

Query No. 3

Subject: Timing of capitalisation of transmission lines and sub-stations as an item of Property, Plant and Equipment from capital-work-in-progress and also in case of modernisation work.¹

A. Facts of the Case

1. A Company (hereinafter referred to as ‘the Company’) is a registered company under the Companies Act, 1956, incorporated on 28-07-1999 and is wholly owned by the State Government with an authorised share capital of INR 1000 crore. The Company was formed by carving out the generation, transmission and distribution function of the erstwhile State Electricity Board. The Company is mainly vested with the functions of transmission of power in the entire State, governed by the provisions of the Electricity Act, 2003. It operates under a license issued by the State Electricity Regulatory Commission. The Company has adopted Indian Accounting Standards (Ind ASs) from 01.04.2016 onwards.

2. The Company is having Property, Plant and Equipment (PPE) to the tune of INR 21,619.58 crore as on 31/03/2020. The assets are being procured by way of:

- (a) Acquisition
- (b) Purchase
- (c) Gift/Consumers’ Contribution
- (d) Construction of Transmission Lines and Sub-Stations

3. Sub-Stations (Plant and Machinery) and transmission lines (lines and cable network) are the major constituents of PPE of the Company. Work of construction of these sub-stations and lines are being carried out by the Company through turnkey contracts. The installation of equipments at sub-station premises and drawing of transmission lines from one station to other are being executed by turnkey contractors under the guidance and supervision of the Company’s engineers. The materials required for these works will be inspected in the works of the vendors, and then dispatch instructions are issued upon confirmation of these materials meeting the technical requirements of the Company. On receipt of the materials at site, they will be verified by the engineer-in-charge of the works for physical damages etc.

4. As per section 162 of the Electricity Act 2003, the Chief Electrical Inspectorate to Government (CEIG) of the State has to inspect the premises. The main objective of the Department of Electrical Inspectorate is to ensure that all electrical installations in the State are installed and maintained as per the relevant safety codes and standards. As such, the new installations will be inspected by the Electrical Inspectorate Authorities by giving preference to ensure adherence of required safety clearances of live points from adjacent structures, from ground and from other live points and for safe and proper erection of equipments. This is being strictly carried out with a specific intention to avoid the danger to human beings and animal life in particular and damage to the property in general. The Department is entrusted with the responsibility of ensuring the safety requirements in generation, transmission, distribution and utilisation of electrical power.

5. After completion of CEIG inspection, constructed line/stations have to be connected to the existing line/station, which require lines clearance from the concerned Electricity Supply Company (ESCOM) and Transmission Lines and Sub-station Divisions (TL&SS Divisions).

¹ Opinion finalised by the Committee on 11.4.2022.

Line clearance means, for energising newly constructed station, electrical power from existing station which is supposed to supply power to new station is to be interconnected. Existing station is already catering power to various stations; hence entire transmission activity in the existing station has to be temporarily diverted to other stations and keep the station idle till the equipments in the newly constructed station are connected to existing station power source line. The entire process of interconnection of newly constructed station and existing station and testing requires 2 to 3 months' time. Obtaining line clearance in large cities like Bangalore is very difficult and may require some more time. Further, pre-commissioning tests will be conducted by Relay Testing (RT) Division of the Company to ensure proper installation including wiring of the equipments. Results of the testing are recoded in a separate register for having completed the tests.

6. The equipment/materials installed in the sub-stations and transmission lines will be energised only after getting the approval from the chief electrical inspectorate authorities (CEIG) and the successful completion of the pre-commissioning tests by relay testing (RT) wing of the Company. Once the erection of all the equipments is completed, the RT wing of the Company conducts pre-commissioning checks of all the equipments installed to ensure the intended performance of the equipments meeting the stipulated technical specifications and then, by extending power supply to the equipments, these will be energised and their performance will be observed by conducting stipulated tests. Load (power) will be transferred on to the new equipment by re-arranging the existing network and then only, it can be said that the equipment is 'available for use'.

7. After completing the inter-connection works by availing line clear, the equipments will be commissioned in the presence of RT wing, the representatives of manufacturers and the contract agency. The loads will be taken on the newly installed equipments thereafter. Once all the tests are completed and line clearance from ESCOMs are obtained, constructed stations/transmission lines are charged (energised), technical authorities of the Company will issue asset commissioned certificate for having energised the station/lines. Based on the asset commissioned certificate, the accounts section of the Company will categorise the work cost (Capital Work in Progress-CWIP) as PPE.

