Query No. 28

Subject: Accounting treatment of expenditure incurred on Complete Track Renewal (CTR), Additional Waterways, Deep Screening, Doubling after initial capitalisation etc. on the Project under the Service Concession Arrangement. [1]

A. Facts of the Case

1. *Background of Company and Transaction Details*

(i) A company (hereinafter referred to as 'the Company') is a public limited company incorporated in India on January 22, 2004, as a Special Purpose Vehicle (SPV) for the gauge conversion of the existing 301 km railway line between Gandhidham and Palanpur in Gujarat. The Company operates as a Joint Venture between R Limited, AP Ltd., D P Authority, and the Government of Gujarat.

(ii) The Company entered into a Concession Agreement dated 8th November 2005 with the President of India, represented through the Executive Director (Perspective Planning), Ministry of Railways (MoR), Government of India. Under this Agreement, the Ministry of Railways (Grantor) authorised the Company (Operator) to develop, finance, design, engineer, procure, construct, operate, and maintain the Project Railway, while exercising the rights, powers, benefits, privileges, authorisations, and entitlements specified therein throughout the concession period.

(iii) The Project, as defined in Clause 1.1 of the Concession Agreement, encompasses the Gauge Conversion along with all associated activities for development, financing, construction, operation, and maintenance of the Project Railway.

(iv) Project Railway as defined in clause 1.1 of Concession Agreement means broad gauge rail link connectivity between Palanpur at Km 0 and Gandhidham at Km 300.81.

(v) The concession is hereby granted for a period of 32 (Thirty-Two) years, commencing on the Appointed Date, or such extended period as provided for in this Agreement, unless terminated earlier.

(vi) In terms of above Agreement, concession period of the Company is 32 years from Appointed Date, which means the date of signing Concession Agreement i.e. 8th November 2005.

(vii) As per clause 4.3 of Concession Agreement, the Company is under obligation:
"to keep the Project Assets in a proper working condition, including making replacement in accordance with the standards laid down by MoR, of all Project Assets whose lives have expired. Such replacement shall be carried out by the Company either by itself or through MoR, and the costs of such replacements shall be borne by the Company".

(viii) Upon the expiry of 32 years as provided, the concession period shall be extended by an equal period of time which corresponds to the period for which material disruption of operations and maintenance occurred during the concession period.

[1] Opinion finalised by the Committee on 11.04.2026.

(ix) Transfer of Project

Clause 5.1 of Concession Agreement provides that "Upon Expiry, the Project Assets shall be handed over by the Company to MoR in accordance with provisions of Article 8."

Clause 8 of Concession Agreement provides:

"8.1 Transfer Payment on Normal Transfer

Upon Normal Transfer, the Company shall be entitled to receive and MoR shall pay to the Company an amount equal to Book Value. The Existing Assets leased to the Company by MoR shall revert back to MoR without any financial consideration.

8.2 Transfer payment on Termination on Account of Concessioning Authority's Event of Default

Upon Termination on account of Concessioning Authority's Event of Default, the Company shall be entitled to receive and MoR shall pay the following as Transfer Payment:

a. 130% of DRV if the default occurs within 15 years of COD.
b. 120% of DRV if default occurs after 15 years but within 25 years of COD.
c. 110% of DRV if the default occurs after 25 years of COD.

8.3 Transfer Payment on Termination on Account of Concessionaire's Event of default

Upon Termination on account of Concessionaire's Event of Default, the Company shall be entitled to receive and MoR shall pay 50% of Book Value as Transfer Payment."

Clause 1.1

""**DRV"** means depreciated replacement value of New Assets and Additional Facilities and is the aggregate cost of replacing each asset on Termination Date minus aggregate depreciation on straight line method, where depreciation on straight line method for each asset means the number of years the asset has been in use divided by the codal life of the asset multiplied by the cost of replacement of asset on Termination Date. The asset life shall be computed as per the provisions in the codes and manuals of the MoR. Where the life of an asset is not mentioned in the MoR codes/manuals, it shall be decided mutually between MoR and the Company. The cost of replacement of each asset shall be determined by the then prevailing accepted rate for the relevant assets of MoR."

(x) In case of material breach in terms of the agreement, the MoR and the Company, both have the right to terminate the agreement if they are not able to cure the event of default in accordance with such agreement. Transfer payment in case of default is also defined in clause 8 of Concession Agreement.

(xi) The operation and maintenance of the project railway is being carried out by the Ministry of Railways (MoR) through Western Railway (WR) under its rights pursuant to the agreement dated 21 August 2007, which is co-terminus with the Concession Agreement entered into between; 'The President of India, acting through its nominated agency WR', and the Company. In accordance with this agreement, WR is responsible for operating and maintaining the Project

Railway from Gandhidham to Palanpur, covering a total distance of 300.81 km, and the Company is required to pay the O&M costs to WR.

(xii) The above transaction, according to the querist, falls within the scope of *Service Concession Arrangements* under Appendix D to Ind AS 115, 'Revenue from Contracts with Customers' and accordingly, the related assets are recognised as intangible assets at the fair value of the services provided together with other directly attributable costs of operation and are amortised over the remaining term of the concession.

(xiii) As per the querist, revenue related to construction or upgrade services under a service concession arrangement is recognised based on the stage of completion of the work performed, when the outcome of construction contract can be measured reliably and where the outcome of construction contract cannot be measured reliably, revenue is recognised only to the extent of contract cost incurred that is probable to be recoverable. Performance obligation is measured by the Company on the basis of inputs to the satisfaction of a performance obligation (i.e. Input Method). Therefore, only cost incurred is recognised as Intangible Assets.

(xiv) A letter was received during the financial year (F.Y.) 2022-23 wherein it was stated that Railway has been doing TRR/CTR (complete track renewal) works regularly for the stretches which were required from maintenance point of view. It was also informed that Railway has done casual renewal of rails in SIOB-GIMB section of the Company's line. In this letter, it has been appraised to the Company that in SIOB-GIMB section of the Company's line, the track structure is 52 kg rail and 60 kg sleeper with 1540 sleeper density and GMT of rail in most of this section has already surpassed its service life. Hence, CTR works needs to be done on priority to avoid any safety hazard on this account. As the Company serves as a feeder route to the Dedicated Freight Corridor (DFC), it has been informed to the Company that, in line with Railway Board advisories, upgradation of DFC feeder routes, removal of operational constraints, and timely sanction and execution of necessary works under the relevant plan heads are essential to meet the target of Mission 3000 MT. Therefore, it is not pragmatic to impose speed restriction in SIOB-GIMB section of the Company. It will also act as an impediment to meet the target of Mission 3000 MT as advised by Railway Board.

2. ***Complete Track Renewal (CTR) and Additional Waterways, Deep Screening etc.***

(i) It is evident from reading of above that Railway is proposing to replace the rails and sleepers with its fitting components to 60 kg from current 52 kg.

(ii) The Company is required to incur various expenditure in order to keep its project in working condition; also, the Company had to create various new facilities for project assets as and when their need arises.

(iii) The said work will take 3-4 years to conclude, and as the work progresses, Railway will advise the actual expenditure of the work to the Company accordingly. The detailed estimate will be advised by Western Railway after obtaining principal approval from the Company for CTR work in SIOB-GIMB section of the Company's line.

(iv) The Company has received demand from Railway for following expenditure:

(Rs. in Crore)

S No.	Details	Total demand	Amount Capitalised as Intangible or intangible under development
1.	CTR work for 133.56 km (Palanpur–Samakhyali and Samakhyali–Gandhidham sections)	376.87	75.59
2.	Deep Screening, Waterway, Casual Renewal, TFR (Through Fastening Renewal) etc.	136.86	81.00
3.	CTR of PNU-SIOB down line not consented by the Company	258.75	-
	Total	**772.48**	**156.59**

(v) Above expenditure of Rs. 156.59 crore incurred by the Company has been recognised as Intangible Assets/Intangible Assets under development in financial statements and amortised/proposed to be amortised over the remaining concession period.

(vi) Following disclosure has been made by the Company in its financial statements:

"Resurfacing /replacement Cost

As per Ind AS 115, the operator may have contractual obligations, it must fulfil as a condition of its license (a) to maintain the infrastructure to a specified level of serviceability or (b) to restore the infrastructure to a specified condition before it is handed over to the grantor at the end of the service arrangement. These contractual obligations to maintain or restore infrastructure, except for any upgrade element shall be recognised and measured in accordance with Ind AS 37 Provision, i.e. at the best estimate of the expenditure that would be required to settle the present obligation at the end of the reporting period.

In terms of Concession Agreement, there is an obligation on the Company to keep the project assets in working condition, including replacement, as per laid down standards of MoR, for project assets, whose codal lives expire during the concession period. Accordingly, Company is required to provide for in respect of replacement obligations arising during the remaining concession period as per requirement of Ind AS 115 for best estimate of expenditure required to settle obligation.

