

Query No. 30

Subject: *Accounting treatment of salary paid to Company Secretary of the Company having single unit project under construction, under Ind AS framework.*¹

A. Facts of the Case

1. A company (hereinafter referred to as ‘the Company’) is a Government Company under the administrative control of the Department of Atomic Energy (DAE) incorporated on 22nd October 2003 as Public Limited Company under the Companies Act, 1956 with the objective of constructing and commissioning the first 500 megawatt electrical (MWe) Fast Breeder Reactor (FBR) and to pursue construction, commissioning, operation and maintenance of subsequent Fast Breeder Reactors for generation of electricity in pursuance of the schemes and programmes of Government of India under the provisions of the Atomic Energy Act, 1962.

2. The Company is currently in the stage of integrated commissioning of 500 MWe Prototype Fast Breeder Reactor (hereinafter referred to as ‘the PFBR’ or ‘the Project’). The PFBR is the forerunner of the future Fast Breeder Reactors and is expected to provide energy security to the country. The PFBR is being built with the design and technology developed at the Indira Gandhi Center for Atomic Research (IGCAR) located at Kalpakkam.

It is an infrastructure project by nature, having long gestation period (project construction activities started in 2003), which is under integrated commissioning stage and expected to commission during the financial year (F.Y.) 2024-25. Indian Accounting Standards (Ind ASs) are applicable to the Company from the F.Y. 2016-17 for having net worth Rs. 500 crore or more.

3. *Funding pattern of the Company:* Initial Project cost of the Company was funded with Debt-Equity ratio of 20:80. Equity is in the form of equity share capital from the Government of India (GoI) and N Ltd., a Central Public Sector Undertaking (CPSU) in the ratio of 95:5.

- (i) Initial approved cost - Rs. 3,492 crores.
- (ii) First revised project cost - Rs. 5,677 crores.
- (iii) Second revised project cost - Rs. 6,840 crores.
- (iv) Third revision is under the approval of GoI for Rs. 7,670 crores.

Authorised share capital of the Company is Rs. 5,000 crores and paid-up capital at the end of the F.Y. 2022-23 is Rs. 4,738.20 crores.

¹ Opinion finalised by the Committee on 29.11.2024.

4. *Progress of the Project:* Presently, the Company is in the stage of integrated commissioning of 500 MWe Prototype Fast Breeder Reactor (PFBR). As per the present approval, the Project is expected to be commissioned in the F.Y. 2024-25. The PFBR is single and indigenous Project under integrated commissioning stage, which is first of its kind in India.

5. The querist has stated that from the initial stage of the project construction (F.Y. 2003-04), the Company's accounting policy relating to capitalisation of indirect cost and administration and general overheads till F.Y. 2015-16 is as follows:

“All indirect costs relating to Project are identified and taken to the respective head and if not relatable to any particular head, to ‘Expenditure During Construction (EDC)’. EDC is allocated on pro rata basis to the assets capitalised on commencement of commercial operation”.

6. The Company was following Indian Generally Accepted Accounting Principles (IGAAP) till the F.Y. 2015-16. From the F.Y. 2016-17, the Company is preparing its financial statements as per Indian Accounting Standards (Ind AS) notified under section 133 of the Companies Act, 2013. The accounting policy on indirect cost in Capital Work in Progress (CWIP) is as follows and there is no change in accounting policy till the recent F.Y. 2022-23:

“v) CWIP also includes all indirect costs, all incidental expenses incurred during construction pending allocation.”

“vi) All indirect costs relating to project are identified and taken to the respective *head* and if not relatable to any particular head, to “Expenditure during construction pending allocation” (EDC). EDC is allocated on pro rata basis to the assets capitalised on commencement of commercial operation.”

Note: "head" refers to classification of the asset.

7. During the F.Y. 2020-21, the newly appointed statutory auditors of the Company had a different opinion on the accounting policy followed by the Company on capitalisation of indirect cost and administration and other overhead on the ground that as per paragraph 19 (d) of Indian Accounting Standard (Ind AS) 16, ‘Property, Plant and Equipment’, “Administrative and other general overhead costs are not costs of an item of Property, Plant and Equipment”, and these indirect expenditures should not be part of CWIP and should be debited to the statement of profit and loss.

