

Presentation of interest earned from deployment of surplus funds with banks

A. Facts of the Case

1. A Company (hereinafter referred to as 'the Company') is a Public Sector Undertaking (PSU), incorporated as a project executing agency under section 617 of the Companies Act, 1956 on 12th July, 1999 by the Ministry of Railways (MoR) and the Government of Maharashtra (GoM) subscribing equity shares in the 51:49 ratio respectively. The main object of the Company is to plan, develop, and execute the ever-growing suburban railway transportation needs of Mumbai Metropolitan Region (MMR) by carrying out surveys, preparing survey/project reports and identifying feasible rail projects/corridors etc. The project to be executed by the Company is called Mumbai Urban Transport Project (MUTP). The other main object of the Company is to carry out the rehabilitation and resettlement of project affected persons. (A copy of Memorandum and Articles of Association have been supplied separately by the querist for the perusal of the Committee.)

2. The MUTP is planned for development over a period of time in various phases. The funds required for MUTP are provided to the Company in a 50:50 ratio by MoR and GoM as budgetary allocation in their respective annual budgets. Some of the projects are funded through a loan from the World Bank/Asian Infrastructure Investment Bank (AIIB), which are routed through GoI and GoM. The Company prepares feasibility reports and formulates estimates for MUTP which are sanctioned by MoR under MTP Plan Head in the Works, Machinery and Rolling Stock Programme of the Ministry of Railways. After sanction of projects by MoR, the funds are released/arranged for/by the Company for execution of the MUTP. (A copy of Memorandum of Understanding executed between the Company, MoR and GoM has been supplied separately by the querist for the perusal of the Committee.)

3. The Company has been incorporated as a project executing agency. As per terms of MoU/Agreements, the ownership of all the operating assets created by the Company under MUTP remains with the Indian Railways. These assets are not accounted for as assets in the books of the Company. The unique nature of accounting for funds received and utilisation in

MUTP is explained in brief hereinafter. The funds received for executing the MUTP project from MoR and GoM are accounted for as 'Funds received for MUTP Works' and are presented under 'Other Long Term Liabilities' and funds utilised on the creation of MUTP assets are accounted for as 'Funds utilised on MUTP' and presented as a reduction from 'Funds received for MUTP' under 'Other Long Term Liabilities' in the financial statements. So, effectively the net balance, i.e., excess of funds received for MUTP over funds utilised on MUTP appears as 'Other Long Term Liability' in the financial statements of the Company.

4. Since the Company is formed without any profit motive and with the object of the advancement of the general public utility with the ultimate aim of improving transportation infrastructure for the Citizens of MMR, the Company is registered under section 12A of the Income-tax Act, 1961 with the Commissioner of Income Tax (Exemption) on 29th October, 2001 w.e.f. date of incorporation, i.e., 12th July, 1999. Since its registration under section 12A, the Company has been enjoying the benefit of exemption under section 11 of the Income-tax Act, 1961. To comply with the relevant provision and to continue to enjoy the exemption under section 11 of the Income-tax Act, 1961, the Company has deleted the declaration and distribution of dividend clause from its Article of Association. Thus, the Company does not have any profit motive as its object and cannot declare or distribute any dividend.

5. The querist has stated that for the purpose of execution, depending on the nature, expertise required, and quantum of work, MUTP component works are assigned by the MoR to the Central and Western Railways, and other agencies. However, a major part of MUTP is directly carried out by the Company for which the Company receives Direction and General (D&G) Charges. Direction and General Charges are charges fixed by MoR in % terms of the amount spent on MUTP and this % is based on the nature, type and complexities of the relevant project involved and past experiences of the execution of the project of the same size and nature. While fixing Direction and General Charges of the Company, MoR

also takes into account the similar projects executed by other zonal railways of Indian Railways and Indian Railway's PSU.

6. The Company incurs an establishment cost to execute the projects allotted under MUTP. The amount of Direction and General Charges fixed by the MoR for carrying out a particular project by the Company is actually nothing but an estimated cost, based on previous experience of execution of projects of similar size and nature, which the Company would be incurring for the execution of the project. So, the Direction and General Charges are nothing but reimbursement of cost, which the Company incurs as an establishment cost to execute a particular project.

7. In addition to revenues received by way of Direction and General Charges, the Company also earns interest on funds temporarily deployed with Scheduled Banks, pending the funds' utilisation in MUTP.

