

Classification of Grant Related to Assets in the Statement of Cash Flows

A. Facts of the Case

1. A company was incorporated on 16th August 1984 for procuring, transmission, processing and marketing of natural gas. The company has an authorised share capital of ₹ 2,000 crore, out of which ₹1,691.30 crore is paid-up share capital. The Government of India (‘GoI’) holds 54% equity of the company at present. The securities of the company are listed on National Stock Exchange, Bombay Stock Exchange and London Stock Exchange. At present, the company owns over 11,000 Kms of pipeline and currently transmits about 206 MMSCM per day of natural gas. The company operates six LPG manufacturing plants in different parts of the country with an installed capacity of 1.04 Million MT of LPG per annum. The company has an integrated petrochemical plant at Pata, Uttar Pradesh for manufacturing polymers. The company has world’s longest pipeline from Jamnagar to Loni for transmission of LPG. The company has integrated its business activities and operates the City Gas Distribution (‘CGD’), Exploration of Natural Gas, Wind Power & Solar Power Plant and Telecom Businesses. The company has formed subsidiaries/associates/joint venture companies for CGD, Petrochemicals, LNG, Gas Trading, Power Generation and Shale Gas.
2. The company has prepared its accounts as per Indian Accounting Standards (Ind ASs) w.e.f. 1st April 2016. In compliance with the Companies (Indian Accounting Standards) Rules, 2015, the company has prepared its financial statements for F.Y. 2016-17 with comparative figures for F.Y. 2015-16. The company has adjusted the impact of transition from Indian Generally Accepted Accounting Principles to Ind ASs in the opening reserve as on 1st April 2015 and in the statement of profit and loss for F.Y. 2015-16. Further, the holding company, subsidiaries, joint ventures, or associate companies of the company also need to make transition to Ind ASs w.e.f. 1st April 2016.
3. The GoI has entrusted with the company the task to execute the 2,600 km long Jagdishpur Haldia and Bokaro-Dhamra Gas Pipeline Project connecting the Eastern states of the country to the National Gas Grid. Five states, viz., Uttar Pradesh, Bihar, Jharkhand, Odisha and West Bengal will benefit from gaining access to natural gas on affordable and equitable basis. The project work is under progress as per phase-wise schedule. The Cabinet Committee on Economic Affairs (CCEA), GoI has approved a capital grant of ₹ 5,176 crore being 40% of estimated capital cost of ₹ 12,940 crore *vide* Notification no. L-14014/44/2006-GP-I (Pt. II) dated 7th October 2016. The first instalment of ₹ 450 crore was disbursed by the GoI to the company during F.Y. 2016-17. (Copy of circular separately supplied by the querist)
4. As per the querist, in accordance with the provisions of Indian Accounting Standard (Ind AS) 20, ‘Accounting for Government Grants and Disclosure of Government Assistance’, the company has accounted for the amount of capital grant under the head “Other non-current liabilities”. Further, the company has classified the amount of capital grant under “Cash flows from financing activities” in the Cash Flow Statement during F.Y. 2016-17 in line with the provisions of Ind AS 7, ‘Statement of Cash Flows’.
5. The Comptroller & Auditor General of India (C&AG) has conducted supplementary audit on the accounts of the company for F.Y. 2016-



- 17 under section 143(6) of the Companies Act, 2013. While conducting the supplementary audit of accounts, the C&AG accepted the accounting treatment made by the company. However, the C&AG has made observation on classification of capital grant by the company as *Financing Activity* in the Cash Flow Statement and opined that it should be classified as an *Investing Activity* in the Cash Flow Statement.
6. The company and its statutory auditors are of the opinion that the capital grant is one of the sources of financing the project expenditure besides loan and internal generation/equity. The company is of the view that had the company not received the capital grant, the alternate source for such financing would be either from equity or borrowings. Thus, in substance, capital grant is in the nature of a financing activity and, therefore, is correctly shown as Financing Activity.
7. However, the C&AG has not accepted views of the company/joint statutory auditors and, instead, is of the view that, since the capital grant was received specifically for investment and acquisition of long-term asset, the company should recognise the government grant as deferred income in accordance with paragraph 24 of Ind AS 20. Accordingly, the amount should be proportionately taken to income over the period of useful life of pipeline project. Unlike financing activities, viz., loan and equity on which interest/dividend is payable, the amount received as government grant will be utilised for investing activities only and, therefore, will not change the equity/borrowing of the company and should be reflected as an “Investing activity” in the Cash Flow Statement.
8. The provisional comment of the C&AG and the reply submitted by the company are as follows:

