

Query No. 43

Subject: Recognition of windmill plant as a property, plant and equipment or as Right of Use Assets.¹

A. Facts of the Case

1. A company (hereinafter referred to as ‘the Company’) is a Central Public Sector Entity (CPSE) registered under the Companies Act, 2013, established with an equity participation of 51% and 49% from another CPSE and Indian Railways (Government of India) respectively. The Company is engaged in the consultancy business of energy management, including renewable energy. The Company is facilitating Indian Railways in procurement of power in open access and in achieving the net zero carbon.

2. The Company is also having a wind power plant of 26 MW (13 Wind Terminal Generator (WTG) of 2 MW each); entire energy of plant is being transmitted at stipulated Traction Sub Station of Indian Railways in terms of Power Purchase Agreement (PPA) for 25 years with Nodal Railways (a copy each of the PPAs has been supplied by the querist for the perusal of the Committee). It may be noted that 26 MW wind plant is the part of a wind farm of 572 MW developed by a developer. Rest of the capacity, i.e., 572 MW less 26 MW, is owned by other CPSEs and private parties.

3. The land for wind farm was allotted to the developer as per the State land lease policy, which was further sub-leased by the developer to the respective CPSEs in the ratio of area covered by wind plant owned by respective CPSE. As such, developer subleased the area related to 26 MW wind plant to the Company.

4. The Company initially recognised the entire cost including one time land lease charges as property, plant, and equipment (PPE) and as per technical assessment of useful lives of the assets as 25 years, provided for depreciation as per straight line method. However, after the introduction of Ind AS 116, ‘Leases’, the Company segregated the cost of leased land and has shown it as a Right of Use (RoU) asset. Thus, as on 31.03.2023, wind power plant is presented as PPE (₹ 10,680.67 Lakh (WDV)) and land on lease for wind plant is presented as ‘RoU’ (₹ 73.85 Lakh (WDV)).

5. The significant accounting policy of the Company on revenue recognition on windmill plant and estimated useful lives of the PPE is reproduced below:

“Revenue from sale of power through wind-mill projects is recognized on the basis of certificate from concerned State Electricity Authority for energy fed in kwh (units) in authority’s system and as per terms and conditions of the contract with the beneficiary.

As per the Company’s technical assessment, Windmill Plants have a higher useful life of 25 years than prescribed in part C of schedule II of the Companies Act, 2013 of 22 years. Therefore, depreciation is charged at a lower rate than prescribed under the Companies Act, 2013.”

6. During supplementary audit of financial statements of the Company under section 143(6) of the Companies Act, 2013, office of Comptroller and Auditor General of India (C&AG) through Director General of Railway Commercial raised an observation on treatment

¹ Opinion finalised by the Committee on 27.12.2023.

of windmill plant owned by the Company. The observation and the management reply are reproduced below:

Observations raised by office of the C&AG	Management response to the observation is also reproduced herein:
<p><u>Property, Plant and Equipment Rs. 15,985.75 lakh</u> <u>Finance Lease</u></p> <p>The Company entered into the Power Purchase Agreement (PPA) for 26 MW wind power project in the State with Northwestern Railway (NWR) on 17.04.2023 for a period of 25 years from the date of commencement of supply of power or till the life of the wind farm.</p> <p>Clause 2.2 of the PPA states that, “the Company shall ensure supply of entire wind energy generated from the 26 MW Wind Farm to NWR for their captive.”</p> <p>Paragraph 63 of Ind AS 116 on ‘Leases’ states that, “Whether lease is finance lease or an operating lease depends on the substance of the transaction rather than the form of the contract. Examples of situations that individually or in combination would normally lead to a lease being classified as a finance lease are:</p> <p>(a) the lease transfers ownership of the underlying asset to the lessee by the end of the lease term;</p> <p>(b) the lessee has the option to purchase the underlying asset at a price that is expected to be sufficiently lower than the <i>fair value</i> at the date the option becomes exercisable for it to be reasonably certain, at the <i>inception date</i>, that the option will be exercised;</p> <p>(c) the lease term is for the major part of the <i>economic life</i> of the underlying asset even if title is not transferred;</p> <p>(d) at the inception date, the present value of the lease payments amounts to at least substantially all of the fair value of the underlying asset; and</p> <p>(e) the underlying asset is of such a specialised nature that only the lessee can use it without major modifications.”</p> <p>Therefore, this kind of arrangement is treated as finance lease as per the Ind AS 116. The scope paragraphs of Ind AS 32, Ind</p>	<p>Paragraph 63 of Ind AS 116, which has been referred to by audit deals with classification of lease as a finance lease or operating lease for a contract/arrangement that contains lease.</p> <p>For identifying whether a contract contains lease or not, relevant provisions of Ind AS 116 are reproduced as under:</p> <p><u>“Identifying a lease (paragraphs B9-B33)</u></p> <p>9. At inception of a contract, an entity shall assess whether the contract is, or contains, a lease. A contract is, or contains, a lease if the contract conveys the right to control the use of an identified asset for a period of time in exchange for consideration. Paragraphs B9-B31 set out guidance on the assessment of whether a contract is, or contains, a lease.”</p> <p>“B9 To assess whether a contract conveys the right to control the use of an identified asset (see paragraphs B13-B20) for a period of time, an entity shall assess whether, throughout the <i>period of use</i>, the customer has both of the following:</p> <p>(a) the right to obtain substantially all of the economic benefits from use of the identified asset (as described in paragraphs B21-B23); and</p> <p>(b) the right to direct the use of the identified asset (as described in paragraphs B24-B30).”</p> <p>An asset to be qualified as a lease must have fulfilled the criteria ‘a & b’ mentioned in Paragraph B9. i.e., customer has the right to obtain substantially all of the economic benefits from the identified assets,</p> <p style="text-align: center;"><i>and</i></p> <p>The customer also has the right to direct the use of such assets.</p>