8. Financial statements of the Company are audited every year by Chartered Accountants appointed by the Comptroller and Auditor General of India (CAG). In addition to the statutory audit conducted by Chartered Accountants, annual supplementary audit of the Company is also conducted by the Principal Director of CAG.

9. As stated in earlier paragraphs, in addition to the Direction and General Charges, the Company earns interest from deployment of surplus funds with the banks as stated at paragraph 7 above. The details of Direction and General Charges, establishment cost and interest earned over a period of last 9 financial years are as under:

Financial Year	D & G Charges	Establishment Cost	Deficit	Interest Income	Surplus/ deficiency
2019-2020	39.98	50.03	-10.05	29.65	19.60
2018-2019	40.39	46.88	-6.49	42.36	35.87
2017-2018	22.98	44.32	-21.34	22.96	1.62
2016-2017	31.51	36.95	-5.44	34.42	23.38
2015-2016	28.42	25.72	2.70	37.51	40.21
2014-2015	26.63	27.74	-0.61	37.18	36.57
2013-2014	17.37	25.02	-7.65	30.66	23.01
2012-2013	11.66	22.66	-11.00	23.24	12.24
2011-2012	11.79	20.22	-8.43	31.14	22.71

10. The querist has stated that from the above details, it may be observed that every year except for financial year (F.Y.) 2017-18 and F.Y. 2019-20,

the quantum of interest earned is higher than the Direction and General Charges. As explained in paragraphs 5 and 6 above that Direction and General Charges are nothing but reimbursement of cost which the Company incurs on executing the project; it is very important to note here that while deciding such % of Direction and General Charges payable to the Company, the MoR also considers the approximate amount of interest, which the Company may earn on the deployment of surplus funds during the execution of the concerned project. Thus, Direction and General Charges and interest, both, form part of the total estimated revenue required by the Company to incur the estimated establishment cost to execute a particular MUTP Project. Hence, interest, just like Direction and General Charges invariably becomes part of the revenue from operating activities of the Company. Considering the above facts and unique circumstances, the Company is of the view that such interest earned shall be classified as 'other operating revenue', if not 'operating revenue' of the Company. The querist has also referred to the minutes of meeting held in November 2000 at the juncture of foundation of the Company (a copy of the minutes has been supplied separately by the querist for the perusal of the Committee), wherein interest is considered along with Direction and General Charges as part of the total estimated cost required by the Company for executing a project and not just as an income from incidental or ancillary investment activity. According to the querist, this is an important document, tantamounting to an MoU between the Ministry of Railways and the Company at the time of the Company's inception.

11. To support the above stated contention, the querist has referred to paragraphs 9.1.7, 9.1.8 and 9.1.9 of the Guidance Note on Division I – Non Ind AS Schedule III to the Companies Act, 2013, (Revised July, 2019 Edition), issued by the Institute of Chartered Accountants of India, which read as under:

"9.1.7 For non-finance companies, revenue from operations needs to be disclosed separately as revenue from

(a) sale of products,

(b) sale of services and

(c) other operating revenues.

It is important to understand what is meant by the term “other operating revenues” and which items should be classified under this head vis-à-vis under the head “Other Income”.

9.1.8 The term “other operating revenue” is not defined. This would include Revenue arising from a company’s operating activities, i.e., *either its principal or ancillary revenue-generating activities*, but which is not revenue arising from the sale of products or rendering of services. Whether a particular income constitutes “other operating revenue” or “other income” is to be decided based on *the facts of each case and detailed understanding of the company’s activities. The classification of income would also depend on the purpose for which the particular asset is acquired or held.*

For instance, a group engaged in manufacture and sale of industrial and consumer products also has one real estate arm. If the real estate arm is *continuously engaged in leasing of real estate properties*, the rent arising from leasing of real estate is likely to be “other operating revenue”. On the other hand, consider a consumer products company which owns a 10 storied building. The company currently does not need one floor for its own use and has given the same temporarily on rent. In that case, lease rent is not an “other operating revenue”; rather, it should be treated as “other income”.

9.1.9 To take other examples, sale of Property, Plant and Equipment is not an operating activity of a company, and hence, profit on sale of Property, Plant and Equipment should be classified as other income and not as ‘other operating revenue’. On the other hand, sale of manufacturing scrap arising from operations for a manufacturing company should be treated as other operating revenue since the same arises on account of the company’s main operating activity.”

