Report on Means of Finance
Guidance – 4
Regulatory perspective to the certifying Chartered Accountant for Report on Means of Finance
Date: 16th March, 2020

Real estate promoters are aware of various opportunities and risks involved in project execution (availability of additional FSI, material price escalation, labour/machinery availability and rate risk, sales/demand risk etc.). However, they have to devise their project execution plans and strategies so as to appropriately mitigate the risk of non-delivery by due date and resultant circumstances leading to liquidity requirements management for allottee refunds. Moreover, sound financial planning encompassing various contingencies and their mitigation plan would certainly lead to swift project execution ensuring timely completion and delivery to allottees. Under the circumstances, Report on Means of Finance for Real Estate project is an essential tool for project planning and execution, which makes the promoter aware of overall financial requirements and challenges of funding, liquidity, refinancing, etc. and RMoF also empowers the promoter by making him aware of various options available to him for ensuring necessary resources for project execution at project planning stage itself.

Relevant Provisions in The Real Estate (Regulation & Development) Act, 2016 and Rules thereunder - The Rule 3 (6) of The Gujarat RERA (General) Rules, 2017, states as under:

> *"The promoter shall disclose,- estimated cost of real estate project as envisaged by the promoter by bifurcating the same into the market value of the land/ lease charges (as determined by the Government Approved Valuer), cost of construction, other costs, interest, taxes, cess, development and other charges and all other charges/cost in relation to the project in two stages, i.e. before the application is made to the Authority for registration of the real estate project and subsequent to the grant of the registration;* ***the means of financing the real estate project along with the cost already incurred and paid by the promoter out of the estimated cost of the real estate project duly certified and signed by the chartered accountant****;"*

The Report on Means of Financing the Real Estate Project is required to be duly certified and signed by the Chartered Accountant (**Circular 19 read with Circular 21)** in accordance with the "Report on Examination of Prospective Financial Information" as per "Standard on Assurance Engagement 3400" issued by the Institute of Chartered Accountants of India. He should obtain sufficient appropriate evidence as to whether:

a. management's best-estimate assumptions on which, the prospective financial information is based are not unreasonable and, in the case of hypothetical assumptions, such assumptions are consistent with the purpose of the information;
b. the prospective financial information is properly prepared on the basis of the assumptions;

c. the prospective financial information is properly presented and all material assumptions are adequately disclosed, including a clear indication as to whether they are best-estimate assumptions or hypothetical assumptions; and
d. the prospective financial information is prepared on a consistent basis with historical financial statements, using appropriate accounting principles.

This would be critical not only for the timely completion of the project, but also for other liabilities under *Section 18 (1) of RERA, 2016 that is, "If the promoter fails to complete or is unable to give possession of an apartment, plot or building;*

(a) in accordance with the terms of the agreement for sale or, as the case may be, duly completed by the date specified therein; or
(b) due to discontinuance of his business as a developer on account of suspension or revocation of the registration under this Act or for any other reason,

he shall be liable on demand to the allottees, in case the allottee wishes to withdraw from the project, without prejudice to any other remedy available, to return the amount received by him in respect of that apartment, plot, building, as the case may be, with interest at such rate as may be prescribed in this behalf including compensation in the manner as provided under this Act:

Provided that where an allottee does not intend to withdraw from the project, he shall be paid, by the promoter, interest for every month of delay, till the handing over of the possession, at such rate as may be prescribed."

Guidance for Certifying Report on Means of Finance

1. **Standard on Assurance Engagements 3400:**
   A statement on Means of Financing the Real Estate project is required to be duly certified and signed by the Chartered Accountant [Rule 3(6) of Gujarat RERA General Rules]. Certified by Chartered Accountant means "Report on Examination of Prospective Financial Information" issued by the Chartered Accountant in accordance with the "Standard on Assurance Engagements 3400 (SAE 3400)". Professionals are expected to carry out their assignments in full compliance with the standards set out by the ICAI, this guidance is to make them aware and aligned to the regulatory perspectives of GujaratRERA for relying on CA certified RMoF and to elaborate on operational aspects that are to be considered by Promoters and Chartered Accountants for preparation and certification of RMoF.