8. The grounds considered by the Company for capitalising all the indirect and other general administrative costs have been provided by the querist as below:

- (i) As per paragraph 16(b) of Ind AS 16, the element of cost that will be the cost for asset are “any costs directly attributable to bringing the asset to the location and condition necessary for it to be capable of operating in the manner intended by management”. As all the expenditure incurred by the Company is only for the construction and commissioning of PFBR and it does not have any other commercial transaction, all the indirect costs are said to be the capital cost for PFBR.
- (ii) Further Question 10 of Educational Material on Ind AS 16, issued by the erstwhile Ind AS Implementation Committee of the ICAI states that “General overhead costs are not costs of an item of property, plant and equipment unless if it can be clearly demonstrated that they are directly attributable to construction”. The answer to Question 10 above envisages a situation that may demand inclusion of general overhead cost as part of the cost, which is the case of the Company. In the case of the Company, because of self-constructed assets, cost is to be recognised by inclusion of administrative costs and other general overhead costs. Therefore, administrative costs and other general overhead costs become directly attributable to be part of self-constructed assets of the Company.

Based on the above and as the Company is a single unit company, according to the querist, it is evident that these costs are clearly attributable only to PFBR and hence, it should be part of the capital cost.

- (iii) The tariff determination norms notified by the Department of Atomic Energy for sale of electricity generated from fast breeder reactors by the Company to State Electricity Board is based on the approved project cost. Hence, to capitalise the entire project cost, the Company has continued to debit all these costs to the EDC.
- (iv) This issue was discussed during implementation of Ind AS for the F.Y. 2016-17 and the same was accepted by the then internal, statutory and the Comptroller and Auditor General of India (C&AG) auditors and by the auditors of the succeeding years also.

However, from the F.Y. 2020-21, the current statutory auditors of the Company based on the explanation of the Company, have included an “Emphasis of Matter Paragraph” in their Independent Audit Report but have not modified their opinion on the same. The specific issue that has been referred by the querist for consideration and opinion of the Expert Advisory Committee (hereinafter referred to as ‘the Committee’) is on accounting treatment of salary paid to Company Secretary of the Company, which is elaborated as below.

9. The querist has informed that the Company Secretary is working at corporate office along with one staff. The Company has offices at two places, viz., Plant site office and the Corporate

office. Salaries paid to corporate office employees are debited to 'Expenditure During Construction (EDC) Account'. Secretarial office at corporate office is taking care of all secretarial works.

B. Query

10. Whether the accounting treatment followed by the Company on capitalisation of salary paid to Company Secretary of a single unit project (where the tariff will be fixed based on the approved project cost) is consistent with the Ind AS. If not, kindly suggest the correct accounting treatment.

C. Points considered by the Committee

11. The Committee notes from the Facts of the Case that the specific issue raised in the query read with the related clarificatory correspondence from the querist relates only to the accounting treatment of 'salary paid to Company Secretary', who is working at the corporate office of the Company, during the project construction period. The Committee has, therefore, considered only this issue and has not examined other issues that may arise from the Facts of the Case, such as, accounting for equity share capital received from GoI and N Ltd., accounting under the previous GAAP and at the time of transition to Ind ASs, appropriateness of accounting policy followed by the Company with regard to indirect costs, administrative costs and overheads, accounting for any other expenses incurred by the Company in relation to the project, impact of project costs incurred on tariff determination, appropriateness of views expressed or reporting or opinion by the auditor etc. Further, 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. The opinion expressed hereinafter is purely from accounting perspective and not from the perspective of legal interpretation of various legal enactments, such as, the Atomic Energy Act, 1962, tariff determination norms, etc.