The Company has made an assessment in respect of its project assets and their respective codal lives. Assets items like rails, sleepers, foundation, bridges and buildings, station buildings have longer lives and most of it would be having remaining codal lives at the end of concession period. The replacement of these are planned on the basis of the condition assessed by the Railways.

The Company has received a cost estimate of Complete Track Renewal (CTR) work amounting to Rs. 376.87 crores from the Railways, however details about year-wise expenses to be incurred are not available as on 31st March 2025, therefore provision for same is not provided in financial statements. The Company is following up with the Western Railway for getting estimated cost and the period over for CTR activities and accordingly on the basis of data availability, will provide the necessary provisions while finalising the accounts in the subsequent financial year."

(vii) During supplementary audit by C&AG under section 143(6)(a) of the Companies Act, 2013, they made the following observation.

3. *Observations made by C&AG:*

The C&AG of India has made the following observations/comments on the accounting treatment of above items as follows:

Observation on CTR and Additional Works and Management Reply to Observation of C&AG

a. <u>Observation</u>
<u>"Comments on Profitability</u>

Statement of Profit and Loss

Expenses - ₹ 1,39,015.80 lakh

Profit of the year – ₹ 1394.01 lakh

Balance Sheet

(d) Intangible assets under development- Note-6- ₹ 17,800 lakh

(b) Provisions- Note No. 15 – ₹ 277.99 lakh

(i) As per Clause 4.3(d) of the Concession Agreement (November 2005) with MoR, the Company is obliged to keep project assets in working condition, including replacement of expired assets, in accordance with MoR standards. Further, as per IRPWM (paragraph 702(d)), rails are required to undergo Complete Track Renewal (CTR) after specified traffic limits.

Western Railway (October 2022 and May 2023) has already raised demands for CTR works, against which the Company consented (October 2022 and July 2023) to expenditure of ₹ 376.87 crore for 133.56 km (Palanpur–Samakhyali and Samakhyali–Gandhidham sections). Further, the Company has also estimated ₹136.86 crore for works over and above the O&M which has also not been provided by the Company. Additionally, in February 2025, WR raised a demand for CTR of 91.70 km (PNU–SIOB down line) requiring funds of ₹ 258.75 crore. Thus, the total CTR fund requirement as on 31.03.2025 works out to ₹ 772.48 crore. Out of this, the Company has already incurred and capitalised an amount of ₹ 156.59 crore (₹ 75.59 crore + ₹ 81.00 crore) under the head 'Intangible Assets under development'.

Thus, due to not providing for the replacement obligations arising during the remaining concession period in violation of Ind AS 115, the 'Provisions' has been understated by ₹ 615.89 crore (₹ 772.48 crore - ₹ 156.59 crore) and overstatement of 'Profit for the period' to the same extent.

(ii) Further, the expenditure of ₹ 156.59 crore (₹75.59 crore + ₹ 81.00 crore) should have been charged to Profit and loss since as per the Concession Agreement of the Company with the Railways, the Company has no ownership of the railway infrastructure assets created by it. The expenditure incurred on CTR work would not result into any additional rights/ intangible assets to the Company. Therefore, it should have been charged to the Statement of Profit and Loss as expenses instead of booking the same as intangible assets. The same is in violation of Appendix D of Ind AS 115 – Revenue from Contracts with Customers.

This has resulted in overstatement of 'Intangible Assets under development', understatement of 'Expenses' by ₹ 156.59 crore and overstatement of Profit for the year' to the same extent."

b. <u>Management Reply to observation of C&AG</u>

"With reference to the audit observation, the Company respectfully submits the following:

i. Contractual Framework under Concession Agreement

- In terms of Clause 4.3(d) of the Concession Agreement with Ministry of Railways (MoR), the Company is required to ensure that the project assets remain in working condition, including carrying out replacements on expiry of codal life, in line with MoR standards.
- The revenue mechanism under the Concession Agreement envisages that payments to the Company are net of O&M expenditure, including CTR. Western Railway (WR) identifies, executes and certifies such works and their costs, following which the same are recognised in the Company's books. Provisioning without such confirmation would not be in consonance with the agreed framework.
- Further, O&M including renewals and special works are determined by WR based on traffic density and track condition. Hence, the Company cannot independently determine the requirement until WR assesses and communicates the same.

ii. Practical Aspects of CTR Works

- CTR works are highly complex field operations involving replacement of rails, sleepers and ballast under running train conditions, necessitating imposition of speed restrictions and phased execution over small stretches.
- For CTR works consented by the Company, WR has proposed upgradation of track standards (60 kg/m rails of 90 UTS in place of 52 kg/m rails of 72 UTS; heavier and wider PSC sleepers; reduced spacing to enable higher axle loads).
- While granting consent, the Company requested WR to restrict procurement to annual requirements and provide year-wise fund requirements. However, such details have not yet been furnished. Presently, WR is deducting ₹6 crore per month from the Company's revenue bills towards the CTR works.

iii. Applicability of Ind AS 115, 'Revenue from Contracts with Customers' and Ind AS 37, 'Provisions, Contingent Liabilities and Contingent Assets'

- Paragraph 21 of Appendix D to Ind AS 115 requires obligations relating to maintenance/restoration of infrastructure under concession arrangements to be accounted for as per Ind AS 37.
- Ind AS 37, paragraph 14 allows recognition of provision only where (a) a present obligation exists, (b) probable outflow of resources is expected, and (c) a reliable estimate can be made.
- Although the Company acknowledges its obligation, reliable year-wise estimates from WR are not presently available for all CTR works. Moreover, credit from disposal of scrap material from replaced track components also remains unascertained.

iv. Current Status of CTR Works and additional works (deep screening, waterways, etc.)

- The Company has consented to CTR works of 133.56 km aggregating to ₹376.87 crore (₹234.00 crore in October 2022 for PNU–SIOB section and ₹142.87 crore in July 2023 for Samakhiali–Gandhidham section).
- Against this, expenditure of ₹75.59 crore has been incurred and capitalised under 'Intangible Assets under Development' up to 31.03.2025.
- In February 2025, WR raised a further demand of ₹258.75 crore for CTR of 91.70 km on the PNU–SIOB down line. This is still under consideration and has not yet been formally accepted by the Company and hence does not meet the recognition test of Ind AS 37.

- Additional works estimated at ₹136.86 crore (deep screening, waterways, etc.) have been disclosed, of which ₹81.00 crore has been incurred and capitalised; the balance will be accounted for on completion.
- The Company has also spent lot of money on Doubling and Railway Electrification (discussed in subsequent paragraphs) and there are CTR demands from WR, if these amounts spent are charged to Statement of Profit and Loss, the net worth of the Company will be eroded and the credit rating of the Company will be affected. The Company considers these works are of capital expenditure; the works when completed will be capitalised for the remaining period of concession period and if the concession period of the Company is extended, the capitalisation shall be made upto the extended period of concession period.

v. Disclosures in Financial Statements

- Note 49 to the financial statements discloses that while a cost estimate of ₹376.87 crore has been received, detailed year-wise expenditure breakup is not available as on 31st March 2025. Accordingly, provision has not been made. The Company is in correspondence with WR and will recognise necessary provisions in subsequent financial years based on confirmed data.
- Expenditure already incurred (₹75.59 crore) has been capitalised under 'Intangible Assets under Development' and will be transferred to 'Intangible Assets' and amortised over the concession period upon completion.
- Capital commitments for CTR have been disclosed in Note 37.

vi. Future Course of Action

- The Company is actively pursuing WR for year-wise requirement of funds and project timelines and will provide appropriate provisions on receipt of such reliable estimates.
- The Company will appoint a technical person for consultation with MoR and Western Railway to ascertain the estimated cost and the period over the CTR activities are to be carried out and accordingly based on the total life of an asset beyond the existing concession period, shall provide for the necessary provisioning in the financial statement of subsequent financial year.
- Additionally, it may be noted that the sister concern of the Company has already sought an opinion from the Expert Advisory Committee (EAC) of the Institute of Chartered Accountants of India (ICAI) on a similar matter. The Company will rely upon the outcome of this EAC opinion and apply the same approach to ensure consistency in accounting treatment.

vii. Conclusion:

As of 31.03.2025, only expenditure of ₹75.59 crore has been incurred on CTR and capitalised under 'Intangible Assets under Development'. Reliable estimates for the balance works are not presently available, and hence, no provision has been recognised. The Company has made appropriate disclosures and will recognise provisions in subsequent years based on confirmed estimates and guidance, including the forthcoming EAC opinion.

In view of the above submissions and the proactive steps being taken, the audit is requested to kindly drop the provisional comment."

4. Further Points for consideration by EAC:

In this whole issue along with reply submitted to C&AG, the Company further submits the following for the consideration of EAC:

(i) Expansion plan of Deendayal Port, Tune Port, Mundra Port and new Port of Jakhau developing in Kutch region:

(a) As per information available, an investment worth ₹ 27,000 crore has been announced by the Union Minister of Ports, Shipping & Waterways during current year as a major initiatives to boost the additional capacity at Deendayal Port Authority (DPA) at Kandla for development of new cargo terminal which will add an additional 135 MTPA capacity to the Kandla.