(Emphasis supplied by the querist.)

The querist has stated that from the close observations of the above stated paragraphs of the Guidance Note, it is established that the deciding criteria for a particular item of income to be

classified either as ‘other operating revenue’ or ‘other income’ are as under:

- i. whether it’s a principle or ancillary revenue-generating activity and not the activity of the sale of products or rendering of services;
- ii. the purpose for which the particular asset is acquired or held;
- iii. the frequency or continuity of the revenue-generating activity; and
- iv. on the facts of each case and detailed understanding of the Company’s activities.

12. The querist has stated that the Company fulfils all of the above-stated tests in the following manner:

- i. The Company deposits the funds received for executing MUTP with the banks pending the funds’ utilisation in the MUTP. This activity of deposit of funds with banks is carried out on a regular basis throughout the period of execution of MUTP. The interest earned on the deployment of funds with banks, pending the funds’ utilisation in MUTP, is inextricably connected to the core activity of the execution of MUTP as the size and nature of the Company and project are such that it requires funds in advance for project planning and execution. Activities of deposit of funds with the banks are made in a well thought-out, planned and prudent manner wherein the expected amount and date of receipt of funds, physical progress of the MUTP and expected amount and time of requirement/utilisation of funds in MUTP are projected, considered, reviewed and monitored in a systematic manner so as to keep uninterrupted funds’ flow towards discharging project liabilities and at the same time, interest, being part of total planned revenue of the Company, on such deposits can be maximized.

Further, how crucial and important is the activity of deposit of funds for the survival of the Company can be observed from the table given in paragraph 9 above that in the last 9 years, except for in the F.Y. 2015-16, Direction and General Charges were not able to meet the

establishment cost of the Company and in the absence of interest income, the Company would have incurred losses in every such year. So, as per the querist, the above establishes the fact beyond any doubt that along with Direction and General Charges, interest is considered as part of the total operating revenue required by the Company for meeting its establishment cost.

It may also be noted that except in the F.Y. 2019-20 and 2017-18, the quantum of interest earned is more than Direction and General Charges and on close observation, it can be seen that in a couple of years, the interest income is even more than double of the Direction and General Charges.

From the above facts, it can be derived that the activity of deposit of funds with banks, in 7 out of last 9 years, generates more income than from the activity of Direction and General Charges. It is also because of the interest income that, in 8 out of 9 years, the Company was able to generate the surplus of income over expenditure otherwise it would have made losses. So, based on the above facts, the Company is of the view that revenue generated from the activity of deposit of funds with banks is crucial, integral and inextricable part of the core revenue generating activities of the Company.

- ii. The purpose for which such assets (in the case of the Company its 'Funds received for MUTP'), are held or acquired is their utilisation in the development of MUTP, the main objective of the Company. The funds given by the MoR and GoM to the Company are deployed in banks pending their utilisation in the core operational activity of the Company, i.e., development of MUTP.
- iii. The activity of deposit of funds is carried out on a regular basis, reviewed and monitored at least on a weekly basis. While deploying the funds in banks some of the important points which are kept in mind are as under:
 - a. The amount of funds estimated for a particular project of MUTP;
 - b. The expected period of the execution of the project and its important milestones;

- c. The dates, schedule and amount of funds expected to be required for a project;
- d. The actual progress of the project;
- e. Actual funds available with the Company for the project; and
- f. Special terms and conditions related to the payment for the project.

Thus, the foundation of activity of deployment of funds is inextricably connected to the execution of MUTP and it is carried out, reviewed and monitored regularly on the same basis, frequency and manner in which the physical progress of the particular project of MUTP is carried out, reviewed and monitored.

- iv. Based on above stated unique facts and circumstances of the Company, the activity of planning and executing of deposit of funds, the inextricable nature of activity with the funding and execution of MUTP, the frequency of the activity itself, and the quantum of the interest earned year after year over the Direction and General Charges give sufficient strength and reason to treat and consider the activity of deposit of funds as an integral and inextricable part of the revenue generating activities of the Company. Hence, interest earned in the case of the Company, because of its unique facts and circumstances, is considered as 'other operating revenue'.