12. At the outset, the Committee notes from the facts that the tariff rules set by the Department of Atomic Energy for selling electricity from fast breeder reactors are based on the approved project cost. In this regard, the Committee wishes to mention that the elements of cost that may be relevant for computing the approved project cost for the purposes of determining tariff, will not necessarily impact the accounting for the elements of cost which are to be considered in determining the cost of the Property, Plant and Equipment to be capitalised which will be as per the requirements of the relevant accounting framework (Ind ASs in the instant case) only. The Committee also wishes to mention that various expenses are incurred during construction period. However, it is not necessary that each expense incurred during construction is eligible to be capitalised to the project/asset being constructed. Similarly, just because the only activity undertaken by the Company at present is the construction activity does not mean that every expense incurred by the Company is directly linked or attributable to the construction activities. The capitalisation of an item of cost to an asset/project depends upon the nature of such expenses in relation to the construction/ acquisition activity in the

context of requirements in this regard laid down in the applicable Indian Accounting Standards (Ind ASs).

13. In this context with regard to the specific issue of accounting for the salary paid to the Company Secretary, the Committee notes the following paragraphs of Ind AS 16, 'Property, Plant and Equipment', notified under the Companies (Indian Accounting Standards) Rules, 2015:

“16 The cost of an item of property, plant and equipment comprises:

- (a) its purchase price, including import duties and non-refundable purchase taxes, after deducting trade discounts and rebates.
- (b) any costs directly attributable to bringing the asset to the location and condition necessary for it to be capable of operating in the manner intended by management.
- (c) the initial estimate of the costs of dismantling and removing the item and restoring the site on which it is located, the obligation for which an entity incurs either when the item is acquired or as a consequence of having used the item during a particular period for purposes other than to produce inventories during that period.

17 Examples of directly attributable costs are:

- (a) costs of employee benefits (as defined in Ind AS 19, *Employee Benefits*) arising directly from the construction or acquisition of the item of property, plant and equipment;
- ...
- (f) professional fees.”

“19 Examples of costs that are not costs of an item of property, plant and equipment are:

- ...
- (d) administration and other general overhead costs.”

14. From the above, the Committee notes that the basic principle to be applied while capitalising cost to an item of a property, plant and equipment (PPE) is that it is directly attributable to bringing the asset to the location and condition necessary for it to be capable of operating in the

manner intended by management. The Committee is of the view that ‘directly attributable’ costs are generally such costs which are necessary to enable the construction activity, i.e. these costs are directly related to the construction activity and without the incurrence of which the asset cannot be brought to the location and condition necessary for it to be capable of operating in the manner intended by management. Accordingly, an expenditure incurred by the Company can be capitalised only if it is directly attributable to bringing the project or the related PPE(s) to the location and condition necessary for it/them to be capable of operating in the manner intended by the management.

The Committee further notes that paragraph 17 of Ind AS 16 gives examples of directly attributable costs and it includes costs of employee benefits (as defined in Ind AS 19, ‘Employee Benefits’) arising directly from the construction or acquisition of the item of property, plant and equipment. Further, as per paragraph 19 of Ind AS 16, administration and other general overhead costs are examples of the costs that are not costs of an item of property, plant and equipment.

Accordingly, the Committee is of the view that the employee benefit costs *arising directly from the construction or acquisition* of the Project/PPE, such as, employee benefit costs of workers, engineers, architects, etc. engaged in construction activity should only be considered as directly attributable costs and capitalised with the Project/PPE. In the extant case, the Company Secretary is working at corporate office along with one staff and is taking care of all secretarial work (which normally include preparing and keeping important documents and records, such as minutes of the meetings of Board of Directors, AGM, etc. and ensuring legal and regulatory compliances of the Company) and is not involved or engaged in the construction activities as such. Further, irrespective of whether the Project is under construction or not, the services of the Company Secretary will still be required and thus, the related expenses would still be incurred. Therefore, the salary paid to him cannot be considered to be *directly attributable* to bringing the PPE (PFBR) or Project to the location and condition necessary for it to be capable of operating in the manner intended by the management. Hence, it cannot be capitalised along with the cost of the Project/PFBR; rather it should be charged to the Statement of Profit and Loss as and when incurred.

D. Opinion

15. On the basis of the above, the Committee is of the opinion that salary paid to Company secretary cannot be capitalised along with the cost of the Project/PFBR; rather it should be charged to the Statement of Profit and Loss as and when incurred, as discussed in paragraphs 13 and 14 above.