(b) The DPA is also working on a number of other projects on mission mode to enhance capacity of Kandla Port significantly. A new mega cargo terminal with a capacity of 2.19 million TEUs is being constructed at Tune Tekra. A new Multi cargo terminal at Tune Tekra is also under consideration. This will add 18.33 MTPA to the existing capacity. 03 new oil jetties are in the process of being constructed and it will further add 10 MTPA capacity.

(c) Mundra Port's development includes a major expansion of its container handling capacity. The Port is also undergoing a significant broader expansion to become the largest container port in India with a target of 6.6 million TEU capacity. A new terminal is being developed at Mundra Port. This expansion is intended to position Mundra as a major transshipment hub for the Middle East, South Asia and India.

(d) A new BG rail line connecting to new Jakhau Port in Kutch region is under construction and it is connecting with Naliya-Jhakau section. It is expected to be completed by March 2026 with an estimated cost of ₹ 410.46 crore which will integrate new Jakhau Port with the IR network as recently multiple projects approved by the Union Cabinet for Kutch district in Gujarat. The approved works include new corridors for Desalpur-Hajipar-Lune spanning 81.77 km and Vayor-Lakhpat covering 62.69 km. These will be complemented by the 24.65 km extension of Bhuj-Naliya line upto Vayor and a 24.88 km link from Naliya to new Jakhau Port. Together the projects involve an investment of around ₹ 3375 crore in Kutch region. Multiple developments are taking place in Kutch region, which will further generate additional traffic (e.g. cement, bentonite clay, limestone, bulk mineral, etc). The Company's line is expected to gain significantly from these developments in coming years.

(e) As Gujarat ports are fast emerging destination ports in India, large scale investment is in the pipeline for expansion of Mundra Port, Deendayal Port and Tune Port at Kandla. The Company's project line is a key feeder route for these ports and accordingly, the traffic volume will also increase.

(f) Due to increasing track capacity, the Company is expecting that annual turnover of revenue apportionments will be generating to the tune of ₹1250 crore during current F.Y. 2025-26 as compared to previous fiscal (F.Y.) 2024-25 of ₹ 1132 crore leading to significant growth of revenue in double digit by over 10%.

(ii) The following benefits are anticipated from the CTR and other incidental works:

(a) The Company's line is a feeder route of WDFC, which is carrying higher throughput with line capacity (120 trains each way) and axle load (25 tonnes) and connecting the Company's Chadotar (CECC) and Palanpur (PNU) stations with its New Chadotar station (CDQN) and New Palanpur (PNUN) station respectively.

(b) Beyond the Company's section, all connecting track structure towards Mundra Port and Deendayal Port/Kandla are being upgraded for carrying 25 tonnes axle load with 60 kg rail and wider and heavier 60 kg sleepers in view of carrying higher axle load.

(c) Annual GMT of the Company's section is nearly 42 GMT as per current F.Y. 2024-25. If one considers it for remaining concession period upto F.Y. 2037-38 (i.e. for balance 13 years), it comes to 42 x 13 = 546 GMT, which means the Company is again required to carry out track renewal if using 52 kg rail/sleeper during its final stage of concession period as it has service codal life of 525 GMT only. Accordingly, the Company has to bear again the cost of track renewal if not using 60 kg rail and 60 kg wider and heavier sleeper which has codal life of 800 GMT.

(d) Codal life of new asset/upgraded track will be beyond the concession period of the Company. In case concession period is not extended by MoR, the Company will get credit of residual value towards the new assets created by the Company.

(e) 25t axle load carries 12-17% more load per wagon than older 22.9 to system. Bulk goods like coal, cement, fertilizers and double stack container trains can be handled with increased capacity and high efficiency in movement of freight trains.

(f) Higher speed enables faster movement of freight trains upto 100 kmph on upgraded track resulting into increase of line capacity for running more trains and meets growing demand for heavy freight transport.

(g) As per Railway Board policy letter No. 2013/Tk-II/22/2/2Pt.II dated 09.07.2018, use of wider and heavier Sleeper (RT-8527) has been planned from F.Y. 2019-20 onwards in IR.

(h) Track renewal standard for 60 kg rail and 60 kg wider and heavier sleeper will provide service codal life of 800 GMT which will be adequate to smoothly maintain during remaining concession period efficiently and residual value will be credited to the Company.

(i) Since the Company's line is notified as DFCC[2] feeder route, track renewal is required to be done to make it fit for running of 25t axle load trains as per Railway Board letter No.2013/CE-II/TS/DFC (Feeder Route) dated 20.07.2018 wherein guidelines was issued that all zonal railways shall make all-out efforts to provide

2 Dedicated Freight Corridors (DFCs) in India are designed for significantly higher axle loads than regular tracks, primarily supporting **25-tonne axle loads**, with some infrastructure, like bridges, even built for **32.5-tonne axle loads**, allowing for heavier, longer freight trains, double-stack containers, and greater efficiency compared to standard Indian Railways' 22.8t (or less) systems, boosting freight movement capacity.

track structure on DFCC Feeder Routes and other notified/identified 25t routes fit for running of 25t axle load trains at the earliest.

(j) Upgrading track structure to 25 t axle load, the speed of freight trains can be increased from existing 30-40 kmph to 100 kmph resulting in line capacity of the Company's section to increase further and more trains can be accommodated.

(k) Railway is enhancing carrying capacity of all type of wagons towards running higher axle load and generating more revenue with less maintenance cost via operating on track structure of 25 t axle load.

(l) After through track renewal, when the track has been upgraded to 60 kg 90 UTS rail, wide-based heavy sleepers, 300 mm ballast cushion, improved rubber pad and mark v-ERC, the life of fittings is supposed to be matching with life of rail. Therefore, in future, there should not be any necessity of through fitting renewal (TFR) and fitting renewal will remain casual renewal only.

(m) The Company is getting advantage by operating more number of trains towards WDFC routes with heavier traffic load (e.g. coal traffic, double stack container, etc.). Currently, more than 50% container rakes are running as double stack container trains, which resulted into increase of container revenue.

(n) Reduction in maintenance cost, enhancing safety and efficiency for higher axle loads (like 25T axle loads). Enhanced frame resistance again buckling and better gauge maintenance.

(iii) Expenditure incurred by the Company towards CTR is up-grade to the infrastructure and not only replacement/maintenance of existing infrastructure; therefore in accordance with requirements of Ind AS 115 and accounting policy of the Company, it has recognised expenditure incurred as Intangible Assets in its financial statements based on principles as stated above. The expenditure incurred by the Company is going to provide benefit in terms of increase in capacity of tracks by operating higher load, and therefore, number of trains shall also increase on track and result in traffic (e.g. Double stack container coal- Traffic, etc.) and increased revenue.

(iv) In olden days, at the time gauge conversion was done by the Company, fittings had a limited life and through fitting renewal (TFR) i.e. renewal of pads and ERC was undertaken at the periodicity of 5-10 years depending on the traffic density.

However, after through track renewal, when the track has been upgraded to 60 kg 90 UTS rail, wide based heavy sleepers, 300 mm ballast cushion, improved rubber pad and mark v-ERC, the life of fittings is supposed to be matching with life of rail. Therefore, in future there should not be any necessity of through fitting renewal (TFR) and fitting renewal will remain casual renewal only. This is additional benefit of CTR i.e. future expenditure shall decrease.

(v) The Company is expecting additional benefits of ₹4,000 crore from doubling and ₹3,000 crore from electrification. Accordingly, the benefits of the CTR should be read in entirety, as they form part of the overall changes undertaken by the Company in anticipation of increased traffic at the Port.

(vi) As stated above, the Company is required to keep assets in working condition. Currently, the Company has not made any provision in this respect. The Company has received and sanctioned a cost estimate of CTR amounting to Rs. 376.87 crores for the railways line and the Company has incurred an expenditure amounting Rs. 75.59 crore upto 31st March 2025 towards CTR.

(vii) Further, after reviewing the progress of the CTR work, it should be understood that total work sanctioned in the year 2022 is for Rs. 376.87 crore, out of which only work of Rs. 142.87 crore for 53 km GIM-SIOB section has yet started and only funds amounting Rs. 58 crore have been deposited by the Company so far, and CTR work of 80 km PNU-SIOB of Rs. 234 crore has not yet started. This indicates a significant delay in the execution of CTR work by Western Railway.