8. The querist has summarised the procedure: the assets will be constructed by the turnkey contractor → pre-commissioning test by the RT wing of the Company will be done → availability of the source line will be ensured → CEIG does the Inspection → CEIG approval will be received by the Company → Test Run → Problems rectified and again tested by RT wing of the Company → Line clearance from ESCOM will be received (for outflow of power) → Station/Line will be connected to the electricity network → Asset commissioned certificate is issued by the Company's engineers.

9. The querist has also drawn attention to the fact that, other than the modernisation work of stations/lines, the initial capital work of construction of an asset is done mostly on requisition letter received from the respective ESCOMs. The Company recovers the cost from ESCOMs by way of tariff rates fixed by the State Electricity Regulatory Commission from time to time. After all the assets are tested and ready for operation, the same will be intimated to the concerned ESCOMs for taking the load by connecting their terminals to the Company's equipment. If line is not connected (output of power from the concerned new assets constructed by the Company) by ESCOMs, then the Company does not wait for capitalisation/categorisation of assets as there is no fault from the Company's end.

10. According to the querist, as the process of commissioning involves many steps, auditors are raising objection on timing of categorisation of assets (transferring from Capital

Work in Progress to PPE Account). The audit observation from Comptroller and Auditor General (C&AG) and reply given by the management are given below:

AE No.	Enquiries	Replies
1	<p>MWD North <u>Statement of Profit and Loss</u></p> <p>Expenditure</p> <p>Note - 31- Depreciation & Amortisation- Rs. 953.72 Cr</p> <p>The above includes Rs. 2,91,42,856 towards depreciation charged, on the value of four fixed assets categorized during the year 2019-20, from the date of commissioning of the asset instead of from the date of CEIG approval, which is not in order.</p> <p>As per paragraph 55 of Ind AS 16, the depreciation of an asset begins when it is available for use, i.e., when it is in the location and condition necessary for it to be capable of operating in the manner intended by the Management. Based on the date of approval accorded by the Chief Electrical Inspectorate to Government (CEIG) against each work order, the transmission lines and sub-stations are charged. Hence, on the date of approval accorded by CEIG, the transmission lines and sub-stations are ready to take the load, i.e., ready to use. Accordingly, the depreciation needs to be charged from the date of approval of CEIG.</p> <p>A test check of assets categorized during 2019-20 revealed that in respect of four assets at Brindavan, Vidyanagar (UG cable from BIAL to Vidyanagar), Nelamangala and Tubagere, the date of commissioning was subsequent to the date of approval of CEIG. <i>However, the depreciation was charged from the date of commissioning instead of charging the depreciation from the date of CEIG approval, from which date the asset was ready to use. Hence, charging depreciation from the date of</i></p>	<p>Sub-stations and Transmission lines after completion of construction have to be inspected and certified by the Chief Electrical Inspectorate to Government (CEIG) before commissioning of the said assets. The major objective of the inspection is to ensure safety, proper working of machinery, calibration of equipment installed etc.</p> <p>Newly constructed line/station has to be connected to the existing line/station, which requires line clearance on 220, 66kv lines/stations. Concurrence has to be obtained from the concerned ESCOM and TL&SS Division. RT division engineers have to conduct final testing on equipment before commissioning.</p> <p>Intention of the Management is to utilise the constructed asset in transmission of power and to generate revenue. Hence, Certification by CEIG cannot be construed as asset is capable of operating in the manner intended by the Management.</p> <p>Hence, Audit para may kindly be dropped.</p>

	<p><i>commissioning was not in order as it resulted in short provision for depreciation amounting to Rs. 81.66 lakh.</i></p> <p>This has resulted in understatement of depreciation and overstatement of Profit by Rs. 81.66 lakh.</p>	
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(Emphasis supplied by the querist.)

Additional view of the Company: It is learnt from the technical authorities in the field, that the CEIG is inspecting with a view to ensure safety, by verifying space clearance in respect of some equipments and height clearance in respect of transmission lines, and generally they do not carry any measurement equipment. They also verify equipment registers to ensure readings provided by manufacturer of the equipment and reading measured by the Company's engineers at the delivery spot are tallying. Based on the above findings, the CEIG will issue approval for commissioning the stations/transmission lines.