<p>AS 109 and Ind AS 107 acknowledge that rights and obligations under leases, to which Ind AS 116 applies, are financial instruments but their measurement is excluded from the scope of these standards. Accordingly, the non-current portion of a finance lease receivable shall be presented under ‘Other non-current financial assets’ while its current portion shall be presented under ‘Other current financial assets’.</p> <p>Management has shown Rs. 10,680.67 lakh (net block) being the windmill plant (26MW) in PPE instead of finance lease.</p> <p>Therefore, this has resulted in overstatement of property, plant and equipment by Rs. 10,680.67 lakh and understatement of finance lease to the same extent.</p>	<p>The Company has PPA with Railways for supply of power generated from windmill plant but <i>customer i.e., Railways has no right at all (emphasis provided)</i> to direct the use of windmill plant owned by the Company.</p> <p>In view of above, it can be seen that windmill plant, though an identified asset and supplies entire power to Railways, does not meet the second limb of <i>Paragraph B9 of Appendix B i.e., “the right to direct the use of the identified asset”</i>, and as such, cannot be treated as leasing arrangement within the ambit of Ind AS 116.</p> <p>Since windmill plant does not qualify to be a lease as explained above, paragraph 63 of Ind AS 116 has no relevance as the same deals with the classification of lease as a finance lease or operating lease.</p>
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7. After submission of the above replies by the management, the office of C&AG has further raised a query. The query raised as well as management reply are reproduced here as under:

Comments on Financial Position by the office of the C&AG	In continuation of Management reply submitted earlier mentioned in the above table
<p>Property, Plant and Equipment Rs. 15,985.75 lakhs</p> <p>The Company set up a 26 MW wind energy power plant in the State for the exclusive supply of power to Indian Railways. In this regard, a Power Purchase Agreement (PPA) was also entered into by the Company with Western Central Railway (WCR) on 29.10.2014 for a period of 25 years from the date of commencement of supply of power or till the life of the wind farm whichever is later.</p>	<p>As per Ind AS 116, for a contract to be considered a lease, the contract should convey “right to control the use of identified assets”. “Right to control” exists if said contract conveys two rights simultaneously i.e., “Right to obtain substantially all economic benefits from use of identified assets” and “Right to direct the use of identified assets”. Paragraph 9 read with paragraphs B9 and B24 to B30 of Ind AS 116 are relevant.</p> <p>To understand the “Right to direct the use” and existence of the same within the ambit of extant PPA, provisions of paragraph B24 of Ind AS 116, which clarify the “Right to direct the use” and relevant clauses of PPA between the Company and Nodal Railway have been <i>deliberated</i> here under.</p> <p>Paragraph B24 and relevant Clauses of PPA specifying obligations and undertaking of the Company and NWR are reproduced below:</p> <p>“B24 A customer has the right to direct the use of an identified asset throughout the period of use only if either:</p> <p style="margin-left: 40px;">(a) the customer has the right to direct how and for what purpose the asset is used throughout the period of use</p>

The Company has disclosed this windmill plant as property, plant and equipment instead of finance lease in violation of paragraph 9 of Ind AS 116, 'Leases'. This has resulted in overstatement of property, plant and equipment and understatement of the finance lease by Rs. 10,680.67 lakh.