(viii) Track was laid with 60 kg sleeper although the rail was 52 kg with the clear understanding that in future if rail is required to be upgraded to 60 kg during the concession period, it should be possible to change the rail without need of changing the sleepers. In instant case, rail replacement became due on GMT basis but sleeper replacement was not due either on the GMT basis or on condition basis. The codal life of PSC sleepers is 50 years irrespective of the GMT. Western Railway has taken a decision to pre-maturely replace the sleepers, perhaps with the intention of upgrading the track to the standard of DFCC feeder route. Any premature replacement has to be justified based on the increased earnings and therefore, will be charged to capital. It may be noted that it is possible to operate 25 tonne axle load even on older design sleepers and several of the Indian railway feeder routes, sleepers have not been changed with the modern wide based sleepers. The Company agreed for premature replacement of sleepers because it was necessary to change the sleepers density also and changing the sleeper density is time-consuming and labour-consuming task. Increased traffic density justified premature change of sleeper on capital account.

(ix) Deep Screening and Through Fitting Renewal (TFR) if done in a routine manner is a maintenance activity and will be the part of Western Railways maintenance cost. However, in the present case, deep screening and Through Fitting Renewal has been done alongwith CTR with increased ballast cushion, upgraded ballast profile and improved fittings. This will provide longer benefits as compared to existing benefits.

(x) The expenditure incurred by the Company has also enhanced the connectivity and freight transportation contributing to sustainable long-term revenue generation in Kutch, Patan and Banaskantha districts of Gujarat alongwith Kandla, Tune and Mundra ports with savings in cost.

(xi) It is also estimated that at the end of concession period (if not extended) then the physical assets created due to above expenditure shall have significant life remaining (e.g. sleepers 40 years) and the Company will be able to receive significant amount at the time of transfer as stated in Concession Agreement.

(xii) It is also submitted that the Company is of the view that at the end of original concession period, assets created under original Concession Agreement may be transferred at book value, however additional assets created shall be transferred at depreciated replacement value.

(xiii) In accordance with terms of original concession arrangement, the Company was getting fair share of its revenue and was not required to carry any of the work including doubling, electrification, CTR etc. However, the Company has amended its concession agreement and carried out all of these works since all of these expenditures are going to provide additional benefit, i.e., return on additional investment made by the Company.

(xiv) The Company has capitalised the expenditure incurred upto 31st March 2025 under 'Intangible Assets under Development/ Intangible Assets' on the grounds that this expenditure relates to the enhancement of the project assets constructed under the Concession Agreement. Further, as stated above, as the Company has submitted a request to the Railway Board requesting an extension of the concession period by at least 15 years, the expected future benefits of such works are anticipated to extend over a longer duration, supporting capitalisation under Appendix D to Ind AS 115.

(xv) The Company believes that the benefits arising from such works—such as reduced operating costs and improved rail operations—accrue over the entire concession period and are not confined to a single financial year. Therefore, charging the entire expenditure to the Profit and Loss Statement in one year would not reflect the underlying economic substance, and accordingly, the amount has been capitalised as an Intangible Asset in accordance with Appendix D to Ind AS 115.

(xvi) Expenditure incurred by the Company towards electrification, doubling, CTR, waterways etc. is up-grade to the infrastructure and not only replacement/maintenance of existing infrastructure. Therefore, in accordance with requirements of Ind AS 115 and accounting policy of the Company, it has recognised expenditure incurred as Intangible Assets in its financial statements based on principles as stated above. The expenditure incurred by the Company is going to provide benefit in terms of increase in capacity of tracks by operating higher load; therefore, number of trains shall also increase on track and result in traffic (e.g. Double stack container coal- traffic, etc.) and increased revenue.

(xvii) As per Indian Railway practice, any accommodation work or additional waterway, drainage etc. need of which was present even at the time of Project implementation has to be charged to capital.

(xviii) In olden days, at the time gauge conversion was done by the Company, fittings had a limited life and through fitting renewal, i.e. renewal of pads and ERC, was undertaken at the periodicity of 5-10 years depending on the traffic density.

However, after through track renewal, when the track has been upgraded to 60 kg 90 UTS rail, wide-based heavy sleepers, 300 mm ballast cushion, improved rubber pad and mark v-ERC, the life of fittings is supposed to be matching with life of rail. Therefore, in future there should not be any necessity of through fitting renewal (TFR) and fitting renewal will remain casual renewal only.

(xix) Deep screening and Through Fitting Renewal if done in a routine manner is a maintenance activity and will be the part of Western Railways maintenance cost. However, in the present case, deep screening and Through Fitting Renewal has been done alongwith CTR with increased ballast cushion, upgraded ballast profile and

improved fittings. As has been explained in case of sleepers, the upgradation element has to be charged to the capital.

5. *Doubling and Electrification Works after initial capitalisation*

(i) As per the Addendum to the Concession Agreement, dated 26.10.2020 between Ministry of Railways and the Company, Project Railway means broad gauge rail link between Palanpur at KM 0 and Gandhidham at KM 300.81 including Double line from Palanpur (KM 0) to Samakhyali (KM 247.73), all loops and other traffic facility works. This also includes all Railway Electrification works on Project line from Gandhidham (KM 300.81) and Samakhyali (KM 247.73) and double line from Samakhyali (KM 247.73) to Palanpur (KM 0).

(ii) Now, as per the Addendum, Doubling and Electrification work is also part of the Concession Agreement.

(iii) The Company has capitalised work carried out for doubling on receipt of Certificate of Safety Engineer in F.Y. 2022-23. However, neither physical nor financial closure of project was reached and various works including payment of previous invoices was going on. Accordingly, the Company has incurred an additional expenditure of Rs. 687.81 crore (Rs. 526.89 crore towards Doubling and Electrification work during the F.Y. 2023-24 and Rs. 160.92 crore during the F.Y. 2024-25) and capitalised the same under the Intangible Assets.

6. C&AG's Observation on Doubling and Electrification works and Management Reply to Observation of CAG:

a. <u>Observation</u>

"Balance Sheet

Assets – 1. Non-current assets

Other Intangible Assets -Note 5- ₹ 3,67,429.32 lakh

Statement of Profit and Loss

Total Expenses – ₹1,39,015.80 lakh

Profit/ (loss) for the period – ₹1394.01 lakhs

The above head of Other Intangible assets includes ₹ 687.81 crore (₹ 526.89 crore pertaining to the financial year 2023-24) and ₹ 160.92 crore (pertaining to the financial year 2024-25) towards doubling and electrification works. As per the concession agreement of the Company with the Railways, the Company has no ownership of the railway infrastructure assets created by it. By doubling and electrifying the railway line, there would be no increase in the amount of freight revenue share to be received from MoR.

Therefore, it should have been charged to the Statement of Profit and Loss as expenses instead of booking the same as intangible assets in compliance to the requirement of Appendix D of Ind AS 115, 'Revenue from Contracts with Customers'.

This has resulted in overstatement of 'Other Intangible Assets', understatement of 'Expenses' by ₹ 687.81 crore and overstatement of Profit for the year' by the same amount.

The observation was also raised on the Financial Statements of the Company for the financial year 2023-24. In response, the Company (September 2024) had given an assurance that an opinion on the same would be taken from the Expert Advisory Committee of ICAI. However, neither opinion in the matter was sought from the ICAI nor adjustments as mentioned above were made."

b. Management Reply to observations of CAG

"In this regard, it is respectfully submitted as under:

The provisions of Ind AS 115 permit recognition of revenue and related rights on the basis of contractual entitlements arising from concession arrangements. In the case of the Company, the concession agreement entered with MoR grants the Company the right to receive a defined share of freight earnings on the project line. This right represents an intangible asset under Ind AS 115 as it is a contractual entitlement to future inflows of economic benefits over the concession period.

The doubling and electrification works executed by the Company were necessitated due to severe congestion and bottlenecks on the existing single line, which had led to diversion of trains towards alternate routes and a resultant decline in revenue apportionments to the Company.

To address these constraints, the Company undertook the Palanpur–Samakhiali doubling project (247 RKM), which was commissioned on 24th February 2023. The project has already resulted in a significant increase in traffic throughput on account of DFC connectivity and other factors, thereby reducing diversions and improving revenue apportionments by nearly 40–50%.

Similarly, the electrification works have provided enduring benefits in terms of lower operating costs, enhanced efficiency in train operations, and environmental advantages through energy savings. Such benefits are not confined to a single reporting period but will continue to accrue throughout the concession term. Accordingly, debiting the entire expenditure to one year's Statement of Profit and Loss would not present a true and fair view of the financial performance of the Company.

Further, as per the amendment in the Concession agreement, Project Railway means broad gauge rail link between Palanpur and Gandhidham including double line from the Palanpur to Samakhayali. This also includes all the Railway Electrification works on Project line from Gandhidham to Samakhayali and double line from Samakhayali to Palanpur.

The expenditure has therefore been capitalised as an intangible asset on the basis that future economic benefits are demonstrably expected to flow to the Company. This is consistent with the recognition criteria laid down in paragraphs 20 and 22 of Ind AS 38.

Further, paragraph 27 of Ind AS 38 stipulates that the cost of an intangible asset shall include:
(a) purchase price, including duties and taxes (net of rebates/discounts), and
(b) directly attributable costs of preparing the asset for its intended use.