AE No.	Enquiries	Replies
2	<p>MWD North Balance Sheet</p> <p>Non-current Assets</p> <p>Note - 3 – Capital Work-in-progress - Rs. 3519.23</p> <p>The above includes Rs. 8,20,00,207 towards cost of construction of 1x12.5 MVA, 66/11 KV sub-station at Mandur, which was not categorized till date, which is not in order.</p> <p>It was observed that all work relating to construction of sub-station was completed in 2009-10 and the capital expenditure was accounted for in August 2015. However, the work order was not closed for want of 66 KV source line from Budigere to Mandur. The work was terminated on 23.1.2017.</p> <p>As per paragraph 55 of Ind AS 16, the depreciation of an asset begins when it is available for use, i.e., when it is in the location and condition necessary for it to be capable of operating in the manner intended by the Management. Hence, as the construction of sub-station was completed, the sub-station was ready to</p>	<p>Construction of 1x12.5 MVA, 66/11 KV sub-station at Mandur, was not completed by A Limited and testing of equipment was not done. The work was terminated on 23.01.2017 by CEE, Transmission Zone, Bengaluru.</p> <p>Further, it is to inform that the sub-station work is not totally completed and in order to take the load, station work must be completed in all respects including testing of equipment. Moreover, <i>source line</i> work is also pending. Station cannot be commissioned unless source line work is completed.</p> <p><i>Intention of the Management is to utilise the constructed asset in transmission of power and to generate revenue.</i></p> <p><i>As such, it cannot be considered as asset is capable of operating in the manner intended by the</i></p>

<p>take the load, i.e., ready to use. Accordingly, the depreciation needs to be charged from the date of completion/ready to use. <i>Although the sub-station was ready to use, the same was not charged/used for want of source line and the asset was not categorised as fixed asset till date.</i></p> <p>This has resulted in overstatement of capital work-in-progress and understatement of fixed assets by Rs. 8.20 crore; and understatement of Depreciation (from the date of completion of work/ready to use) and overstatement of profit by the same amount.</p> <p>The amount of depreciation to be charged from the date of completion/ready to use may be worked out and intimated to audit.</p>	<p><i>Management.</i></p> <p>Hence, the categorisation was not done for the above reason and it is requested to drop the Audit para.</p>
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(Emphasis supplied by the querist.)

Additional view of the Company: Due to Right of way (ROW) issues, source line to energise the station is not completed. Only on supply of power to the station, the Company's engineers start testing equipment and make the station to cater power.

AE No.	Enquiries	Replies
3	<p>MWD North <u>Balance Sheet</u></p> <p>Non-current Assets</p> <p>Note - 3 – Capital Work-in-progress - Rs. 3519.23</p> <p>(a) This includes Rs. 45,01,15,659 being the expenditure incurred towards Renovation and Modernization (R&M) of 220/66/11 KV receiving station at SRS Peenya which also includes cost of erection of 150 MVA 220/66/11KV Power Transformer, which is not in order.</p> <p>This work was entrusted to M/s M Electricals, Bangalore on 21.1.2014 at a cost of Rs. 40.98 crores. A review of progress of the above work revealed the</p>	<p>The Detailed Project Report (DPR) for the work of Renovation and Modernisation (R&M) works at 220/66/11kV SRS Peenya is approved vide Corporate OM No B19/1738/90.91 dated 17.02.2011. The said work is awarded to M/s M Electricals vide DWA No. CEE/T&P/SS-620/2403, 2404 & 2405 dated: 02.01.14. The target for completion of the work was 11.02.2015 revised upto 31.10.15 as per OM No: CEE/TZB/SEE (O)/AE-3/F-1629/14-15/8848-51 dated: 31.10.14. The Scope of the work of Renovation and Modernization includes the following:</p> <ol style="list-style-type: none"> 1. Conversion of existing 220kV and 66kV strung bus to rigid bus

