

## Chapter 3 Accounting of Assets in Indian Railways

Indian Railways (IR) is a departmental Commercial undertaking<sup>30</sup> of Government of India. Provisions of Rule 18 of Government Accounting Rules, 1990 stipulate that financial results of government undertakings should be expressed in normal commercial form so that the cost of service or undertaking may be accurately known. Rule 36 of Government Accounting Rules, 1990 stipulates that department or departmental undertakings of the Government functioning on commercial lines should observe the essential formalities of Commercial Accounts to the extent prescribed by the Government. In such cases, separate commercial accounts of the department or undertaking should be kept outside the regular Government Accounts. Railway accounts should, therefore, not only secure the essential requirement of commercial accounting but also conform to the practices of Government accounting.

IR earns revenues on transporting Goods traffic and carrying Passengers across the country. As per Para 427 of Indian Railway Financial Code (Volume-I), the Appropriation Accounts should be supported by Block Account<sup>31</sup>, Capital Statement, Balance Sheet and Profit and Loss Account of the Railways. IR prepares financial statements such as Profit and Loss Account and Balance Sheet for reporting financial transactions carried out by it.

Audit conducted a study to analyze and evaluate the system of accounting of assets of the Railways, maintenance of assets records, depreciation of assets, condemnation of assets and accounting standards followed by the Zonal Railways, Construction Organization and Workshops including Production Units during 2013-14 to 2015-16. The relevant provisions contained in Indian Railway Code for Accounts Department (Part I), Indian Railway Financial Code (Volume I and Volume II), Indian Railway Code for Engineering Department and Indian Railway Permanent Way and Works Manual etc. and their compliance by the Railways in accounting of assets were examined in audit.

### Audit Findings

The aspects related to accounting of assets and exhibition of assets by the Zonal Railways and Production Units in their Block Accounts and Balance Sheets were reviewed in the Zonal Railways and Production Units. The audit findings are discussed in the succeeding paragraphs.

### 3.1 Block Account

Block Account represents all the physical assets of the Railways financed from different sources viz Capital, Depreciation Reserve Fund (DRF), Development

<sup>30</sup> Para 201 of Indian Railways Code for the Accounts Department (Part-I)

<sup>31</sup> Block Account exhibits all the physical assets financed from different sources

Fund (DF), Capital Fund (CF), Open Line Works-Revenue (OLW-R)<sup>32</sup>, Railway Safety Fund (RSF) and Special Railway Safety Fund (SRSF).

Block Account is prepared in two Parts-Part I represents the value of assets created from Loan Capital (Gross Budgetary Support) and Part II represents the value of all assets acquired or improvement cost of the assets replaced from Railway's own generation of funds (DRF, DF, and CF) including Loan Capital. Block Account is prepared under the various Plan Heads<sup>33</sup> reflecting the classes of Assets and details of assets acquired, constructed or replaced. It exhibits figures of total expenditure to the end of previous year, expenditure during the year, total expenditure to end of the year and source of fund. All the Zonal Railways and Production Units prepare the Block Accounts. Consolidated Block Accounts of IR for Commercial Lines and Strategic Lines are prepared and printed in the Detailed Appropriation Account (Annexure-G)<sup>34</sup> of IR.

### 3.1.1 Summarized position of Consolidated Block Assets of IR

The Block Accounts of IR for Commercial Lines and Strategic Lines are broadly categorized under certain sub-heads. The value of Assets under these sub-heads are summarised below:

**Table 3.1-Value of Assets shown in Block Account of IR (2015-16)**

(₹ in crore)

Sub-heads-Category	Commercial Lines	Strategic Lines <sup>35</sup>	Total
10-Preliminary Expenses	9,516.45	0.53	9,516.98
20-Land	16,770.14	6.66	16,776.80
30-Structural Engineering Works-Formation 40-Structural Engineering Works-Permanent Way 50-Structural Engineering Works-Bridges, and 60-Structural Engineering Works-Stations and Buildings	2,16,469.44	2,491.90	2,18,961.34
70-Equipment, Machinery and Plant	52,908.07	244.99	53,153.06
80-General Charges-Establishments, and 90-General Charges-Other than Establishments	19,185.62	209.52	19,395.14
1200-Purchase of New Lines	7.86	-	7.86
2100-Rolling Stock	74,023.36	12.83	74,036.19
6100-Investment in Government Commercial Undertakings-Road Services	162.53	-	162.53
6200-Investment in Government Commercial Undertakings-Public Undertakings, and 6300-Investment in Non-Government Undertakings including JVs/SPVs	32,560.92	-	32,560.92

<sup>32</sup> *New or additional improvement/replacement works (other than Passenger amenities works) costing less than one lakh from revenue.*

<sup>33</sup> *Plan Heads included activities like New Lines, Gauge Conversion, Doubling, Track Renewals, Railway Electrification, Rolling Stock, Machinery and Plant, Workshops and Production Units etc.*