The Company in its reply has stated that the Company has PPA with Railways for the supply of power generated from the windmill plant but customer i.e., Railways has no right at all to direct the use of the windmill plant owned by the Company.

In this regard, the Company may refer to the suitable clause of the PPA under which the right to direct the use of the windmill plant is with parties other than the Indian Railways.

(as described in paragraphs B25–B30); or

- (b) the relevant decisions about how and for what purpose the asset is used are predetermined and:
 - (i) the customer has the right to operate the asset (or to direct others to operate the asset in a manner that it determines) throughout the period of use, without the supplier having the right to change those operating instructions; or
 - (ii) the customer designed the asset (or specific aspects of the asset) in a way that predetermines how and for what purpose the asset will be used throughout the period of use.”

Clause 2 of PPA:

OBLIGATIONS & UNDERTAKINGS of THE COMPANY

2.1 The Company shall ensure date of commencement of the wheeling after successful commissioning of the Wind Farm by the developer and commencement of the commercial operation date and it is necessary that during the duration of the contract period, the Company shall continue wheeling and supply from 26 MW Power through XYZ/ State DISCOM till the validity of this Agreement, subject to Force Majeure conditions.

2.2 The Company shall ensure supply of entire wind energy generated from the 26 MW Wind Farm to Nodal Railway for their captive. Power will be injected from 26 MW Windmill Plant in the State and the Utility will use the entire power for traction use at its Traction Substation points (TSSs) 132 KV and above voltage level emanating from the respective RVPN substations.

Wind power will be used at all Railways existing TSSs and at the TSSs to be commissioned in future in the State.

2.3 The Company shall ensure that all the requisite permissions/statutory clearances, as per relevant provisions, required for setting up the 26 MW wind farm will be obtained from the State Renewable Energy Corporation Limited (SRECL).

2.4 The Company shall coordinate with the DISCOM(s) directly or through the Developer for wheeling the energy delivered by developer to DISCOM(s) at delivery point(s) for consumption by Nodal Railway and also ensures the adjustment of the wheeled energy in the electricity bills of the DISCOM at Rly's load centre.

Clause 3 of PPA:

OBLIGATIONS & UNDERTAKINGS of NODAL RAILWAY

Nodal Railway shall ensure consumption of entire wind energy from 26 MW Wind Farm for their captive use. The Power will be injected from 26 MW Windmill Plant in the State and Utility will

use the entire power on must run basis for traction use at its Traction Substation points (TSSs) of 132 KV and above voltage level emanating from the respective substations (as per Schedule-1) during the tenure of the Agreement:

...

Any change in the Load Centre will be subject to approval from the one of the state PSU, XYZ/the Company and financial implications (if any), to be borne by **NWR**.

3.2 Nodal Railway shall pay the monthly bills raised by the Company.

3.3 *Text Deleted.*

3.4 Nodal Railway shall specify to the Company drawl schedule at their specified locations as per Schedule-1 of this PPA.

3.5 Wherever Nodal Railway wishes to draw energy at different locations based on its requirement, NWR shall allow inspection of its locations by DISCOM(s) as per the provisions of the Wheeling Agreement as concluded by the Company with XYZ/ DISCOM(s)

Deliberation of paragraph B24(a) of Ind AS 116:

26 MW wind energy plant is owned by the Company. The plant was commissioned in 2015 and is being operated by the Company through an OEM (Original Equipment Manufacturer) in compliance with the extant industry and regulatory norms, grid code. Electricity generated is wheeled and supplied to NWR through XYZ/State DISCOM (Clause 2.1 of PPA) for use of power by NWR for traction purpose in the State (Clause 2.2 of PPA) with an obligation on NWR to use the same for traction purpose only at specified load centre on a must run basis without any right to change the load centre (clause 3 of PPA).

Paragraphs B25 and B26 of Ind AS 116, which provide further explanation on paragraph B24, categorically state that “right to direct how and for what purpose the asset is used *must have been defined in the contract itself*. It may be seen from the PPA attached herewith and the clauses reproduced above that PPA is defining only the right to obtain the energy with an obligation to use it for the specified purpose and *no other right has been defined in the PPA*.

In view of the above, it is clear that *PPA does not give any right, explicit or implicit*, to direct the use of wind plant to Nodal Railway. On the contrary, it can be concluded that “*right to direct how and for what purpose the wind plant is used throughout the period of use of plant*” is not relevant in view of the nature of asset i.e., wind plant can only be used in a manner as decided by the operator i.e., the Company through operator and purpose is already defined in the PPA i.e. to supply the

generated energy to Nodal Railway.