following:			<p>formation.</p> <ol style="list-style-type: none"> 2. Upgradation of protection system of 220kV and 66kV side. 3. Installation and commissioning of additional new 220/66/11kV 100MVA Power Transformer. 4. Construction of 2 new 220kV line Bays and 7 new 66kV line bays for re-routing/re-alignment of 220kV Subramanyapura line and existing 66kV lines. 5. Dismantling of existing concrete structures at 220kV and 66kV side. <p>The main objectives of the work (as per Approved DPR) are as below:</p> <ol style="list-style-type: none"> 1. To improve the reliability of Power supply to the surrounding areas. 2. To meet the future load growth. 3. For replacing the existing strung bus by rigid bus to minimize interruptions. 4. To strengthen the sub-station to meet the present load demand. 5. To provide numerical protection relays and bay control unit conforming to IEC 61850 communication protocol with sub-station automation system. 6. To provide bus bar protection system on the 220kV system. <p>The existing 220/66/11kV R/s at SRS Peenya is more than 50 years old and some of the equipments have served their useful life and the spares for the same are not available. The existing RCC structure of Main bus, Isolators, PI and other equipments at 220kV and 66kV are deteriorated. To meet the present load conditions, fault conditions, adopting latest fast acting protection equipments and to facilitate SAS operations, the R&M works are to be carried out in different stages by availing minimum line clear/ with minimum shutdown in live sub-station. The existing</p>
Sl. No	Nature of Work	Date of Commissioning	
1	Erection of Power Transformer	12.01.2019	
2	220 KV South Bus (Charging)	11.10.2015	
3	220 KV North Bus (Charging)	11.01.2016	
4	Subramanyapura Bay (Charging)	16.02.2019	
5	Hoody Hebbal Line (Charging)	11.03.2019	
6	Nelamangala 2 (Charging)	14.06.2019	
7	Nelamangala 4,5 Bay (Charging)	31.08.2019	
8	66 KV Brindavan UG Cable (Charging)	18.03.2019	
9	66 KV Nelagadirenahalli HTLS Line (Charging)	19.03.2019	
<p>As per paragraph 43 of Ind AS 16, each part of an item of property, plant and equipment with a cost that is significant in relation to the total cost of the item shall be depreciated separately. As the above works of erection of Power Transformer and the works on 220 KV side line have been completed and charged before March 2020, the same should have been capitalized in line with Ind AS 16. Further, it was observed that, balance work to be taken up pertains to replacement of 220 kv transformer side Bay equipment and R&M works on 66 kv side.</p> <p>Non-categorisation of the above assets has resulted in overstatement of capital work-in-progress and understatement of Property, Plant and Equipment; and understatement of depreciation and</p>			

<p>overstatement of profit by the same amount. The component cost of the above completed works and depreciation to be charged may be worked out and intimated to audit.</p> <p>(b) Further, although works on 220 KV side and most of 66 KV side and additional 100 MVA were completed, the division capitalized IDC (Interest During Construction) of Rs. 2,32,62,507 on opening balance, which should have been charged to revenue account. This has resulted in overstatement of capital work-in-progress and overstatement of profit by Rs. 2.33 crore.</p>	<p>North, South & Auxiliary strung buses on 220kV side have been converted to Rigid bus and also North & South strung buses of 66kV side are to be converted to rigid bus using aluminum tube and also the work of 66kV line side protection scheme is to be taken up. This work can only be executed by doing temporary arrangements in the sub-station and availing line clear as and when required when it needs to.</p> <p>As on date, the 220kV and 66kV Side of the transformer bay equipments, such as, current transformer, Lightning arrester, Protection system cabling and wiring, C&R Panel and integration to SAS System work is to be taken up which can be completed only after availing line clear. Further, out of 13 66kV line bay portion, only 2 Nos. bays are completed and re-routing of the lines to the new bays which is to be taken up. Only after completion of the re-routing of line work, load can be catered on the new bays. Also 11 Nos. of 66kV bay work is to be taken up for which re-routing is also to be taken up, which requires line clear and amounts to major portion of R&M Works. Earth mat work and cable duct work is also to be taken up for 66kV side.</p> <p>To take up the replacement of bus work on 66kV side from strung bus to rigid bus, line clear was requested several times from August 2019 to till date, but the same is not issued to take up the work. The main work which involved in the said project, such as R&M work of 220kV line bays, 220kV side was completed during the year 2019, however still 220/66/11kV Transformer bays at 220kV side and 66kV side, 66kV side bus work is to be taken up simultaneously only after approval of</p>
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		<p>line clear.</p> <p>The station is being utilized by making use of already existing equipment. After completion and commissioning of both 220kV and 66kV side works, the station can be fully utilized and the benefits as mentioned in the DPR can be achieved.</p> <p>However, for achieving the benefits which are mentioned in the DPR, the following balance works are required to be carried out by availing line clears and with the proper planning, since the existing live station is having installed capacity of 3x150MVA +1x100MVA and 1x 67.5MVA totaling to 617.5MVA are feeding to the prime areas of Bengaluru Metropolitan area zone in Bengaluru:</p> <ol style="list-style-type: none"> 1. 66kV side strung bus system to be converted to rigid bus system. 2. 4 Nos of 220/66/11kV Transformer bay equipments to be replaced and commissioned. 3. Out of 13 Nos of 66kV Outgoing line bays, 2 Nos of line bays (Brindavan and Nelagadirenahalli) renovation and modernisation work has been completed and remaining 11 Nos of line bays R&M work to be taken up. 4. Establishment of SAS for the total sub-station and to be integrated with SCADA SLDC for monitoring of real time data. 5. Site surfacing of the entire yard to be taken up. <p>Due to non-availability of line clear and due to outbreak of COVID-19 during March 2020, entire 220kV side work could not be completed. In order to achieve the objectives mentioned in the DPR, the total work which includes both 220kV and</p>
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		<p>66kV side has to be completed as per DWA (Detailed Work Award) scope of the work.</p> <p>The intention of the management is to utilise the constructed asset in transmission of power. As such, it cannot be considered as the said asset is capable of operating in the manner intended by the management.</p> <p>Hence, the categorisation is not done for the above reasons. Further, as the work is under progress, the capitalisation of IDC is in order.</p> <p>Hence, it is requested to drop the audit para.</p>
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Additional view of the Company: In renovation & modernisation (R&M) work, existing station equipment will be replaced by higher capacity latest and updated equipment. Though the R&M work is under progress, station is being utilised to cater power. In the above station, new equipments are being installed adjacent to existing equipment. Once the incoming source line work and outgoing line works are completed, new equipment will be energised; till such time, the station is made to cater power using existing equipment. Due to non-availability of line clearance, the completion of the above work is getting delayed inordinately. Majority of the equipments are installed and connected to incoming source line, but the work in respect of outgoing line is not completed due to non-availability of line clearance.