<sup>34</sup> *Detailed Appropriation Accounts includes Budget and Expenditure under different Grants, Statements, Annexures, Block Account, Balance Sheet, Profit and Loss Account etc. and presented to the Parliament.*

<sup>35</sup> *Strategic Lines-Railway lines of strategic importance constructed at the request of Defence and under operation in four Zonal Railways viz. NR, NWR, WR and NEFR.*

7100-Store Suspense, 7200-Manufacturing Suspense, and 7300-Miscellaneous Advance-Capital	17,673.97	84.25	17,758.22
98-Deduct-Miscellaneous Receipts	(-) 10,765.94	(-) 25.22	(-) 10,791.16
<b>Total</b>	<b>4,28,512.42</b>	<b>3,025.46</b>	<b>4,31,537.88</b>

Source: Part II-Detailed Appropriation Accounts-Annexure 'G'-Block Account (Commercial and Strategic)-2015-16

Note-The above figures include expenditure from Capital (Gross Budgetary Support), CF, DRF, DF, RSF, SRSF, OLW-R.

Assets created under different sources of funds in IR at the end of 2015-16 were as under:

**Table 3.2-Value of Assets created in IR at the end of 2015-16**

Sl. No.	Source	Value of Assets created (₹ in crore)
1	Capital (Loan Account)	2,54,887.91
2	DRF	61,052.56
3	DF	32,921.75
4	CF	50,449.91
5	RSF	14,035.45
6	SRSF	15,756.05
7	OLW-R	1,252.32
8	Miscellaneous <sup>36</sup>	1,181.93
	Total	4,31,537.88

Source: Part II-Detailed Appropriation Accounts-Annexure 'G'-Part-II-Statement of Block Account of Indian Government Railways including Loan Account (Commercial and Strategic)-2015-16

From the above, it can be seen that the major source of assets creation in IR was GBS (59.07 per cent) followed by DRF (14.15 per cent) and CF (11.69 per cent) of the total assets created.

### 3.1.2 Exhibition of Assets in Block Accounts

Review of Block Account of IR revealed the following:

- Fixed Assets such as buildings, track structures etc. are not separately depicted in the Block Account. For maintaining transparency in the Accounts and disclosing the correct picture of all the fixed assets, the existing format of Block Account needs revision so as to exhibit the vital fixed assets for use of various stakeholders.
- In the Block Account, value of assets is shown under certain Plan Heads under each source of fund. As per Indian Railway Finance Code (Volume II), sub-head 20 is exclusively prescribed to record all expenditure on acquisition of land. Railway Board, while framing (in year 2005) the allocation rules for Plan Head 1700-Computerisation and Plan Head 3300-Signal and Telecommunication Works, had not taken into account the implication of allocating sub-head 20 for purposes other than land i.e. 1720-Passenger Reservation System and 3320-Structural Works.

<sup>36</sup> Contribution from Government of Maharashtra (CIDCO) etc.

Audit observed that expenditure amounting to ₹ 28.51 crore<sup>37</sup> was shown under sub-head-1720 and sub-head-3320 in six Zonal Railways during 2013-14 to 2015-16. As a result, the expenditure incurred on heads 'other than land' is also being shown under the sub-head 'land'.

Hence, expenditure under sub-head 20 is not reflecting the actual expenditure on 'land' in the Block Accounts of the Zonal Railways and as well as consolidated Block Account of IR. The inconsistency in allocation rules and non-correlation with prescribed columns of Block Account had resulted in wrong depiction of value of 'land' in the Block Account.

- Capital Works-in-progress<sup>38</sup> includes cost of constructing the fixed assets before construction is substantially complete. Expenditure on capital assets which are in the process of construction or near completion though forms part of the total Block Assets; it is not distinctly shown in the Block Account. Hence, the amount of capital expenditure incurred on on-going projects in the Zonal Railways was not ascertainable from the Block Accounts. The format of Block Account needs modification to exhibit the actual expenditure incurred on the on-going projects.

It was observed that there were 432 ongoing projects<sup>39</sup> (155 New Line, 42 Gauge Conversion and 235 Doubling) in IR at the end of 2015-16 wherein a sum of ₹ 1,12,744 crore was spent up to 2015-16. However, this fact was not reflected separately as 'Capital works-in-progress' in the Block Accounts of the Zonal Railways and IR.

- Any cost incurred for improvement of assets, which results in increasing the life or the utility of asset, is considered as cost of improvement. Para 430 of Indian Railway Financial Code (Volume-I), provides that the cost of improvement will be excess over the cost of replacement<sup>40</sup> of an asset at current prices by a like asset or its original cost, estimated if not known, whichever is greater. Para 723 of Indian Railways Code for Engineering Department mentions that in the estimates for replacement and renewal works, it should be clearly stated whether any improvement is involved in the proposed works and if so, the extent of such improvement should be briefly indicated so as to enable the preparation of the Block Account.