Provisional Comment	Reply
<p>III. Standalone Cash Flow Statement for the financial year ended 31st March 2017</p> <p><u>Cash Flow from financing activities</u></p> <p>The above includes ₹ 450 crore towards the capital grant received from Govt. of India for execution of Jagdishpur-Haldia-Bokaro-Dhamra Pipeline Project (JHBDPL).</p> <p>In this regard, Para 6 of Ind AS 7 states that “<i>Investing activities are the acquisition and disposal of long-term assets and other investments not included in cash equivalents</i>” while “<i>Financing activities are activities that result in changes in the size and composition of the contributed equity and borrowings of the entity</i>”.</p> <p>However, audit observed that capital grant received from GoI was for investment purpose and to meet out the capital expenditure (acquisition of long-term assets) of above said pipeline project. Thus, the same should have been classified as investing activity whereas the company has classified this grant under financing activities in Cash flow Statement.</p>	<p>It is submitted that the company has received ₹ 450 crore during the year towards capital grant approved by Cabinet Committee on Economic Affairs (CCEA), Government of India for execution of Jagdishpur Haldia Bokaro Dhamra Pipeline Project (JHBDPL).</p> <p>The long-term asset will be constructed by utilising the Government grant given for a specific purpose. The grant received, being specific, is source of funds for the creation of the said asset. If the company would not have received any grant from GoI, the alternate source for such financing would be either from equity or borrowings. Thus, in substance, capital grant is in the nature of financing activity as per the provision of Ind AS 7.</p> <p>It is also submitted that as per Indian GAAP (AS-3), the amount of grant was disclosed under Capital Reserve, which forms part of Reserves and Surplus. Further as per the provisions of Ind AS 7 also, the amount of Grant become part of Non-Current Liabilities. Thus, the nature of grant is financial activities.</p>

Provisional Comment	Reply
<p>Management / Joint Statutory Auditors replied that if the company would not have received any grant from GoI, the alternate source for such financing would be either from equity or borrowings. Thus, in substance, capital grant is in the nature of financing activity.</p> <p>Management's/Joint Statutory Auditors' replies are not acceptable as govt. grant has been received specifically for investment and acquisition of long-term asset and the company has to recognise the Government Grant as deferred income in accordance with Para 24 of Ind AS 20 which would be proportionately taken to income over the period of useful life of pipeline project. Unlike, financing activities, viz. loan and equity on which interest/dividend is payable, the amount received as Govt. grant will be utilised for investing activities only and therefore will not change the equity/ borrowing of the company. Thus, statement of cash flows is also deficient to that extent.</p>	<p>It is further submitted that the expenditures that result in a recognised asset in the balance sheet are eligible for classification as investing activities, whereas the financing activities are related to forecast claims on future cash flows by providers of capital to the entity.</p> <p>Since the grant received by the company was source of fund for creation of assets, the company has correctly classified the capital grant as financing activities.</p> <p>Further, the user is able to understand the cash receipts from grant from the disclosure in Cash Flow Statement. Hence, Provisional Comment may please not be pursued further.</p>

9. It is also pertinent to mention that Ind AS 7 does not provide any guidance on treatment of capital grant received from GoI as described hereinabove in the Cash Flow Statement as such. In view of the difference of opinion with the C&AG, it was decided to take the opinion of the Expert Advisory Committee of the Institute of Chartered Accountants of India on the said matter.

B. Query

10. The querist has sought the opinion of the Expert Advisory Committee on the following issues:
- Whether the classification of ₹ 450 crore received as capital grant from Government of India under 'Financing activities' in the Statement of Cash Flows for FY 2016-17 for the reasons mentioned in paragraph 6 above is correct as per Ind AS 7.
 - In case the answer to (i) above is not in the affirmative, what should be the appropriate classification of capital grant of such nature and purpose from Government of India in the Statement of Cash Flows.