11. The querist has informed that the contention of C&AG Auditors on the above three issues are:

AE No.1- Approval of the CEIG shall be considered for capitalising as PPE, as the asset is in the location and condition necessary for it to be capable of operating in the manner intended by the Management; and asset needs to be categorised and depreciation charged from the date of approval of CEIG.

AE No.2- As station work was completed long back, the sub-station was ready to take the load, i.e., ready to use. Accordingly, the depreciation needs to be charged from the date of completion/ready to use irrespective of the fact of no-source power line.

AE No.3- As per paragraph 43 of Ind AS 16, each part of an item of property, plant and equipment with a cost that is significant in relation to the total cost of the item shall be categorised and depreciated separately.

12. The contention of the Company on the above three issues are:

AE No.1- After CEIG approval, newly constructed station needs to be energised by taking line clearance and several test needs to be conducted to ensure proper working of the equipment and to ensure taking up the load by station to transmit the power. On completion of the said procedure, intention of the management to utilise the constructed asset in transmission of power and to generate revenue is achieved and asset commissioned certificate

will be issued accordingly by the Company's engineers. Based on the asset commissioned certificate, asset will be categorised.

AE No.2- The conclusion regarding completion of station work can be drawn only when CEIG approval is obtained, station energised, equipment tested by the Company's engineers and found that it is ready to transmit power. In this case, station is not energised as power source line is not completed and consequently, testing too is not done. As and when these procedures are completed, intention of the Management to utilise the constructed asset in transmission of power and to generate revenue is achieved and asset commissioned certificate will be issued accordingly by the Company's engineers. Based on the asset commissioned certificate, asset will be categorised.

AE No.3- Though a few equipments are installed and connected to incoming line, transmission of power cannot be carried out, as outgoing line work is under slow progress due to non-availability of line clearance. Intention of the management to utilise the constructed asset in transmission of power and to generate revenue is not achieved. Hence, such works cannot be categorised as assets.

The above issues have given space for more speculations as to the point that has to be considered while categorising/capitalising of an asset.

13. The Company acknowledges the fact that the CEIG approval is a mandatory statutory requirement to be taken by the Company before the constructed power infrastructure is connected to the grid. However at times, the CEIG has issued post-facto approval i.e., the Company has obtained the CEIG approval post connection of its power network to the grid. Hence, the Company is of the view that the CEIG approval is an administrative procedure to be adopted before formal operation is conducted. The Company also acknowledges that the sole motive of creation of new power infrastructure is to cater to the increasing power demand posed by the ESCOMs.

14. As there was a difference between the views of C&AG and the Company, the Company has given assurance to the C&AG to seek an opinion from the Expert Advisory Committee.

B. Query

15. In view of the above, the querist has sought the opinion of the Expert Advisory Committee (EAC) on the following issues:

- (i) Whether the date of capitalisation (from CWIP to PPE) of an asset is the date of approval from CEIG or the date of asset commissioned certificate.
- (ii) Can the Company capitalise an asset pending availability of source line though all the equipments (Plant and Machinery) in the station are installed/erected but not tested?
- (iii) Can the Company capitalise an asset pending output of power/energy from the station though all the equipments (Plant and Machinery) in the station are installed/erected, tested and CEIG approval is received?
- (iv) Whether the date of successful test run to be adopted as the date of capitalisation of an asset.
- (v) Whether on erection and connecting the equipment to the incoming source line, such equipment is to be categorised though transmission of power cannot be carried out.