Audit observed that the above provisions for working out the cost of assets acquired through Depreciation Reserve Fund and exhibition of

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<sup>37</sup> Sub-head 1720 - ₹ 6.99 crore (2013-14-CR, NEFR), ₹ 14.39 crore (2014-15-CR, NEFR, NWR, SR) and ₹ 6.32 crore (2015-16-CR, ECoR). Sub-head-3320- ₹ 0.33 crore (2013-14-SR), ₹ 0.27 crore (2014-15-SR, SWR) and ₹ 0.21 crore (2015-16-SWR).

<sup>38</sup> Expenditure incurred against ongoing projects

<sup>39</sup> Standing Committee Report on Railways (2015-16) Sixteenth Lok Sabha Tenth Report on Pending Projects

<sup>40</sup> To be worked out on the basis of formulae given in Annexure-I of Para 430 of Indian Railway Financial Code (Volume-I).

improvement element in the Block Account were not adhered to in 12 Zonal Railways and two Production Units<sup>41</sup>. Zonal Railways were using different methods for working out the improvement element which resulted in understatement/overstatement of assets in the Block Accounts. The methods for working out the improvement element by the some of the Zonal Railways/Production Units were as under:

- In SCR, there was no uniformity in the exhibition of improvement element in Block Account and the field units were adopting different methods for calculation of improvement element.
- In NR, a fixed percentage of 59.3 was taken into account for working out the improvement element.
- In SWR and RWF, the actual expenditure incurred on the procurement of machinery was taken into account in the block Account and not on the basis of improvement element.

### 3.2 Exhibition of Assets in Balance Sheet

Balance Sheet is a statement of financial position of the organization indicating its assets, liabilities etc. at a specific point of time. Review of Balance Sheet of IR revealed the following:

- IR does not follow the system of disclosing the significant accounting policies which should form the very basis of preparation of any Financial Statement such as Accounting of Fixed assets, Depreciation and provision of liability for pension etc.
- Balance Sheet of IR depicts Block Assets at their original cost and not at depreciated value. It is, however, reduced from its account at the time of replacement/renewal or condemnation without replacement. Thus, the value of block assets as depicted in the Balance Sheet did not represent the true written down value of the assets.
- Investments<sup>42</sup> are assets held by an enterprise for earning income by way of dividends, interest and rentals for capital appreciation or for other benefits to the investing enterprise. According to Accounting Standards 13<sup>43</sup>, the accounting policy, classification of investments {long term investment, current investment, investment property (i.e. investment in land or buildings)} and profit/loss on disposal should be disclosed in the financial statements. Investments made by the Company are reflected on Assets Side of the Balance Sheet of the Company.

<sup>41</sup> CR, ER, ECR, ECoR, NR, NCR, Metro Railway/Kolkata, NWR, SR, SER, SECR, WCR, CLW and RWF.

<sup>42</sup> Accounting Standards 13 on Accounting for Investments.

<sup>43</sup> Issued by the Ministry of Corporate Affairs.

It was observed that Ministry of Railways (MoR) had invested a sum of ₹ 32,560.92 crore in Equity Shares in the various Government Commercial Undertakings, Special Purpose Vehicles (SPVs) and Joint Ventures (JVs) etc. up to 2015-16. However, these investments are being depicted in the Block Accounts under Plan Heads 6200 and 6300 instead of exhibiting distinctly in the Balance Sheets. Thus, the value of investments shown in the Balance Sheet of IR remained understated to that extent.

### **3.3 Maintenance of records**

Rules mentioned in the Codes and Manuals of IR provide that the records/registers in respect of the assets created should be maintained in the Railways. Review of status of maintenance of registers/records in the Railways revealed the following:

#### **3.3.1 Assets Register**

In order to prove the value of assets, an Assets Register<sup>44</sup> is to be maintained wherein the investment cost of all projects should be docketed. In case of projects executed by the Construction Organisation, the Assets Register should be handed over to the Open Line Organisation (i.e. Division) for retention as permanent record. There are different kinds of assets in IR viz Track, Buildings, Rolling Stock, Machinery, Bridges, Signalling and Telecom equipments, Medical equipments etc. These entire assets are to be brought in the Assets Register by the departments concerned.

Audit observed that

- Assets Register was not maintained in seven Zonal Railways<sup>45</sup> and two other units (CORE and MTP/Chennai).
- In 10 Zonal Railways and four Production Units<sup>46</sup>, the Assets Register was maintained.
- No information regarding maintenance of Asset Register was available in respect of CLW. In DLW and MCF/RBL, maintenance of Asset Register was under preparation.
- In four Zonal Railways (ECR, NWR, WR and Metro Railway/Kolkata) and two Production Units (RWF and RCF), though the Assets Registers were maintained, the same were not updated.