13. However, there is another view in respect to the classification and presentation of such interest. Note No. 4 of General Instructions for Preparation of the Statement of Profit and Loss in Part II of the Schedule III of the Companies Act, 2013 reads as under:

"4. Other income

Other income shall be classified as:

- (a) Interest Income (in case of a company other than a finance company);
- (b) Dividend Income;
- (c) Net gain/loss on sale of investments;
- (d) Other non-operating income (net of expenses directly attributable to such income)."

The other view is based on Note No. 4, as reproduced above. It is claimed that since the Company is also a company other than a finance company, interest shall be classified and presented as part of "Other Income".

The querist further wishes to bring to the notice of the Expert Advisory Committee (EAC) of Query No.11 of Volume XXXVII of Compendium of Opinions, wherein it was opined that interest should be classified as 'Other Income' and not as 'Other Operating Revenue'.

14. However, on the basis of reasons and grounds as enumerated in paragraphs 9 to 12 above and unique facts and circumstances of the Company being different from the facts and ratio of the Opinion of EAC to Query No.11, as mentioned in paragraph 13 above, the Company is of the view that the present treatment of accounting, classification and presentation of interest earned on funds deployed with banks as 'Other Operating Income' is reasonable and correct.

15. The querist has separately informed that the word 'establishment cost' in Railway parlance means the cost incurred to run an establishment. It includes all the costs of an establishment. In the case of the Company, 'establishment cost' means all the expenses incurred/debited in the Income and Expenditure Account by the Company to run its operations. The following items of expenses are establishment costs of the Company:

- i. Salary and Wages/Employee Cost
- ii. Administrative Expenses
- iii. Depreciation/Amortisation Expenses
- iv. Any other Expenses.

B. Query

16. On the basis of above, considering the unique facts and circumstances of the Company as submitted above, the Company has sought the opinion of the Expert Advisory Committee as to whether the present practice of accounting and presentation of interest earned from the activity

of deployment of funds with banks, pending their utilisation in MUTP, as 'other operating revenue' in the financial statements is correct. If not, then what should be the correct treatment and presentation of interest earned on deployment of funds with banks in the financial statements of the Company?

C. Points considered by the Committee

17. The Committee notes that the basic issue raised by the querist relates to the presentation of interest earned on the surplus/idle funds deployed with banks, viz., whether the same should be presented as 'other operating revenue' or 'other income' in the Income and Expenditure Account of the Company. The Committee has, therefore, considered only this issue and has not examined any other issues that may arise from the Facts of the Case, such as, accounting for receipt of funds provided by the MoR and GoM as budgetary allocation and utilisation thereof for MUTP, accounting for loan from the World Bank/AIIB routed through the GoI and GoM, accounting for MUTP component works assigned to other agencies, accounting for Direction and General Charges and establishment cost, application of the provisions of Accounting Standard (AS) 5, 'Profit or Losses for the Period, Prior Period Items and Changes in Accounting Policies' (if any), etc. The Committee notes from the annual report for the financial year 2019-20 that the Company is following Accounting Standards, notified under the Companies (Accounting Standards) Rules, 2006¹; therefore, the Committee has examined the issue considering these standards only. Further, the Committee has examined the issue only from accounting perspective and has not looked into the regulatory or legal aspects and implications, including those arising under Income-tax Act.

18. The Committee notes the following paragraphs of the Guidance Note on Division I – Non Ind AS Schedule III to the Companies Act, 2013 (revised July, 2019 Edition), issued by the Institute of Chartered Accountants of India (hereinafter referred to as the 'Guidance Note'):

¹In respect of accounting period(s) commencing on or after April 1, 2021, Companies (Accounting Standards) Rules, 2006 (as amended from time to time) have been superseded by Companies (Accounting Standards) Rules, 2021.

“9.1.7 For non-finance companies, revenue from operations needs to be disclosed separately as revenue from

- (a) sale of products,
- (b) sale of services and
- (c) other operating revenues.

It is important to understand what is meant by the term “other operating revenues” and which items should be classified under this head vis-à-vis under the head “Other Income”.

9.1.8 The term “other operating revenue” is not defined. This would include Revenue arising from a company’s operating activities, i.e., either its principal or ancillary revenue-generating activities, but which is not revenue arising from the sale of products or rendering of services. Whether a particular income constitutes “other operating revenue” or “other income” is to be decided based on the facts of each case and detailed understanding of the company’s activities. The classification of income would also depend on the purpose for which the particular asset is acquired or held. For instance, a group engaged in manufacture and sale of industrial and consumer products also has one real estate arm. If the real estate arm is continuously engaged in leasing of real estate properties, the rent arising from leasing of real estate is likely to be “other operating revenue”. On the other hand, consider a consumer products company which owns a 10 storied building. The company currently does not need one floor for its own use and has given the same temporarily on rent. In that case, lease rent is not an “other operating revenue”; rather, it should be treated as “other income”.