- (vi) Whether the assets need to be capitalised when all the works mentioned in the DWA is completed by the Contractor (pending obtaining of CEIG approval and source line).
- (vii) Whether in case of modernisation work, the assets need to be capitalised on erecting of part of the assets mentioned in the DWA though the end use of transmission of power not achieved.

C. Points considered by the Committee

16. The Committee notes that the basic issue raised in the query relates to timing of capitalisation of transmission lines and sub-stations as an item of Property, Plant and Equipment from capital-work-in-progress in case of construction as well as in case of modernisation. The Committee has, therefore, considered only this issue and has not considered any other issue that may arise from the Facts of the Case, such as, accounting for assets acquired by way of gift/consumer's contribution, method and measurement of depreciation on fixed assets located at different locations, accounting for interest during construction, accounting for costs incurred during suspension of activities due to COVID, presentation and disclosure requirements as per Schedule III to the Companies Act, 2013, application of Ind AS 116, 'Leases', in the context of arrangements with ESCOMs, etc. Further, the Committee has opined purely from accounting perspective and not from any legal perspective, such as from the perspective of tariff regulations issued by the Central or State Electricity Regulatory Commission or technical aspects thereof. Further, the accounting Standards referred hereinafter are Indian Accounting Standards, notified under the Companies (Indian Accounting Standards) Rules, 2015, as amended/revised from time to time.

17. At the outset, the Committee notes the following paragraphs of Ind AS 16, 'Property, Plant and Equipment':

“Property, plant and equipment are tangible items that:

- (a) are held for use in the production or supply of goods or services, for rental to others, or for administrative purposes; and**
- (b) are expected to be used during more than one period.”**

“7 The cost of an item of property, plant and equipment shall be recognised as an asset if, and only if:

- (a) it is probable that future economic benefits associated with the item will flow to the entity; and**
- (b) the cost of the item can be measured reliably.”**

“10 An entity evaluates under this recognition principle all its property, plant and equipment costs at the time they are incurred. These costs include costs incurred initially to acquire or construct an item of property, plant and equipment and costs incurred subsequently to add to, replace part of, or service it. ...”

Subsequent costs

“12 Under the recognition principle in paragraph 7, an entity does not recognise in the carrying amount of an item of property, plant and equipment the costs of the day-to-day servicing of the item. Rather, these costs are recognised in profit or loss as incurred. Costs of day-to-day servicing are primarily the costs of labour and

consumables, and may include the cost of small parts. The purpose of these expenditures is often described as for the ‘repairs and maintenance’ of the item of property, plant and equipment.”

“15 An item of property, plant and equipment that qualifies for recognition as an asset shall be measured at its cost.

16 The cost of an item of property, plant and equipment comprises:

- (a) its purchase price, including import duties and non-refundable purchase taxes, after deducting trade discounts and rebates.
- (b) any costs directly attributable to bringing the asset to the location and condition necessary for it to be capable of operating in the manner intended by management.
- (c) the initial estimate of the costs of dismantling and removing the item and restoring the site on which it is located, the obligation for which an entity incurs either when the item is acquired or as a consequence of having used the item during a particular period for purposes other than to produce inventories during that period.

17 Examples of directly attributable costs are:

...

- (e) ²costs of testing whether the asset is functioning properly, after deducting the net proceeds from selling any items produced while bringing the asset to that location and condition (such as samples produced when testing equipment). Excess of net sale proceeds of items produced over the cost of testing, if any, shall not be recognised in the profit or loss but deducted from the directly attributable costs considered as part of cost of an item of property, plant and equipment; and

...”

“20 *Recognition of costs in the carrying amount of an item of property, plant and equipment ceases when the item is in the location and condition necessary for it to be capable of operating in the manner intended by management.* Therefore, costs incurred in using or redeploying an item are not included in the carrying amount of that item. For example, the following costs are not included in the carrying amount of an item of property, plant and equipment:

- (a) costs incurred while an item capable of operating in the manner intended by management has yet to be brought into use or is operated at less than full capacity;

...”

“22 The cost of a self-constructed asset is determined using the same principles as for an acquired asset. If an entity makes similar assets for sale in the normal course of business, the cost of the asset is usually the same as the cost of constructing an

² Substituted vide Notification No. G.S.R. 255(E) dated 23rd March, 2022.

asset for sale (see Ind AS 2). Therefore, any internal profits are eliminated in arriving at such costs. *Similarly, the cost of abnormal amounts of wasted material, labour, or other resources incurred in self-constructing an asset is not included in the cost of the asset.* Ind AS 23, *Borrowing Costs*, establishes criteria for the recognition of interest as a component of the carrying amount of a self-constructed item of property, plant and equipment.”