Thus, due to non-maintenance/non-updating of Assets Registers, value of the assets of the Railways shown in the Block Accounts could not be tallied with the initial records. There is possibility of pilferage/loss of assets due to non-maintenance/non-updating of Assets Register by the concerned departments in the Zonal Railways.

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<sup>44</sup> Para 1720 of Indian Railways Code for Engineering Department

<sup>45</sup> ER, NR, NCR, SR, SCR, SWR and NEFR.

<sup>46</sup> CR, ECR, ECoR, NWR, SER, SECR, WR, WCR, NER, Metro Railway /Kolkata, RWF, RCF, ICF, DMW.

### 3.3.2 Land and Building Registers

Land Records Register should be maintained in Chief Engineer's Office<sup>47</sup> in which details of transactions both acquisition and relinquishment of land should be noted. Land Records Register should also be maintained in Divisional Engineer's Office.

Review of the records of Divisional Engineer's Office revealed that

- Land Records Register was not maintained in four Zonal Railways<sup>48</sup>.
- In three Zonal Railways (ECR, NWR and SCR), the Land Records Register was not updated.

Similarly, in Construction Organization, Land Records Register was not maintained in Chief Engineer's Office in nine Zonal Railways<sup>49</sup> and CORE. In three Zonal Railways and two Production Units<sup>50</sup>, the Land Records Register was not updated.

Though this matter was also highlighted<sup>51</sup> by Audit in the past, there was no improvement in the system of accounting of land at Divisional and Zonal levels. In absence of proper recording of transactions of land, the value of 'land' shown in the Block Account could not be established from the records maintained in the Zonal Railways.

In terms of Para 220 of Indian Railway Way and Works Manual and Para 1977 of Indian Railway Code for Engineering Department, Zonal Railway Administrations are responsible to maintain a complete up-to-date list of all buildings both residential and service in each Division. Register should be reviewed by the Divisional Engineer every quarter to see that the information is compiled properly and the Register is maintained up-to-date. Up-to-date Building Register should also be maintained in Chief Engineer's Office and Accounts Office. It is the responsibility of the Engineering Department to maintain the list of buildings, grouped separately for each pool of residential buildings and tallied with the capital outlay.

Audit observed that Building Register was not maintained in Accounts Office of all Zonal Railways except three Zonal Railways (CR, ECoR and SER). The Engineering Department (Chief Engineer's Office and Divisional Engineer's Office) of three Zonal Railways (ER, NR and SR) and CORE did not maintain the Building Register. In eight Zonal Railways/Production Units<sup>52</sup>, though the Building Register was maintained, the same was not updated.

<sup>47</sup> Paragraph 806 (b) of Indian Railways Way and Works Manual

<sup>48</sup> ER, NR, SR, SWR.

<sup>49</sup> ER, ECoR, NR, NCR, NWR, SR, SECR, SWR, WR.

<sup>50</sup> ECR, SCR, NER, ICF/Perambur and RWF/Yehalanka

<sup>51</sup> Paragraph 4.6.2.3 of Chapter 4 of Railway Audit Report No. 24 of 2015 (Volume-II)

<sup>52</sup> CR, ECR, NWR, SCR, SWR, Metro Railway/ Kolkata, ICF/Perambur and RWF/Yehalanka

Audit further observed that the value of assets (Land and Buildings) indicated in the Block Account was not tallied with the initial records in all Zonal Railways/Production Units except three Zonal Railways and one Production Unit<sup>53</sup>.

### 3.4 Acquisition of Rolling Stocks through Indian Railway Finance Corporation

Indian Railway Finance Corporation (IRFC) is dedicated financing arm of the MoR. Since its inception in December 1986, IRFC is raising money from the market to part-finance the plan outlay of IR. Rolling Stock assets funded by the IRFC are leased to the MoR under finance lease<sup>54</sup>. IR pays lease charges to the Company (IRFC). The accounting of rolling stocks of IRFC in the books of accounts of IR was examined in audit and the followings were noticed:

- Lease charges paid to IRFC in respect of these assets have two components-Principal component and interest. Prior to 2005-06, these payments were fully met from Revenue Grant No.9-Operating Expenses-Traffic. However, from 2005-06, the accounting policy in respect of accounting of lease charges payable to IRFC was modified and the principal component was to be charged to Capital Fund (Plan Head 2200-Grant No. 16) and interest charges under Revenue Grant No.9. It was observed<sup>55</sup> that MoR had violated its accounting policy and made payment of principal component of ₹ 12,629.49 crore from Gross Budgetary Support (i.e. Capital) during 2011-12 to 2013-14. MoR admitted its aberration and from 2014-15, it restarted making payment of principal component from its own resource i.e. Capital Fund. Since the expenditure of ₹ 12,629.49 crore on principal component of lease charges was met from Capital, the same was reflected in the Block Account under source of fund 'Capital'. It was observed that during 2016-17, MoR had again made a payment of ₹ 3,999.99 crore towards principal component of lease charges to IRFC from Gross Budgetary Support (i.e. Capital) which was in violation of accounting policy.
- Expenditure on acquisition of Rolling Stocks is accounted for and depicted under Plan Head 2100 and shown in the Block Accounts. As per consolidated Block Account (2015-16), value of Rolling Stocks in IR was at ₹ 45,831.73 crore. Till March 2016, rolling stock assets (8,390 Locomotives, 45,545 Passenger Coaches, 2,04,456 Wagons, 85 Track Machines and Cranes) valued at ₹ 1,37,037 crore have been added to the