C. Points considered by the Committee

11. The Committee notes that the basic issue raised by the querist relates to classification of the receipt of ₹ 450 crore by way of grant related to assets (hereinafter referred to as 'the grant') from the Government of India (hereinafter referred to as 'the government') in the statement of cash flows for the financial year 2016-17 in the context of Indian Accounting Standards (Ind ASs) notified under the Companies (Indian Accounting Standards) Rules, 2015 (hereinafter referred to as 'the Rules'). The Committee notes from the facts of the case that C&AG has agreed that the amount received is in the nature of government grant and not shareholder's contribution. The Committee has, therefore, considered only the issue raised and has not examined any other issue that may be contained in the Facts of the Case, such as amount to be recognised in the balance sheet and statement of profit and loss, classification, recognition, measurement and accounting treatment of grant received by the company. Further, the Committee presumes that the pipeline will be owned and controlled by the company and that the company is not

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acting only as an implementing/executing agency of the government and consequently, the pipeline or components thereof, as the case may be, will be recognised as asset(s) in the company's financial statements.

12. The Committee notes that the terms 'Investing activities' and 'Financing activities' are defined in paragraph 6 of Indian Accounting Standard (Ind AS) 7, Statement of Cash Flows, notified under the Rules, as below:

"Investing activities are the acquisition and disposal of long-term assets and other investments not included in cash equivalents."

"Financing activities are activities that result in changes in the size and composition of the contributed equity and borrowings of the entity."

13. The Committee first examines whether receipt of the grant should be classified as cash flow from financing activity in the cash flow statement. For classification as financing activity, the receipt of the grant should result in change in the size and composition of contributed equity and borrowings. Although there can be equity contribution otherwise than by way of subscription to equity shares, in the extant case, the receipt of the grant does not represent equity contribution from the government neither it is borrowing from the government.
14. As per paragraph 6 of Ind AS 7 reproduced in paragraph 12 above, only acquisition and disposal of long-term assets and other investments not included in cash and cash equivalents should be classified as investing activities. Hence, at first sight, it may appear that receipt of the grant does not meet the definition of investing activity, since the resulting cash inflow does not arise from disposal of any asset. However, in substance, to the extent of the grant, cost of the pipeline project is borne by the government. In effect, the cash outflow on the long-term asset, i.e., pipeline, is reduced by the amount of the grant. This factual position is not changed by the accounting and presentation requirements of Ind AS 20, 'Accounting for Government Grants and Disclosure of Government Assistance', notified under the Rules. Accordingly, the Committee is of the view that the receipt of the grant is an investing activity. This view is

strengthened by paragraph 28 of Ind AS 20 which states as follows:

"28. The purchase of assets and the receipt of related grants can cause major movements in the cash flow of an entity. For this reason and in order to show the gross investment in assets, such movements are disclosed as separate items in the statement of cash flows."

D. Opinion

15. On the basis of the above, the Committee is of the following opinion on the issues raised by the querist in paragraph 10 above:
- The classification of ₹450 crore received as grant related to assets from Government of India as part of cash flows from 'Financing activities' in the statement of cash flows for the financial year 2016-17 is not correct.
 - The same should be classified as part of cash flows from 'Investing activities' in the statement of cash flows for the financial year 2016-17 as discussed in paragraphs 13 and 14 above.

1.	The Opinion is only that of the Expert Advisory Committee and does not necessarily represent the Opinion of the Council of the Institute.
2.	The Opinion is based on the facts supplied and in the specific circumstances of the querist. The Committee finalised the Opinion on January 04, 2018. The Opinion must, therefore, be read in the light of any amendments and/or other developments subsequent to the issuance of Opinion by the Committee.
3.	The Compendium of Opinions containing the Opinions of Expert Advisory Committee has been published in thirty six volumes. A CD of Compendium of Opinions containing thirty six volumes has also been released by the Committee. These are available for sale at the Institute's office at New Delhi and its regional council offices at Mumbai, Chennai, Kolkata and Kanpur.
4.	Recent opinions of the Committee are available on the website of the Institute under the head 'Resources'.
5.	Opinions can be obtained from EAC as per its Advisory Service Rules which are available on the website of the ICAI, under the head 'Resources'. For further information, write to eac@icai.in . ■