(Emphasis supplied by the Committee.)

The Committee notes from the above that an item of PPE shall be measured at cost which comprises its purchase price, *any costs directly attributable to bringing the asset to the location and condition necessary for it to be capable of operating in the manner intended by management* and cost of dismantling/removing and restoring the asset. It may also be noted that cost of testing whether the asset is functioning properly is also an example of directly attributable cost. The Committee notes that the assets covered in the extant case are in the nature of self-constructed assets. Further, in terms of paragraph 22 of Ind AS 16, the cost of a self-constructed asset is determined using the same principles as for an acquired asset. Therefore, in the extant case, the principles for ‘acquired assets’ under Ind AS 16 shall be equally applicable to the self-constructed assets covered under the contract with the turnkey contractors in the extant case.

18. The Committee further notes from paragraph 20 of Ind AS 16 that recognition of costs in the carrying amount of an item of PPE should cease when an item is *in the location and condition necessary for it to be capable of operating* in the manner intended by management, even though there is a possibility of the item operating at less than full capacity. From this, the Committee is of the view that an item of capital work in progress should be transferred to the gross block of PPE when such item is *in the location and condition necessary for it to be capable of operating* in the manner intended by management.

19. The Committee now considers the issue of determining the point in time when an item is in the location and condition necessary for it to be capable of operating in the manner intended by the management. The Committee is of the view that in the case of self-constructed assets, an assessment should be made as to what event or activity characterises the point at which an asset's physical construction or installation is complete and when that asset can be considered to be in the location and condition necessary for it to be capable of operating in the manner intended by the management as per the requirements of Ind AS 16, so that all directly attributable costs incurred up to that point can be included in the cost of the self-constructed PPE and the asset can be transferred from capital work in progress to gross block of PPE.

20. In this context, the Committee notes from the Facts of the Case that various steps/stages are involved in construction and installation of sub-stations and transmission lines. As explained by the querist, after the asset is constructed by the turnkey contractor, pre-commissioning testing is undertaken by the relay testing wing of the Company and availability of source lines is ensured. After this, inspection is conducted by CEIG and after obtaining approval from CEIG, further testing by conducting test runs is done by the Company and identified problems are rectified by the relay testing wing of the Company. After this, line clearance is obtained from ESCOMs and stations lines will be connected to the electricity network and asset commissioned certificate is issued by the Company’s engineers.

21. The Committee is of the view that the date or point when an asset can be considered to be in the location and condition necessary for it to be capable of operating in the manner

intended by the management as per the requirements of Ind AS is a matter of technological assessment and judgement, which the Company should exercise itself in its specific facts and circumstances, considering various factors such as, technological parameters, safety parameters, various pre-requisite and substantive approvals from competent authorities, completion of test runs to ensure that the asset is functioning properly, etc. In this context, the following broad guidance may be used:

(i) The Committee notes from the Facts of the Case that at times, CEIG has issued post-facto approval, i.e., post connection of its power network to the grid. Therefore, the Committee is of the view that in the extant case, CEIG approval may not be the sole determining factor for determination of such date/point as discussed above. The Committee is also of the view that normally, the purpose of trial and test runs is to ensure that the asset is functioning properly, i.e., technical and physical performance (and not financial performance) of the plant/asset, as expected for its intended use, is ensured. During test/trial runs, if there are technical deficiencies/problems, adjustments are made and problems are rectified to ensure that the plant is ready for its intended use, i.e. capable of producing the intended inventories or rendering the intended services. Therefore, before such trial/test run, the plant/asset cannot be considered to be in the location and condition necessary for it to be capable of operating in the manner intended by management as per the requirements of Ind AS 16.

(ii) The Committee is further of the view that while determining such date or point, the manner of operation intended by the management or in other words, intended use of acquisition or construction of an item of PPE should also be taken into consideration. Thus, after acquisition/construction of certain equipments/PPE which are part or components of a larger and integrated PPE/project, if these are not capable of operating due to other parts/components/facilities being under development or construction and cannot be operated independently, those equipments/ PPE cannot be considered to be in the location and condition necessary for them to be capable of operating in the manner intended by the management, as per the requirements of Ind AS 16. Conversely, if a part or component is capable of being used while construction continues on other parts, that part or component should be capitalised as PPE and depreciated accordingly, as per the requirements of Ind AS 16.