<sup>53</sup> NEFR, SWR, WR and DMW/ Patiala

<sup>54</sup> Finance lease is a lease that transfers substantially all the risks and rewards incidental to ownership of an asset to the lessee.

<sup>55</sup> Audit comments made in Para No. 1.11 of Report No.53 of 2015-Union Government (Railways)-Railways Finances

asset base of the IR with funding assistance from IRFC. However, the assets leased by IRFC to Railways which accounted for two-third of the total rolling stock of IR had not been showed as disclosure in the Block Account of the Railways.

- As per Block Account (2015-16), a sum of ₹ 35,770.27 crore was paid to IRFC towards principal component of lease charges from Capital Grant (Capital: ₹ 12,629.49 crore and Capital Fund: ₹ 23,140.78 crore). As per disclosure made below the summarised Balance Sheet (2015-16)<sup>56</sup>, the cumulative capital component of lease charges to IRFC stood at ₹ 48,470.94 crore including ₹ 12,188.66 crore (Provisional) paid up to March 2005 from revenue. Thus, ₹ 36,282.28 crore (₹ 48,470.94 crore- ₹ 12,188.66 crore) was paid from Capital Grant, whereas the Block Account depicts ₹ 35,770.27 crore paid to IRFC from Capital Grant. There is variation of ₹ 512.01 crore between the figures of payment of principal component of lease charges to IRFC shown in the Block Account and disclosure given below the summarized Balance Sheet which needs reconciliation.
- The value of assets (rolling stocks) taken on lease from IRFC are not being depicted in the Block Accounts and Balance Sheets of the Railways. However, a disclosure is being made below the Summarised Balance Sheet shown in the Printed Appropriation Accounts-Part-I-Review. As per disclosure below the summarised Balance Sheet (2015-16), total value of assets taken on lease by MoR from IRFC was ₹ 1,39,165.08 crore up to March 2015-16, whereas, the value of assets of IRFC shown in the IR Year Book (2015-16) and IRFC's Annual Report (2015-16) was ₹ 1,37,037 crore and ₹ 1,37,038 crore respectively at the end of 2015-16. Thus, there is variation in the value of leased assets of IRFC which needs reconciliation.
- MoR provides a certificate each year that the leased assets are maintained in good condition as per norms, procedures and standards. The basis of certification of existence of assets by the Zonal Railways could not be verified in audit as no separate Assets Register for rolling stocks procured through IRFC funding was maintained by the Zonal Railways.

### 3.4.1 Condemnation of Rolling Stock acquired through IRFC funding

Para 704 of Indian Railway Financial Code (Volume-I), envisages writing off the capital cost of assets abandoned without being replaced from the books by contra debit to DRF. Omission of write back adjustments for the

<sup>56</sup> Part-I-Review-Appropriation Accounts (2015-16)

condemned assets would result in avoidable payment of dividend<sup>57</sup> to general revenues for non-existing assets. Audit observed that no instructions for carrying out the write back adjustments for condemnation of assets acquired through IRFC funding were issued to the Zonal Railways by the MoR. As a result, there was no uniformity in accounting of rolling stocks which were acquired through IRFC funding and condemned in the Zonal Railways. The following instances were noticed:

- In two Zonal Railways (NEFR and WCR), value of condemned rolling stocks acquired through IRFC funding was reduced through write back adjustments. However, no reduction in the value of rolling stocks acquired through IRFC due to condemnation was made in two Zonal Railways<sup>58</sup>.
- In SCR, audit had pointed out (2012-13 and 2013-14) the issue of non-exhibition of value of condemned rolling stock acquired through IRFC funding (₹ 4.97 crore) in the 'Statement of Credits to Capital for retired assets'.
- In SER, no write back adjustment for rolling stocks acquired through IRFC funding amounting to ₹ 38.30 crore condemned during 2013-14 to 2015-16 were carried out and also not shown in the Statement of Credits to capital for retired assets.

Thus, the value of assets (Rolling stock) shown in Block Accounts were overstated due to non-carrying out the write back adjustments for condemned/non-existing rolling stocks.

