that financial instrument at an amount equal to *12-month expected credit losses*.”**

**“Simplified approach for trade receivables, contract assets and lease receivables**

**5.5.15 Despite paragraphs 5.5.3 and 5.5.5, an entity shall always measure the loss allowance at an amount equal to lifetime expected credit losses for:**

- (a) trade receivables or contract asset that result from transactions that are within the scope of Ind AS 115, and that:
  - (i) do not contain a significant financing component in accordance with Ind AS 115 (or when the entity applies the practical expedient in accordance with paragraph 63 of Ind AS 115); or
  - (ii) contain a significant financing component in accordance with Ind AS 115, if the entity chooses as its accounting policy to measure the

**loss allowance at an amount equal to lifetime expected credit losses. That accounting policy shall be applied to all such trade receivables or contract assets but may be applied separately to trade receivables and contract assets.**

...”

**“Measurement of expected credit losses**

**5.5.17 An entity shall measure expected credit losses of a financial instrument in a way that reflects:**

- (a) an unbiased and probability-weighted amount that is determined by evaluating a range of possible outcomes;**
- (b) the time value of money; and**
- (c) reasonable and supportable information that is available without undue cost or effort at the reporting date about past events, current conditions and forecasts of future economic conditions.”**

From the above, the Committee is of the view that the Company should measure expected credit loss in a way that reflects an unbiased and probability-weighted amount that is determined by evaluating a range of possible outcomes; the time value of money; and reasonable and supportable information that is available without undue cost or effort at the reporting date about past events, current conditions and forecasts of future economic conditions as per the above-mentioned requirements of Ind AS 109.

**D. Opinion**

33. On the basis of above, the Committee is of the opinion on the issues raised in paragraph 28 above that the condition under paragraph 9(e) of Ind AS 115 with regard to collectability of consideration is satisfied in the extant case. Therefore, the Company should account for contract with DISCOMs and accordingly, recognise revenue as per the requirements of Ind AS 115 (which are based on accrual basis and not cash or receipt basis of accounting), as discussed in paragraph 30 above. Further, in case the Company after evaluating the requirements of Ind AS 115 determines that the contract contains a significant financing component, the same should be accounted for as per the requirements of Ind AS 115 and Ind AS 109, ‘Financial Instruments’ as discussed in paragraphs 31 and 32 above. Furthermore, considering that the requirements of paragraph 9(e) of Ind AS 115 relating to collectability of consideration were satisfied at the inception of the contract, as discussed above, the receivables (and interest thereon) so recognised should be tested for impairment subsequently for uncertainty about collection and should measure expected credit loss, as per the requirements of Ind AS 109.