The expenditure on doubling and electrification is clearly of a directly attributable nature, being incurred to enhance the effective utilisation of the concession right. The same is therefore, eligible for capitalisation in compliance with Ind AS 38 read with Appendix D of Ind AS 115.

Though the benefits arising from doubling and electrification have not been separately quantified, the overall results in terms of increased apportionments and reduction in costs substantiate that substantial long-term benefits are accruing to the Company.

It is also pertinent to mention that the Company has already approached the Railway Board for extension of the concession period by at least 15 years, which further strengthens the expectation of sustained economic benefits over a longer horizon.

Further, the Company has assured that during the current financial year, a detailed opinion will be sought from the Expert Advisory Committee (EAC) of ICAI on this matter. Based on the opinion so received, the Company shall take necessary action in the subsequent financial year.

In view of the substantial and continuing economic benefits derived from the doubling and electrification projects, and considering that the expenditure is directly attributable to the concession right, the capitalisation as intangible assets is appropriate. The Audit is therefore requested to kindly drop the Provisional comment."

7. Apart from submissions made in paragraph 4(i) above, the Company has submitted the following for the consideration of EAC:

(i) Works carried out after CRS commissioning certificate issued for starting trains operation:

While seeking CRS certification for commissioning of a rail line (i.e. GC, DL etc.), there is target and single moto of R Ltd. to provide bare minimum works and focus mostly on works directly related to starting trains operations at the earliest in order to start revenue generation. Due to the following reasons, the completion takes nearly 1-2 years beyond CRS certificate for commissioning of rail line/starting training operations:

(a) CRS authorisation is issued subject to compliance of several works and stipulations. Remarks made by CRS while issuing commissioning certificate for compliance are for example, development of circulating area, approach road, gang hut, platforms, FOB, passenger amenities works at stations, good sheds, works of shunting neck at yards, fencing of LC gates for safety of trains, S&T works, etc.

(b) Miscellaneous associated works required to complete are part of the work as per approved plans.

(c) There is only difference in timing of works and payment i.e. works those were priority in nature were carried out first and those were secondary are taken on later stage.

(d) This can be understood in a way that while constructing a housing complex, there remains provision for multiple lifts; however initially project becomes operational and various amenities including lifts, swimming pools, clubs, gym etc. are completed at later stage.

(ii) Requirement and advantages of Doubling on SPV (PNU-SIOB/248 route km) project line:

(a) There were bottlenecks, congestions and constrained line capacity on single line due to which trains bound for northern hinterland were being diverted from the Company's project line resulting in loss of revenue to the Company.

(b) In order to enhance the existing line capacity and number of trains, increasing freight revenue and future traffic growth, the Company had planned, successfully commissioned and operationalised the doubling project on Palanpur - Samakhiali project line (248 RKM) on 24th Feb 2023.

(c) *Codal life of new assets/track will be beyond the concession period of the Company. In case concession period is not extended by MoR, the Company will get credit of residual value towards the new track/assets created by the Company.* (Emphasis supplied by the querist.)

(d) As a result of increase in line capacity, the traffic has increased on the project line because of DFC and other factors; and movement of traffic is done with reduction in diversion of traffic which in turn has increased the Company's revenue apportionments by 40-50%.

(e) Advantage due to execution and commissioning of doubling, a comparative summary is tabulated below:

	Number of Trains	**Apportionment Earnings**	**Diversion of trains**
F.Y. 2020-21	22511 Rakes	₹ 756 Crore	1047 rakes
F.Y. 2021-22	25671 Rakes	₹ 835 Crore	1504 rakes
F.Y. 2022-23	29058 Rakes	₹ 1133 Crore	1553 rakes
F.Y. 2023-24	28351 Rakes	₹ 1179 Crore	437 rakes
F.Y. 2024-25	27961 Rakes	₹ 1132 Crore	145 Rakes
F.Y. 2025-26 (provisional)	30147 Rakes	₹ 1250 Crore	130 rakes (approx.)
% change (compared to F.Y. 20-21 with F.Y. 25-26)	+ 34 % Increase	+ 65 % increase	- 87% decrease

Due to doubling, further diversion of trains is reducing gradually to almost negligible.

From the above table, it may be seen that annual apportionments of the Company was ₹756 crore during F.Y. 2020-21 before completion of doubling. After doubling got successfully commissioned in Feb'23, the apportionments had increased to ₹ 1133 crore during F.Y. 2022-23, resulting in increase in apportionments of the Company by approximately 50% as compared to F.Y. 2020-21.

(f) Additional revenue advantage due to doubling from F.Y. 2021-22 onwards for remaining concession period.

(g) Average annual increase in revenue: Rs. 494 Crore (Rs. 1250 crore minus Rs. 756 Crore).

(h) Increase in revenue over the remaining concession period from F.Y. 2021-22 onwards upto F.Y. 2037-38 is 16 years = ₹494 x 16 yrs = ₹7904 crore.

(i) Anticipated O&M Cost @ 50% = Rs. 3952 crore.

(j) Net profit for the Company= Rs. 3952 crore (Rs. 7954 crore minus Rs. 3952 crore) .

(k) Keeping above in view, overall, the Company is getting net advantage of nearly ₹ 4000 crore which is more than the doubling cost incurred by the Company in addition to residual value of remaining codal life towards new assets created by the Company.

(iii) Expenditure incurred by the Company towards doubling is up-grade to the infrastructure and not maintenance of existing infrastructure; entire new infrastructure is created by the Company, therefore, in accordance with requirements of Ind AS 115 and accounting policy of the Company, it has recognised expenditure incurred as Intangible Assets in its financial statements based on principles as stated above. The expenditure incurred by the Company is going to provide benefit in terms of increase in capacity; and number of trains shall also increase on track, which will result in traffic and increased revenue.

(iv) With reference to capitalisation of additional expenditure incurred after initial capitalisation, the Company is of the view that there is no difference between nature of both the expenditure in service concession arrangement, both are part of original plan and there is difference of timing of capitalisation only.

(v) The expenditure incurred by the Company has also enhanced the connectivity and freight transportation contributing to sustainable long-term revenue generation in Kutch, Patan & Banaskantha districts of Gujarat alongwith ports of Kandla, Tune & Mundra ports with savings in cost.

(vi) It is also estimated that at the end of concession period (if not extended), then the physical assets created due to above expenditure shall have significant life remaining (e.g. sleepers 40 years) and the Company will be able to receive significant amount at the time of transfer as stated in Concession Agreement.

(vii) It is also submitted that the Company is of the view that at the end of original concession period, assets created under original concession agreements may be transferred at book value, however additional assets created shall be transferred at depreciated replacement value.

(viii) In accordance with terms of original concession arrangement, the Company was getting fair share of its revenue and was not required to carry out any of the work including doubling, electrification, CTR etc. However, the Company has amended its Concession Agreement and carried out all of these works since all of these expenditure are going to provide additional benefit, i.e., return on additional investment made by the Company.

(ix) The Company has capitalised the expenditure incurred upto 31st March 2025 under 'Intangible Assets under Development/ Intangible Assets', on the grounds that this expenditure relates to the enhancement of the project assets constructed under the Concession Agreement. Further, as stated above, as the Company has submitted a request to the Railway Board requesting an extension of the concession period by at least 15 years, the expected future benefits of such works are anticipated to extend over a longer duration, supporting capitalisation under Appendix D to Ind AS 115.

(x) The Company believes that the benefits arising from such works—such as reduced operating costs and improved rail operations—accrue over the entire concession period and are not confined to

a single financial year. Therefore, charging the entire expenditure to the Profit and Loss Statement in one year would not reflect the underlying economic substance, and accordingly, the amount has been capitalised as an Intangible Asset in accordance with Appendix D to Ind AS 115.

B. Query

8. On the basis of the above, the querist has sought the opinion of the EAC of the ICAI on following issues:

(i) *Expenditure incurred like Complete Track Renewal (CTR):* The Company has received a cost estimate of ₹ 635.62 crore from the Railways towards CTR, against which it has not yet given consent for ₹ 258.75 crore and has already incurred ₹ 75.59 crore. The Company seeks guidance on the following:

(a) The appropriate accounting treatment, under the applicable Ind AS, for the expenditure of Rs. 560.03 crore (Rs. 635.62 crore minus Rs. 75.59 crore) is required to be accounted for in the financial statements, including whether capitalisation under Ind AS 115 is appropriate or whether the expenditure is required to be charged to the Statement of Profit and Loss as per the C&AG's view.

(b) How expenditure of Rs. 75.59 crore which has been incurred upto 31st March 2025 should be recognised in financial statements?