#### 3.4.2 Distribution of lease charges among the Zonal Railways

The lease charges viz principal component and interest charges are paid to the IRFC for the leased assets. Lease charges are distributed by the Railway Board among the Zonal Railways. Review of distribution of lease charges revealed the following:

- Separate records are not being maintained at Zonal Railways levels to identify and segregate the value of assets acquired through lease.
- The basis of distribution of lease charges (both principal component and interest charges) could not be checked in audit as relevant records were not made available by the Railway Board. MoR vide its letter dated 04 December 2017 stated that apportionment of lease charges amongst the Zonal Railways is done differently for each category of rolling stock as given below:

<sup>57</sup> *Railway Convention Committee recommended that Dividend to General Revenues by the Railways may be waived off for 2016-17. After merger of Railway Budget with General Budget from 2017-18, GOI decided to exempt Railways from payment of Dividend to General Revenues.*

<sup>58</sup> *SCR and SER*

**Wagons** – The apportion of lease component of wagons is done on the basis of targeted wagon holding issued from time to time by the Traffic Transportation Directorate.

**Locomotives and Coaches** - On the basis of ownership holding as provided in the Annual Statistical Statement by Statistics Directorate.

**Track Machines** – In the ratio of actual IRFC investment on Track Machine provided to individual Railways.

From the above, it is evident that principal component and interest is not being distributed on the basis of rolling stock etc. actually held by the Zonal Railways. The ad-hoc distribution may result in understatement/over statement of principal component of lease charges in the block account besides impact on operating ratio of the Zonal Railways.

### 3.5 Accounting and disclosure of EBR (IF) funded projects

IR had started borrowing funds<sup>59</sup> from institutional sources so as to ensure availability of funds for completion of projects (viz. New Lines, Gauge Conversion, Doubling, Traffic facility works and Railway Electrification etc.) critical for the Railways for generation of revenues. EBR (IF)<sup>60</sup> funded projects would be treated like Deposit Works for accounting of funds flow. Each Zonal Railway shall operate an account for EBR (IF) funded projects in Deposit Misc. Register.

Audit observed that a sum of ₹ 9,887.95 crore<sup>61</sup> was spent under EBR (IF) during 2015-16. However, this fact was not indicated in the Block Accounts of the concerned Zonal Railways and in the consolidated Block Account of IR for the year 2015-16 as a disclosure for expenditure incurred in the railway projects through EBR (IF) funding.

### 3.6 Accounting of Rail Vikas Nigam Limited (RVNL) Projects

As per Procedure Office Order (POO) issued vide Railway Board's letter No. 2011/AC.II/1/6/RVNL dated 30-12-2016<sup>62</sup>, ownership of the assets created by RVNL would vest in it, until these are transferred to Railways. After physical completion of a project by RVNL, the asset would be straight away transferred to concerned Zonal Railways. The Zonal Railways will add the value of the created assets in their Block Accounts<sup>63</sup>.

<sup>59</sup> Paragraph 1 of P.O.O. No. 2015/FS Cell/1/2 dated 23.10.2015.

<sup>60</sup> Extra Budgetary Resources-Institutional Finance (Life Insurance Corporation of India)

<sup>61</sup> Expenditure under EBR (IF) during 2016-17 was ₹ 11,465.15 crore as reported by Accounts Directorate of Railway Board.

<sup>62</sup> In supersession of Procedure Office Order No. 2011/ACII/1/6/RVNL dated 17-12-2013

<sup>63</sup> Paragraph 2.2.2 and 2.3.1 to 2.3.3 of Revised P.O.O. No. 2011/AC II/1/6 /RVNL dated 30-12-2016

As per POO, RVNL will provide year wise details of expenditure to Railway Board. The Railway Board will pass on the information to NR. In turn, NR will transfer these projects to respective Zonal Railways. This would involve transfer without financial adjustment from Plan Head 6300 under NR to the appropriate Plan Heads under the concerned Zonal Railways. The Zonal Railways shall debit its relevant plan heads under relevant source of finance. Projects once completed will remain as leased assets in the books of RVNL till the loan is completely repaid even after the project is transferred to Zonal Railway<sup>64</sup>. The cost of asset shall be progressively reduced in the books of RVNL with the capital repayment component and corresponding amount will be added in the Block Account of Zonal Railways every year.

Test check of records revealed that

- Procedure envisaged in the POO was not implemented in eight Zonal Railways<sup>65</sup>.
- Investments in the Government Commercial undertakings, SPV and Joint Ventures etc. are still being shown in the Block Account of NR which clearly indicates that no action has been initiated to transfer the value of projects completed by RVNL to the concerned Zonal Railways to exhibit under the respective plan heads through financial adjustments. Though there was no impact in consolidated Block Account of IR, the Block Accounts of the concerned Zonal Railways remained understated to that extent.