2. **Estimate of Cash Outflows:**
   Estimated project costs mentioned in RMoF should be in sync with various Estimated Project Costs shown in the Form – 3. Land Cost & Development cost related to construction activities, payments to statutory authorities, etc. provided in means of finance should be within the Project end date declared in Form-B. All these costs have to be bifurcated in Pre-RERA Registration cost and prospective cost on quarterly basis.

a) Land Cost

Payment of Land cost has to be in accordance with legal documentation (e.g. payment terms of Development Agreement/purchase agreement of land, etc). Computations in RMoF for payment of land cost has to be as per terms and conditions mentioned in legal documents.

b) Development Cost

Chartered Accountant shall ensure that the Promoter has to plan and plot start date and end date for various activities for Block wise construction and development of common amenities. This exercise enable promoter to have quarterly construction schedule/plan of his project available with him. Computation of development cost and onsite overheads shall have to be based on the construction schedule, bill of material and bill of quantity and other base information.

c) Interest Cost and Repayment of Borrowed funds

Computation of Interest cost has to be aligned with borrowing plan of the promoter. Careful assessment of requirement, quantum, timing and cost of borrowed funds be carried out and the Interest cost estimates be made. Cash outflows on repayment of borrowed funds has to be in accordance with the borrowing plan and/or contractual obligation of the promoter in case of institutional borrowings.

d) Other Cost (Not forming part of Form – 3 Estimated Cost)

Advertisement, Marketing, Administrative and other costs which do not form part of Estimated Cost (Form-3) of real estate project, but are essential for real estate business, should be reported in Means of Finance under this head.

3. Estimate of Cash Inflows:

Veracity of the sources of the fund utilized for financing the project till the date of verification of books of account should be verified.

a) Promoter's Capital

Computation of promoter contributions be made considering Promoter's capacity to infuse capital assessed with supporting documents like Equity capital contribution, availability of reserves & surplus along with composition of liquid and bankable assets reflecting the solvency of the promoter/entity. Further, the individual partner's and director's capacity to infuse necessary capital should also be assessed and documents like past Income Tax Returns, partnership shares in another concern/s, etc. shall be considered as supporting documents for preparation RMoF.

b) **Receipts from allottees:**

Chartered Accountant shall ensure that the promoter formulates the marketing and sales plan for the real estate project depicting quarterly sales and Projection of Receipts from allottees. Adequate emphasis be made on demand of projects of similar type, scale, segment in the area of the project. Further, such projections shall also be in sync with projected Construction stages of the project leading to percentage completion-based receipts from the allottees. Booking trends of past projects of the promoter can be considered for sales forecast of units in project being undertaken by a particular promoter/group.

c) **Institutional Loans**

Careful assessment of requirement, quantum, timing and cost of borrowed funds be carried out in the light of borrowing plan for computation of Institutional Loans. When real estate project is to be funded by institutional loan, documents reflecting promoter's line of credit and tie ups with Banks / Financial institutions should be verified by certifying Chartered Accountant before submitting the same before the Authority. When institutional loan is backed by collateral other than the project assets, repayment of the loans can go beyond project completion date.

d) **Other Borrowings**

Other borrowing in form of contribution & support from friends and relatives by way of unsecured loans is another source of fund for execution of real estate project. Reliance upon other borrowings for execution of the project be computed in light of borrowing plan of the promoter. Extent, Timing and Quantum of unsecured loans be computed considering past history of such transactions done by the promoter/entity or group.

Financing Mix Options:

Means of Financing Plan of the Project should be cash-positive in all quarters to ensure liquidity on hand. Computations of cash inflows in accordance with the guidance provided in above paragraphs would required the Promoter and Chartered Accountant to opt for an appropriate financing mix for the project considering project and promoter specific circumstances. For Capital strong promoter/entity reliance on borrowed funds may not be required. Whereas for promoter not having proven track record for borrowed fund raising, wherewithal for own capital infusion has to be demonstrated.

Reliance on allottee contributions coupled with contractual obligations for payments towards land as per development/purchase agreement requires framing of the optimal financing mix, which has to demonstrate necessary liquidity for servicing of these scheduled obligations, for which additional capital infusion or contractual deferment of payments towards land dues may be considered so as to ensure uninterrupted construction of the project. The need for capital infusion may also be substituted by borrowed financing where the promoter has institutional arrangement or proven track record for the same.

Empirical data with authority reveals that the principal cause of slow construction progress of registered projects is liquidity crunch and absence of contingency mitigation plan with the promoter. Requirement for framing the financial plan for project execution at the time of registration is aimed at making available a well thought plan with the promoter for ensuring necessary liquidity with promoter for smooth execution of construction activities in a time bound manner so that he can fulfil his promise of Delivery of Real Estate by Project End Date.

Objective preparation of RMoF encompassing this guidance will surely contribute to project executions being well-planned and well-managed, protecting interests of all stakeholders and contributing to thriving real estate sector in the State of Gujarat.