(ii) *Expenditure incurred on Additional Waterways, Deep Screening etc.:* The Company has received a cost estimate of ₹ 136.86 crore from the Railways towards additional waterways, deep screening, TFR and related works on the railway line and has already incurred ₹ 81.00 crore. The Company seeks guidance on the following:

(a) The appropriate accounting treatment, under the applicable Ind AS, for the expenditure of Rs. 136.86 crore in the financial statements, including whether capitalisation under Ind AS 115 is appropriate or whether the expenditure is required to be charged to the Statement of Profit and Loss as per the C&AG's view.

(b) The appropriate accounting treatment, under the applicable Ind AS, for the expenditure of Rs. 81 crore, which has not yet been incurred in the financial statements, including whether capitalisation under Ind AS 115 is appropriate or whether the expenditure is required to be charged to the Statement of Profit and Loss as per the C&AG's view.

(iii) *Expenditure/ payments made for doubling after initial capitalisation:* whether the additional expenditure of ₹ 687.81 crore (₹ 526.89 crore for F.Y. 2023-24 and ₹ 160.92 crore for F.Y. 2024-25) incurred on doubling works—after the initial capitalisation of the project—should be capitalised or expensed to the Statement of Profit and Loss under the applicable Ind AS.

(iv) Disclosure requirements pursuant to above transactions in financial statements.

C. Points considered by the Committee

9. The Committee notes that the issues raised by the querist relate to the accounting for subsequent expenditure and certain specific costs incurred by the Company with regard to the service concession arrangement of Gandhidham–Palanpur Gauge Conversion project, viz., Complete track renewal (CTR) works, additional works (involving deep screening, waterway, casual renewal, TFR, etc.) and doubling works on the project line. The Committee has, therefore, considered only these issues and has not examined any other issue that may arise from the Facts of the Case, such as, classification of the arrangement as service concession arrangement, recognition of intangible asset including amortisation of intangible asset recognised, recognition, measurement and presentation of various expenses incurred by the Company other than those for which the query has been raised in paragraph 8 above, such as expenditure on electrification etc., impact of consent not being given for expenditure on CTR of PNU-SIOB down line by the Company, measurement and presentation of provision/liability for resurfacing cost (if any), accounting for operating and maintenance (routine) obligations under the arrangement and costs incurred in relation thereto, leasing of existing assets on the Project to the Company, accounting for the Company's entitlement to receive depreciated replacement value of all the assets upon expiry of the arrangement, revenue recognition under the arrangement, timing of capitalisation as intangible asset, impact of credit/proceeds from disposal of scrap material from replaced track components, application (if any) of Ind AS 8, 'Accounting Policies, Changes in Accounting Estimates and Errors', impairment of intangible assets/ financial assets related to the service concessions arrangement, whether the contract is onerous as per Ind AS 37, etc. Further, the Committee has not examined the relationship or arrangement between the Company and Western Railways/Ministry of Railways. The Standards hereinafter referred are the Indian Accounting Standards (Ind AS), notified under the Companies (Indian Accounting Standards) Rules, 2015. At the outset, the Committee presumes from the Facts of the Case that the concession arrangement in the extant case falls in the scope of Appendix D, 'Service Concession Arrangements' to Ind AS 115.

10. The Committee notes that in the given case, the service concession arrangement entered into by the Company with MoR on 8th November 2005, encompasses the gauge conversion along with all associated activities for development, financing, construction, operation, and maintenance of the Project Railway for a period of 32 years. As per Clause 5.1 of Concession Agreement, upon expiry, the project assets shall be handed over by the Company to MoR in accordance with provisions of Clause 8.1, under which upon normal transfer, the Company shall be entitled to receive and MoR shall pay an amount equal to book value (i.e. the value of the new assets and additional facilities created by the Company, net of depreciation charged on the basis of straight line method).

As per Clause 4.3(d) of the Concession Agreement, the Company is required to ensure that the project assets remain in proper working condition, including carrying out replacements in accordance with standards laid down by MoR, of all Project Assets whose lives have expired. Such replacement shall be caried out by the Company either by itself or through MoR/Western Railways and such costs shall be borne by the Company. Further, the Company signed an addendum to the original Concession Agreement on 26th October, 2020 to include doubling of certain stretch of the Company's railway line as part of its obligations under the Concession Agreement.

The Committee further notes that the Company received letters dated 19th January 2022 and 20th May 2022 from Western Railways (MoR) seeking its consent to carry out certain Complete Track Renewal (CTR) works, which broadly involves replacement of rails and sleepers on the Company's railway line.

Thus, in the given case, the service concession arrangement involves inter-alia the following promises to the grantor:

(a) Construction/conversion of the Broad-Gauge rail line – After construction, the above rail line was successfully commissioned;
(b) Operation of the rail line;
(c) Routine maintenance; and
(d) Major replacement works.

In addition, the Company has created additional facilities, such as, doubling of rail line and undertaken certain upgrade work.

11. The Committee notes that Appendix D to Ind AS 115 provides as follows:

"12 Under the terms of contractual arrangements within the scope of this Appendix, the operator acts as a service provider. The operator constructs or upgrades infrastructure (construction or upgrade services) used to provide a public service and operates and maintains that infrastructure (operation services) for a specified period of time.

13 The operator shall recognise and measure revenue in accordance with Ind AS 115 for the services it performs. The nature of the consideration determines its subsequent accounting treatment. …"

The Committee notes that Appendix D requires that the separate services within a service concession arrangement, i.e., 'construction services', 'upgrade services' or 'operation services', must be segregated because each separate phase or element has its own distinct skills, requirements and risks. The allocation of revenue for the provision of these separate services is determined in accordance with Ind AS 115. This involves identifying the performance obligations under the contract with the customer, determining the transaction price under the contract(s), and allocating that transaction price to the performance obligations in the contract. Accordingly, the Company, being the operator under service concession arrangement, needs to evaluate whether the above promises should be accounted for separately under Ind AS 115. In this regard, the Committee notes the following requirements of Ind AS 115:

"22 At contract inception, an entity shall assess the goods or services promised in a contract with a customer and shall identify as a performance obligation each promise to transfer to the customer either:

(a) a good or service (or a bundle of goods or services) that is distinct; or

(b) a series of distinct goods or services that are substantially the same and that have the same pattern of transfer to the customer (see paragraph 23)."

"27 *A good or service that is promised to a customer is distinct if both of the following criteria are met:*

(a) the customer can benefit from the good or service either on its own or together with other resources that are readily available to the customer *(ie the good or service is capable of being distinct)*; and

(b) the entity's promise to transfer the good or service to the customer is separately identifiable from other promises in the contract *(ie the promise to transfer the good or service is distinct within the context of the contract)*."

(Emphasis supplied by the Committee.)

Thus, the promises stated above should be accounted for separately as performance obligations if they are both (1) capable of being distinct, and (2) distinct in the context of the contract.

12. In the above context, the Committee notes that in the extant case, the construction activity (viz., conversion of the Broad-Gauge rail line) is clearly a separate performance obligation. It is capable of being distinct and also being distinct in the context of the contract since:

— grantor (MoR) can benefit from the rail line on its own.
— other entities could provide the construction services.

Construction of the rail line is separately identifiable from other promises and does not significantly affect the other services. On account of construction/conversion of Broad-Gauge rail line (from Gandhidham to Palanpur), the Company has received a right to get share of freight earning from the use of the above rail line by the general public. Therefore, as per the requirements of Appendix D (paragraphs 15 to 18), an intangible asset measured at the fair value of the construction services (and not the cost of construction) would be recognised.

13. *Accounting for CTR works*

The Committee notes that in terms of Concession Agreement, there is an obligation on the Company to keep the project assets in working condition, including replacement, as per laid down standards of MoR, for project assets, whose codal lives (useful lives) expire during the concession period. Such replacements shall be carried out by the Company either by itself or through MoR and the cost of replacements shall be borne by the Company. Further, it is noted that the Company will not be reimbursed separately by the grantor for these replacement/restoration activities. Accordingly, the Company is required to carry out replacement/restoration activities based on predetermined useful life of project assets.

14. With regard to accounting for replacement/restoration obligation, the Committee notes paragraph 21 of Appendix D of Ind AS 115 as follows:

"Contractual obligations to restore the infrastructure to a specified level of serviceability

21 The operator may have contractual obligations it must fulfil as a condition of its licence (a) to maintain the infrastructure to a specified level of serviceability or (b) to restore the infrastructure to a specified condition before it is handed over to the grantor at the end of the service arrangement. These contractual obligations to maintain or restore infrastructure, except for any upgrade element (see paragraph 14 of this Appendix), shall be recognised and measured in accordance with Ind AS 37, ie at the best estimate of the expenditure that would be required to settle the present obligation at the end of the reporting period."

The Committee notes that paragraph 21 of Appendix D requires an entity to recognise and measure its contractual obligations to maintain or restore infrastructure (except any upgrade element) in

accordance with Ind AS 37. Therefore, the restoration/maintenance activity will not be accounted for as a separate performance obligation and instead be accounted for as per Ind AS 37. Thus, in the extant case, the accounting treatment of the expenditure incurred on CTR works will depend upon whether the activity performed under the Concession Agreement is the entity's contractual obligations to maintain or restore infrastructure or the same is any upgrade element.