### **3.7 Depreciation policy of IR**

As per the commercial system of accounting, depreciation, representing the reduction in value of assets on account of wear and tear and usage over the estimated economic life, obsolescence, is charged to the income statement every year. Depreciation policy forms an important part of the overall financial accounting. Disclosure of accounting policies for depreciation followed by the enterprise is necessary to appreciate the view presented in the financial statements of the enterprise.

Para 340 of Indian Railway Financial Code (Volume I) mentions that Budget Estimate for appropriation to DRF is based on the replacement programme including arrears of depreciation, if any, to be made good during the following year. Such an estimate is not an isolated exercise for its purpose of annual budget but is a part of the overall resources planning of the railways determined earlier for the five year plan period in consultation with the Planning Commission and the Ministry of Finance and as approved by the Railway Convention Committee. In the Para 340 of Indian Railway Financial Code (Volume I) it has been

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<sup>64</sup> Paragraph 6.3.3 of Revised P.O.O. No. 2011/AC II/1/6 /RVNL dated 30.12.2016.

<sup>65</sup> ECoR, NWR, SR, SCR, SER, SECR, SWR, WR.

mentioned that even though the estimate of appropriation to DRF is prepared by the Railway Board, the amount finally fixed is distributed over the Railways on the basis of Capital-at-charge<sup>66</sup> of each Railway at the end of the previous year.

Review of appropriation to DRF, its distribution and status of fund balances in the Zonal Railways and Production Units revealed the following:

- IR depicts assets at their original cost and not at depreciated value. Appropriation to DRF is not being made in a scientific manner taking into account the historical cost, expected useful life, expected residual value of the depreciated asset. MoR is appropriating funds to DRF depending on likely withdrawals, balance available and financial position of the Railways. The system in vogue in IR is to set apart an adhoc sum towards contribution to DRF by charging off to the working expenses. This gives leverage to IR to manage the net revenue surplus at the desired level.
- The appropriation to DRF is distributed Zone-wise in proportion to the Block Account (i.e. value of assets held) of each Zonal Railway instead of proportion of Capital-at-charge of the previous year as provided in the Indian Railway Financial Code. In IR, as a whole, the percentage of appropriation to DRF with reference to Block Accounts worked out to 2.71 (2013-14), 2.38 (2014-15) and 1.53 (2015-16) as shown below:

**Table 3.3-Value of Block Assets and Appropriation to DRF**

*(₹ in crore)*

year	Value of assets as per Block Accounts (of the previous year)	Appropriation to DRF during the year	Percentage of appropriation to DRF w.r.t Block Accounts
2013-14	2,98,644.25	8,100	2.71
2014-15	3,34,727.24	7,975	2.38
2015-16	3,79,826.02	5,800	1.53

*Source: Part II-Detailed Appropriation Accounts-Annexure 'G'-Block Account (Commercial and Strategic)-2015-16 and DRF Account.*

Thus, the appropriation to DRF was not being made by IR in a well founded manner resulting in backlog of replacement and renewal of over aged assets in the railway system. MoR admitted<sup>67</sup> that appropriation to DRF should be made in a well founded manner. Also, the Railways have a very large assets base whereas the financial position of the Railways has not remained stable most of the times so as to permit appropriation to DRF as per a set formula. However, all along, endeavour has been to ensure maximum appropriation to DRF permissible by the Railway financial position in a year.

- The average life of various category of assets (Civil Engineering Assets, Mechanical Assets, Signalling and Telecommunication Assets and Electrical Assets) are mentioned in the Para 219 of Indian Railway

<sup>66</sup> *Capital-at-charge represents Central Government's investment in Railways by way of loan capital and value of assets thus created*

<sup>67</sup> *Action Taken Note on Para 11 of Report No. 53 of 2015-Railways Finances (September 2016)*

Financial Code (Volume I). Thus, based on the average life of assets, appropriation to DRF needs to be provided to replace/renew of worn-out assets in time.

- Due to less appropriation and more withdrawal from the fund, there was negative balance under DRF in nine Zonal Railways and three Production/other units<sup>68</sup> at the end of 2015-16. MoR, in its reply, had stated (July 2017) that distribution of DRF is done proportionately on the basis of the Block Account whereas outgo from the fund is need based. Hence, the negative balance in some Zonal Railways cannot be ruled out which are offset by the positive balances on the other railways. The contention of MoR is not tenable as the appropriation to DRF is charged to the working expenses which ultimately affect the Operating Ratio of the Railways. Also, the withdrawal from the fund is equally important to timely renew/replace the over aged assets.
- There was a meagre balance of ₹ 32.78 crore in DRF at the end of 2015-16<sup>69</sup>. The throw forward value of assets to be replaced from DRF (up to 2015-16) was ₹ 41,274.49 crore<sup>70</sup>. Non-availability of funds under DRF to replace the over aged assets is indicative of weak financial health of IR. MoR needs to appropriate required funds under DRF so as to clear the huge backlog of renewal and replacement of over aged assets in railway system for safe running of trains.