9.1.9 To take other examples, sale of Property, Plant and Equipment is not an operating activity of a company, and hence, profit on sale of Property, Plant and Equipment should be classified as other income and not as ‘other operating revenue’. On the other hand, sale of manufacturing scrap arising from operations for a manufacturing company should be treated as other operating revenue since the

same arises on account of the company’s main operating activity.”

“9.2 Other income:

...

9.2.2 All kinds of interest income for a company other than a finance company should be disclosed under this head such as interest on fixed deposits, interest from customers on amounts overdue, etc.”

From the above-reproduced requirements of the Guidance Note, the Committee notes that the ‘other operating revenue’ includes *revenue* arising from a company’s *operating activities*, i.e., either its principal or ancillary revenue-generating activities, but which is not revenue arising from sale of products or rendering of services. Thus, whether a particular income constitutes ‘other operating revenue’ or ‘other income’ is a matter of judgement considering the specific facts and circumstances of each case, and considering the nature of activity the Company is engaged into, etc. The Committee also notes that the Guidance Note requires all types of interest income in case of a Company other than finance company to be disclosed under the head ‘other income’.

Accordingly, the Committee is of the view that as per the requirements of the Guidance Note, interest income in case of a company other than finance company needs to be disclosed under the head ‘other income’ unless it is arising from the company’s operating activities (as in case of a finance company).

In this context, the Committee notes that in the extant case, the main object of the Company is to plan, develop, and execute the ever-growing suburban railway transportation needs of Mumbai Metropolitan Region (MMR) by carrying out surveys, preparing survey/project reports and identifying feasible rail projects/corridors etc. The project to be executed by the Company is called Mumbai Urban Transport Project (MUTP) and the Company is an executing/implementing agency of the GoM and MoR for carrying out MUTP. Thus, essentially the Company’s operating activities comprise activities relating to execution of MUTP.

The Committee further notes that during project execution, excess funds are deployed with banks leading to earning of interest income.

19. The Committee now examines whether the interest earned in the extant case can be considered to be arising from the Company's operating activities and in this regard, the Committee notes that the querist has stated that while deciding the percentage of Direction and General charges payable to the Company, the MoR also considers the approximate amount of interest which the Company may earn on the deployment of surplus funds during execution of the concerned project. In this regard, the querist has also referred to the following clause from Railway Board decision (minutes) taken on 11.11.2000 which states as follows:

"Staffing Pattern

3.1 The organisation should be kept lean but this shall be left to the Board of Directors of the Company. It should, however, be ensured that the size remains small enough for *the establishment costs to be contained within the D&G charges/Interest available to the Company.*" (Emphasis supplied by the querist.)

Without getting into the interpretation of the Board decision, the Committee is of the view that the above paragraph or any other paragraph in the Railway Board decision does not clearly indicate that the percentage of Direction and General charges payable to the Company has been decided after considering the approximate amount of interest which the Company may earn. Further, the above also does not indicate that interest is the compensation/consideration of operating activities of the Company, which is execution of MUTP, as discussed above. Further, the various communications between the Company and the Railway Board (MoR) while making a request to the Board to allow the Company to retain the interest (separately provided by the querist for the perusal of the Committee), also do not clearly demonstrate that the MoR allowed the Company to temporarily retain such interest as a compensation/consideration of the operating activities of the Company.

Accordingly, the Committee is of the view that in the extant case, considering the requirements of the Guidance Note and the information and facts available with the Committee, interest income in the case of the Company (being an 'other than finance company') should be disclosed under the head 'other income'.

With regard to various contentions provided by the querist, the Committee also wishes to point out that accounting treatment depends on the nature of income and mere allowing to retain or use interest income for meeting the expenditure does not change the nature of income. The Committee is also of the view that regularity or quantum of an item of income may not necessarily determine the nature of an income as operating or non-operating.

D. Opinion

20. On the basis of the above, the Committee is of the view that in the extant case, interest income should be disclosed under the head 'other income', as discussed in paragraph 19 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 September 01, 2021. 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 forty volumes. This is 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 .