In this context, the Committee notes that the querist has stated that CTR works are highly complex field operations involving replacement of rails, sleepers and ballast under running train conditions, necessitating imposition of speed restrictions and phased execution over small stretches. For CTR works, WR has proposed *upgradation of track standards* (60 kg/m rails of 90 UTS in place of 52 kg/m rails of 72 UTS; heavier and wider PSC sleepers; reduced spacing to enable higher axle loads).

Further, with regard to replacement of track in the CTR works, the querist has informed that during initial construction, the track was laid with 60 kg sleeper although the rail was 52 kg with the clear understanding that in future if rail is required to be upgraded to 60 kg during the concession period, it should be possible to change the rail without need of changing the sleepers. In instant case, rail replacement became due on GMT basis but sleeper replacement was not due either on the GMT basis or on condition basis. The codal life of PSC sleepers is 50 years irrespective of the GMT. Western Railway has taken a decision to pre-maturely replace the sleepers, perhaps with the intention of *upgrading the track to the standard of DFCC feeder route*.

Furthermore, in this regard, the querist has mentioned that the Company was required to incur various expenditure in order to keep its project in working condition and also, the Company had to create various *new facilities* for project assets as and when their need arises. Moreover, in the letter of MR/Western Railways, it was stated that Railways have been doing CTR works regularly for the stretches which were required from *maintenance* point of view. It was also informed that railway has done *casual renewal* of rails in SIOB-GIMB section of the Company's line. In SIOB-GIMB section of the Company's line, the track structure is 52 kg rail and 60 kg sleeper with 1540 sleeper density and GMT of rail in most of this section has already surpassed its service life. Hence, CTR works needs to be done on priority to avoid any safety hazard on this account.

Thus, based on the facts stated by the querist, it appears that some of the CTR works/activities may include an upgrade element (for example, in respect of sleepers which are being upgraded due to CTR works) and some are incurred to keep the project assets in their serviceable level/condition (for example, change of rails whose useful life has expired due to continuous use and required replacement as per original concession arrangement).

15. As discussed in paragraph 11 above, upgrade or construction services are separate performance obligations in the contact. The Committee notes that in the given case, the Company undertook certain upgrade work under CTR activities as per the directives or letters received from MoR in F.Y. 2021-22 and 2022-23, which required creation of additional facility/ assets in form of certain upgraded assets (having additional load/capacity) on the commissioned rail line. Thus, it would represent upgrade activities (and not the requirement to maintain or restore the infrastructure to a specified level of serviceability or a specified condition; and therefore, cannot be considered as maintenance/restoration activities).

The Committee further notes that as per the Concession Agreement, these upgrades were not explicitly mentioned or planned at the time of entering into the Agreement. Hence, the Committee is of the view that in the extant case, 'upgrade' does not seem to be a contractual obligation under the Concession

Agreement and therefore, it is not a component of the original intangible asset recognised in exchange of construction of Broad Guage rail line.

In this regard, the Committee notes the following requirements of Appendix D to Ind AS 115:

> **"Construction or upgrade services**
>
> 14 The operator shall account for construction or upgrade services in accordance with Ind AS 115.
>
> **Consideration given by the grantor to the operator**
>
> 15 If the operator provides construction or upgrade services the consideration received or receivable by the operator shall be recognised in accordance with Ind AS 115. The consideration may be rights to:
>
> (a) a financial asset, or
>
> (b) an intangible asset.
>
> 16 The operator shall recognise a financial asset to the extent that it has an unconditional contractual right to receive cash or another financial asset from or at the direction of the grantor for the construction services; the grantor has little, if any, discretion to avoid payment, usually because the agreement is enforceable by law. The operator has an unconditional right to receive cash if the grantor contractually guarantees to pay the operator (a) specified or determinable amounts or (b) the shortfall, if any, between amounts received from users of the public service and specified or determinable amounts, even if payment is contingent on the operator ensuring that the infrastructure meets specified quality or efficiency requirements.
>
> 17 The operator shall recognise an intangible asset to the extent that it receives a right (a licence) to charge users of the public service. A right to charge users of the public service is not an unconditional right to receive cash because the amounts are contingent on the extent that the public uses the service."
>
> "19 The nature of the consideration given by the grantor to the operator shall be determined by reference to the contract terms and, when it exists, relevant contract law. The nature of the consideration determines the subsequent accounting as described in paragraphs 23–26 of this Appendix. However, both types of consideration are classified as a contract asset during the construction or upgrade period in accordance with Ind AS 115."
>
> "26 Ind AS 38 applies to the intangible asset recognised in accordance with paragraphs 17 and 18 of this Appendix. Paragraphs 45–47 of Ind AS 38 provide guidance on measuring intangible assets acquired in exchange for a non-monetary asset or assets or a combination of monetary and non-monetary assets."

The Committee notes from the above that revenue and costs relating to construction or upgrade services should be recognised in accordance with Ind AS 115. This implies that construction or upgrade services should be accounted for in accordance with the appropriate model (intangible asset or financial asset), regardless of when they take place. Thus, if an upgrade adds to or extends the existing infrastructure from which an entity can generate additional revenue, then the extension of the

infrastructure will create a new intangible asset, giving rise to new construction revenues, which are recognised using the same principles as for the initial construction revenue.

However, from the limited facts supplied, it appears that the upgrade activities under CTR will not result in the extension of the existing rail line; instead, it will only replace some of the parts of the existing rail line with improved or better parts having more load/capacity. Thus, there is no new intangible asset to be recognised; rather it is a subsequent expenditure on existing intangible asset, which as per the requirements of paragraph 26 of Appendix D should be recognised as per the requirements of Ind AS 38, 'Intangible Assets'. With regard to subsequent expenditure on an existing intangible asset, paragraph 20 of Ind AS 38 states as follows:

> "The nature of intangible assets is such that, in many cases, there are no additions to such an asset or replacements of part of it. Accordingly, most subsequent expenditures are likely to maintain the expected future economic benefits embodied in an existing intangible asset rather than meet the definition of an intangible asset and the recognition criteria in this Standard. In addition, it is often difficult to attribute subsequent expenditure directly to a particular intangible asset rather than to the business as a whole. Therefore, only rarely will subsequent expenditure—expenditure incurred after the initial recognition of an acquired intangible asset or after completion of an internally generated intangible asset—be recognised in the carrying amount of an asset. … "

The Committee notes that the querist has mentioned that the upgrade activity provides future economic benefits in the form of saving in costs and increased revenue (due to increasing train speed and frequency, and enhancing overall network capacity, ultimately leading to higher volumes and increased revenue). Considering this, the Committee notes that the upgrade of rail track will provide additional/ incremental benefits from the rail line or project through (a) cost savings (b) retaining the existing traffic and (c) also increase in revenue compared to original projections due to higher speed, frequency and efficiency. Accordingly, the Committee is of the view that the expenditure incurred on upgrade of rail line in the extant case should be recognised in the carrying amount of the existing asset as per the requirements of Appendix D.

16. With regard to activities or expenditure under CTR that are undertaken or incurred to keep the project assets in their serviceable level/condition (viz., for maintenance or restoration of the rail track or its parts), the Committee notes that the Company's maintenance or restoration obligation arises as a consequence of use of the project assets during the operating phase and therefore, as per the requirements of Appendix D and Ind AS 37, a provision should have been recognised for these obligations during the construction period, at the best estimate of the expenditure required to settle the present obligation at each reporting date, by charge to profit or loss over the useful life of the respective project assets till the expected date of maintenance/restoration. Further, such provision should be reviewed and adjusted to reflect the current best estimate at each reporting date as per the requirements of Ind AS 37. Therefore, as and when the restoration/maintenance takes place and the expenditure is incurred in this regard, the provision so created should be utilised for meeting such expenditure.

However, in the extant case, it appears that the Company has not created any such provision for restoration/maintenance activity so far during the concession period. The Committee notes that the querist has submitted that the Company was not aware of the requirement towards CTR/TRR works towards the replacement of sleepers and implicitly, it would not have recognised any obligation towards the same. Therefore, the Committee is of the view that the approach followed by the Company of non-provisioning towards this restoration/maintenance obligation seems inappropriate. As per the aforesaid requirements of Appendix D and Ind AS 37, the Company is required to recognise the

provision over the usage period of project assets as per the requirements of Ind AS 37 since the inception of the Concession Agreement. The Committee, however, has not examined the implications of Ind AS 8, 'Accounting Policies, Changes in Accounting Estimates and Errors' in respect of any adjustments that may arise from the above.

Accounting for additional works (involving deep screening, waterway, casual renewal, TFR, etc.)