However, in this context, the Committee wishes to point out that the once the asset is in the location and condition necessary for it to be capable of operating in the manner intended by the management as per the requirements of Ind AS 16, if the Company is not able to operate the PPE due to non-availability of inputs or raw materials (for example, power supply in the extant case) or not able to operate at a certain level, the timing of capitalisation to PPE (i.e., transfer from CWIP) should not be delayed. In other words, timing of capitalisation to PPE is determined based on when the asset is ready to use and not when the asset is put to use. If the asset is ready to use but not put to use due to non-availability of power supply in the extant case, capitalisation cannot be delayed. Further, if there are any abnormal delays during construction period, leading to incurrence of costs of abnormal amounts of wasted material, labour, or other resources, such costs should not be included in the cost of the asset/PPE.

22. The Committee also notes that Ind AS 16 lays down similar principles for major subsequent expenditure on PPE. Therefore, in the extant case, if major subsequent expenditure, viz., modernisation work meets the recognition criteria as per paragraph 7 of Ind AS 16, similar principles of recognition and measurement will be applicable as applicable in case of a self-constructed asset as discussed in earlier paragraphs. Thus, in the extant case,

when the asset on which modernisation work is carried out or a component/part thereof, can be considered to be in the location and condition necessary for it to be capable of operating in the manner intended by the management as per the requirements of Ind AS 16, the same can be capitalised.

23. The Committee also wishes to mention that the Company should also consider the impairment of assets, if any, considering the requirements of Ind AS 36 for assets which are taking longer time to complete due to non-availability of source line, etc.

24. Further with regard to the issue raised in the facts relating to commencement of depreciation, the Committee notes paragraph 55 of Ind AS 16 as follows:

“55 Depreciation of an asset begins when it is available for use, ie when it is in the location and condition necessary for it to be capable of operating in the manner intended by management. Depreciation of an asset ceases at the earlier of the date that the asset is classified as held for sale (or included in a disposal group that is classified as held for sale) in accordance with Ind AS 105 and the date that the asset is derecognised. Therefore, depreciation does not cease when the asset becomes idle or is retired from active use unless the asset is fully depreciated. However, under usage methods of depreciation the depreciation charge can be zero while there is no production.”

From the above, the Committee notes that depreciation of an asset should commence from the date the asset is available for use, i.e., when the asset is in the location and condition necessary for it to be capable of operating in the manner intended by the management. Accordingly, in the extant case, the depreciation should commence when the various assets are transferred from capital work in progress to gross block of PPE, as discussed above.

D. Opinion

25. On the basis of above, the Committee is of the following opinion on the issues raised in paragraph 15 above:

The date or point when an asset can be considered to be in the location and condition necessary for it to be capable of operating in the manner intended by the management as per the requirements of Ind AS 16 and when an item of capital work in progress can be transferred to gross block of PPE is a matter of technological assessment and judgement, which the Company should exercise itself in its specific facts and circumstances, considering various factors such as, technological assessments, safety parameters, various pre-requisite and substantive approvals from competent authorities, etc., as discussed in paragraphs 17 to 22 above. Additionally, the Company should also comply with the guidance discussed in paragraphs 23 and 24 regarding impairment and commencement of depreciation based on the specific facts and circumstances.

Subject to the above overall guidance,

- (i) and (vi) The CEIG approval date or the date of asset commissioned certificate may not be the sole determinant(s) for capitalisation of the asset. Further, regarding implication on capitalisation pending source line see (iii) and (v) below.
- (ii) and (iv) Normally, the purpose of trial and test runs is to ensure that an asset is functioning properly, i.e., technical and physical performance (and not financial performance) of the plant/asset, as expected for its intended use, is

ensured. During test/trial runs, if there are technical deficiencies/problems, adjustments are made and problems are rectified to ensure that the plant is ready for its intended use, i.e. capable of producing the intended inventories or rendering services. Therefore, before such trial/test run, the plant/asset cannot be considered to be in the location and condition necessary for it to be capable of operating in the manner intended by management as per the requirements of Ind AS 16.

- (iii) and (v) Once the asset is in the location and condition necessary for it to be capable of operating in the manner intended by the management as per the requirements of Ind AS 16, just because the Company is not able to operate the PPE due to non-availability of inputs or raw materials (for example, power supply in the extant case) or not able to operate at a certain level, the timing of capitalisation to PPE (i.e., transfer from CWIP) should not be delayed. In other words, timing of capitalisation to PPE is determined based on when the asset is ready to use and not when the asset is put to use. If the asset is ready to use but not put to use due to non-availability of power supply in the extant case, capitalisation cannot be delayed.

- (vii) In case of modernisation work, when the asset on which modernisation work is carried out or a component/part thereof, can be considered to be in the location and condition necessary for it to be capable of operating in the manner intended by the management as per the requirements of Ind AS 16, the same should be capitalised, as discussed in paragraph 22 above.