### 3.8 Accounting Reforms in IR

IR had taken up a project (February 2006) on Accounting Reforms for implementation of practices which are in line with the commercial accounting and reporting. The project was to be completed in 30 months. Delay in submission of Report by the consultants and its acceptance by the MoR was commented upon in the Audit Reports<sup>71</sup>. Though the consultants had submitted their Report in July 2010, there were number of limitations and gaps with reference to Terms of Reference (TOR)<sup>72</sup>. After rounds of further consultations, in July 2013, the consultants agreed to address the gaps and limitations. The revised Report was circulated to all the Directorates of Railway Board in June 2014 for comments. The consultants were asked to test the proposed

<sup>68</sup> CR,ER,NCR,SCR,SER,SECR,SWR,WR,WCR,,ICF,CORE,MTP/Chennai

<sup>69</sup> DRF balance at the end of 2016-17: ₹ 450.50 crore

<sup>70</sup> Throw forward value of assets (up to 2016-17) estimated at ₹ 47,679 crore

<sup>71</sup> Para 3.5 of Audit Report No.33 of 2010-11-Union Government (Railways)-Railways Finances and Para 1.12 of Audit Report No.53 of 2015-Union Government (Railways)-Railways Finances

<sup>72</sup> The terms of reference of the Consultants included ensuring compilation of government accounts as per the accounting standards stipulated by GASAB, compilation of Railways' accounts in commercial accounting form as per Generally Accepted Accounting Principles (GAAP), costing of train operations and ensuring activity based unit costing for cost analysis and cost control management.

recommendations in the field units through pilot study in one Division. However, the consultants had reservations on this, as a pilot study was not covered in the TOR.

In December 2014, MoR engaged Accounting Research Foundation of the Institute of Chartered Accountants of India (ICAI) to validate the Accounting Reforms Report of the consultants, conducting pilot study and compiling the detailed Accrual Accounting Manual for the propose of implementation of accrual based commercial accounting in the Zonal Railways and Production Units. While the pilot study had been completed in NWR (October 2016), the same is in advanced stage of completion in RCF. MoR has planned to roll out all the three Modules<sup>73</sup> of Accounting Reforms by February/March 2019 across IR.

### **3.9 Conclusion**

Financial Statements are a structured representation of the financial position and financial performance of an organisation. The objective of financial statements is to provide information about the financial position, financial performance and cash flow of an organisation that is useful to a wide range of users in making economic decisions. Thus, a complete set of financial statements consist of Balance Sheet, Income Statement/Profit and Loss Account and notes comprising summary of significant accounting policies, schedules and notes to the financial statements.

IR, as a departmental commercial undertaking, though prepares Balance Sheet and Profit and Loss Account besides Block Account, does not disclose the significant accounting policies which forms the basis of preparation of financial statements like accounting of fixed assets, depreciation, valuation of investments etc. As a result, key information like capital works-in-progress, depreciated value of assets, investments in property, plant and machinery, improvements in utility of assets etc. are either absent or cannot be recognized easily from the financial statements.

The formats of Block Account and Balance Sheet have not been revised to distinctly exhibit the capital works-in-progress in Block Account, exhibition of the investments in the Balance Sheet etc. Audit observed that no disclosure of assets (rolling stocks) acquired through IRFC funding and value of projects executed under EBR (IF) funding were incorporated in the Block Accounts and Balance Sheets of the Zonal Railways and IR as well. Assets Registers, Land and Building Registers etc. were either not maintained in the Zonal Railways and Production Units or maintained but not updated to reflect the true value of assets created.

The system in vogue in IR is to set apart an adhoc sum towards contribution to DRF by charging off to the working expenses. The present policy results in under

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<sup>73</sup>*Module-1-Accrual Accounting, Module-2-Performance Costing, Module-3-Outcome Budgeting*

provisioning of depreciation and inadequate maintenance/replacement of assets. Existing policy of depreciation gives leverage to IR to manage Net revenue surplus at a desired level.

### 3.10 Recommendations

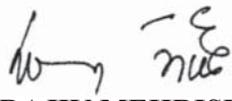
- *Indian Railways needs to ensure that Block Accounts and Balance Sheets of Zonal Railways and Production Units should reflect the true value of the assets duly supported by Assets Registers. Preparation of Assets Registers should be made mandatory for each Zonal Railways and Production Units.*
- *Indian Railways should follow the system of disclosing the significant accounting policies forming the basis of preparation of financial statements such as accounting of fixed assets, depreciation, investments etc.*
- *Ministry of Railways needs to make provision for depreciation in a more scientific method by adopting relevant Accounting Policies.*

New Delhi  
Dated: 05 February 2018

  
(NAND KISHORE)  
Deputy Comptroller and Auditor General

Countersigned

New Delhi  
Dated: 06 February 2018

  
(RAJIV MEHRISHI)  
Comptroller and Auditor General of India