17. The Committee further notes that the Company has also incurred certain costs on the Project Assets such as, deep screening by BCM machine and manual and other associated works in connection PNU-GIM section, casual renewal of scabby and kinky rails under ADEN-RDHP and ADEN-GIM jurisdiction (the Company's portion), repairs to staff quarters at various stations in the section of ADEN-RDH, etc., the details of which have been submitted by the querist in a separate document 'Details of Expenditure incurred towards Project line'.

The Committee also notes that in respect of the additional works, the querist has submitted that in olden days, at the time gauge conversion was done by the Company, fittings had a limited life and through fitting renewal (TFR), i.e. renewal of pads and ERC was undertaken at the periodicity of 5-10 years depending on the traffic density. However, after through track renewal, when the track has been upgraded to 60 kg 90 UTS rail, wide-based heavy sleepers, 300 mm ballast cushion, improved rubber pad and mark v-ERC, the life of fittings is supposed to be matching with life of rail. Therefore, in future there should not be any necessity of through fitting renewal (TFR) and fitting renewal will remain casual renewal only. Further, it is also mentioned that deep screening and Through Fitting Renewal if done in a routine manner is a maintenance activity and will be the part of Western Railway's maintenance cost. However, in the present case, deep screening and Through Fitting Renewal has been done alongwith CTR with increased ballast cushion, upgraded ballast profile and improved fittings.

From the above, the Committee is of the view that the Company should analyse the exact nature of each individual item of these expenses as to whether these are contractual obligations to restore or maintain the railway infrastructure to a specified level of serviceability (and accordingly required to be accounted for as a provision over the concession agreement by charge to the Statement of Profit and Loss as per the requirements of Ind AS 37, as required by paragraph 21 of Appendix D as described in paragraph 16 above), or whether these represent separate upgrade performance obligation (and therefore required to be accounted for as described in paragraph 15 above); and accordingly account for the same. Further, any expenditure incurred on normal repairs activity should be expensed in the Statement of Profit and Loss unless it can be clearly demonstrated that such expenditure relates to fulfilling a contractual obligation to restore or maintain the railway infrastructure to a specified level of serviceability under the concession arrangement, which should be accounted for in accordance with the requirements applicable to such obligations, as discussed above.

18. *Accounting for doubling of the rail line after initial capitalisation:*

The Committee notes that this activity will involve doubling the rail line and resultantly, as submitted by the querist, the GMT/load will be distributed on both UP & DN lines and major loaded traffic will be on new line. Further, the querist has submitted that the Company is expecting additional benefits from doubling and the benefits of the CTR should be read in entirety, as they form part of the overall changes undertaken by the Company in anticipation of increased traffic at the Port. Thus, though there is no change in the share or percentage of freight revenue as contended by C&AG, there are additional/incremental benefits including cost savings, increased quantum of revenue, etc.

As discussed above, upgrade or construction services are separate performance obligations specified in the contact. The Committee notes that in the given case, the Company undertook the doubling of the rail line from F.Y. 2020-21 onwards as a result of entering into addendum to original Concession Agreement, which required creation of additional facility/ assets on the commissioned rail line. Thus, it would represent upgrade activities (and not the requirement to maintain or restore the infrastructure to a specified level of serviceability or a specified condition; and therefore, cannot be considered as maintenance activities).

Also, the Committee notes from the facts supplied by the querist that no such upgrades were planned at the time of entering into the original Concession Agreement. Hence, the Committee is of the view that in the extant case, 'upgrade' does not seem to be a contractual obligation under the original Concession Agreement and therefore, it is not a component of the original intangible asset recognised in exchange of construction of Broad Guage rail line.

In this regard, the Committee notes from the requirements of paragraphs 14, 15, 16, 17 and 19 of Appendix D to Ind AS 115 (as reproduced in paragraph 15 above) that revenue and costs relating to construction or upgrade services should be recognised in accordance with Ind AS 115. This implies that construction or upgrade services should be accounted for in accordance with the appropriate model (intangible asset or financial asset), regardless of when they take place. Thus, if an upgrade adds to or extends the existing infrastructure from which an entity can generate additional revenue, then the extension of the infrastructure will create a new intangible asset, giving rise to new construction revenues, which are recognised using the same principles as for the initial construction revenue.

Accordingly, the expenditure incurred by the Company towards doubling, shall be in the nature of a separate infrastructure asset. These would have to be accounted for as separate asset under Appendix D in accordance with requirements of Ind AS 115 and, correspondingly, the Company shall recognise a separate intangible asset / financial asset in accordance with the requirements of Appendix D to Ind AS 115.

19. With regard to the disclosures to be provided by the Company, the Committee notes that Appendix E to Ind AS 115 states as follows:

> "6 All aspects of a service concession arrangement shall be considered in determining the appropriate disclosures in the notes. An operator and a grantor shall disclose the following in each period:
>
> (a) a description of the arrangement;
>
> (b) significant terms of the arrangement that may affect the amount, timing and certainty of future cash flows (eg the period of the concession, re-pricing dates and the basis upon which re-pricing or re-negotiation is determined);
>
> (c) the nature and extent (eg quantity, time period or amount as appropriate) of:
>
> (i) rights to use specified assets;
>
> (ii) obligations to provide or rights to expect provision of services;
>
> (iii) obligations to acquire or build items of property, plant and equipment;
>
> (iv) obligations to deliver or rights to receive specified assets at the end of the concession period;

(v) renewal and termination options; and

(vi) other rights and obligations (eg major overhauls);

(d) changes in the arrangement occurring during the period; and

(e) how the service arrangement has been classified.

6A An operator shall disclose the amount of revenue and profits or losses recognized in the period on exchanging construction services for a financial asset or an intangible asset.

7 The disclosures required in accordance with paragraph 6 of this Appendix shall be provided individually for each service concession arrangement or in aggregate for each class of service concession arrangements. A class is a grouping of service concession arrangements involving services of a similar nature (eg toll collections, telecommunications and water treatment services)."

The Committee notes that there are other standards also that are applicable and the disclosure requirements of those standards would be also appliable, such as:

- Ind AS 115 (paragraphs 110-123 dealing with various disclosure requirements).
- Ind AS 38 (paragraphs 118-122 dealing with various disclosure requirements).
- Ind AS 37, 107 and 109.

D. Opinion

20. On the basis of the above and subject to paragraph 9 above, the Committee is of the following opinion on the issues raised in paragraph 8 above:

(i) CTR works

As explained in paragraphs 11-16 above, some of the CTR works/activities may include an upgrade element and some are incurred to keep the project assets in their serviceable level/condition and required replacement as per original concession arrangement. The revenue and costs relating to upgrade services should be recognised in accordance with Ind AS 115. With regard to activities or expenditure under CTR that are undertaken or incurred to keep the project assets in their serviceable level/condition (viz., for maintenance or restoration of the rail track or its parts), the Company's maintenance or restoration obligation arises as a consequence of use of the project assets during the operating phase and therefore, as per the requirements of Appendix D and Ind AS 37, a provision should have been recognised for these obligations during the concession period at the best estimate of the expenditure required to settle the present obligation at each reporting date, by charge to profit or loss over the useful life of the respective project assets till the expected date of maintenance/restoration. Further, such provision should be reviewed and adjusted to reflect the current best estimate at each reporting date as per the requirements of Ind AS 37. Therefore, as and when the restoration/maintenance takes place and the expenditure is incurred in this regard, the provision so created should be utilised for meeting such expenditure. The Committee is of the view that the approach followed by the Company of non-provisioning towards this restoration/maintenance obligation seems inappropriate. The Company is required to recognise the provision over the usage period of project assets as per the requirements of Ind AS 37 since the inception of the Concession Agreement.

(ii) Expenditure incurred on Additional works, like waterways, deep screening etc.

As explained in paragraph 17 above, the Committee is of the view that the Company should analyse the exact nature of each individual item of these expenses as to whether these are contractual obligations to restore or maintain the railway infrastructure to a specified level of serviceability (and accordingly required to be accounted for as a provision over the Concession Agreement by charge to the Statement of Profit and Loss as per the requirements of Ind AS 37, as required by paragraph 21 of Appendix D as described in paragraph 16 above), or whether these represent separate upgrade performance obligation (and therefore required to be accounted for as described in paragraph 15 above); and accordingly account for the same. Further, any expenditure incurred on normal repairs activity should be expensed in the Statement of Profit and Loss unless it can be clearly demonstrated that such expenditure relates to fulfilling a contractual obligation to restore or maintain the railway infrastructure to a specified level of serviceability under the concession arrangement, which should be accounted for in accordance with the requirements applicable to such obligations, as discussed above.

(iii) Expenditure on Doubling after initial capitalisation:

As explained in paragraph 18 above, the expenditure incurred by the Company towards doubling, shall be in the nature of a separate infrastructure asset. These would have to be accounted for as separate asset under Appendix D in accordance with requirements of Ind AS 115 and, correspondingly, the Company shall recognise a separate intangible asset / financial asset in accordance with the requirements of Appendix D to Ind AS 115.

(iv) Refer paragraph 19 above.

****