As such, the extant PPA does not meet the condition specified in paragraph B24 (a) of Ind AS 116, rather it can be concluded that “how and for what purpose a power plant is used” is predetermined in case of a power plant.

Deliberation of paragraph B24(b)(i) of Ind AS 116:

The wind plant is installed by the Company and is being operated through O&M contractor appointed by the Company, who is OEM of wind plant. Further as per clause 2 of PPA, all the obligations related to operation of plant, wheeling and supplying of electricity, coordination with DISCOM(s) is on the Company. Paragraph B27, which provides further explanation on paragraph B24(b)(i), inter alia states that when “how and for what purpose asset is used” is pre-determined, decision making rights related to operating and maintenance of the assets are relevant. In this connection, following excerpts from commentary on Ind AS 116 of an eminent professional is worth mentioning:

“... Operating decision: These are ignored, unless the “how and for what purpose” decisions are predetermined, in which case if the customer makes the operating decision there is a lease”.

Thus, when “how and for what purpose” is pre-determined and operating decision is taken by supplier, it is not a lease.

Since decision rights regarding operation and maintenance are with the Company and not with Nodal Railway, as explained above, and “how and for what purpose wind plant is used” is pre-determined, condition of paragraph B24 b(i) of Ind AS 116 is not satisfied.

Deliberation of paragraph no. B24(b)(ii) of Ind AS 116:

The windmill plant was constructed by M/s I Ltd., an OEM, who was engaged by the Company with scope of work “Setting up of Windmill Farm of 25 MW (± 1 MW) in the J district of the State (India) on Lump Sum Turnkey (LSTK) basis with comprehensive operation and maintenance services”. It is further submitted that M/s I Ltd. has developed the total wind farm of 572 MW, consisting of 286 WTG in which 13 WTG (2 MW each) is owned by the Company. Balance WTG / MW is owned by other public / private players. It is submitted that the wind farm has been designed / constructed by I Ltd. for supply of energy to different types of customers including public and private. As such, *there is no role of the Nodal Railway in designing the 26 MW wind energy plant.* Accordingly, the condition specified in paragraph B24(b)(ii) is also not satisfied.

In view of the above deliberation, it can be seen that PPA does not have any clause that satisfy the condition specified in paragraph B24 of Ind AS 116. Accordingly, the Nodal Railway does not have any right to direct the use of the wind energy plant.

	<p>Further, following clauses of PPA may also be seen which implicitly indicate that wind power plant is PPE of the Company since entire responsibility relating to payment of various charges is on the Company:</p> <p><u>Clause-3.0 of the Annexure-iv of the PPA</u></p> <p>The Company shall ensure that developer or itself shall duly and punctually pay all taxes on power generation, (if applicable), license fees, registration charges, renewal fees, plant outage charges if any, etc. payable to DISCOM and any other statutory bodies and NWR will have no liability, <i>except for Tariff purposes.</i></p> <p><u>Clause-6.0 of the Annexure-iv of the PPA</u></p> <p>It is expressly agreed that the Company shall ensure that any liability with regard to any claim, loss or damage in respect of installation, <i>use, generation or operation of the power plant shall rest with the Producer and Developer.</i> The NWR shall have no liability therefor.</p> <p>From the above detailed deliberation, it can be seen that extant PPA does not contain lease; as such, 26 MW windmill power plant has correctly been classified as PPE of the Company.</p>
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(Emphasis supplied by the querist.)

8. Observation was not pressed further in view of the management's assurance to refer the observation of audit for opinion of Expert Advisory Committee of the Institute of Chartered Accountants of India (ICAI).

9. As can be seen from the conjoint reading of first and second observation of audit, reproduced above, audit is insisting on "Right to Direct the use of the windmill plant" and is asking for a clause which gives the said rights to parties other than Indian Railways. Management is of the view that PPA does not provide *implicitly or explicitly* any right to direct the use of windmill plant to Indian Railways, although drawl of output is pre-determined i.e., as per PPA. As such, management is of the considered view that the fact of consumption of entire output generated from the windmill plant by Indian Railway does not conclusively indicate the availability of 'Right to Direct the use' with Indian Railways. Paragraph B29 of Appendix B of Ind AS 116 clearly clarifies that ability to specify the output in a contract before the period of use, *without any other decision-making rights relating to the use of the asset*, gives a customer the same rights as any customer that purchases goods or services. (Emphasis supplied by the querist.)

B. Query

10. In view of the above, the opinion of Expert Advisory Committee has been sought as to whether recognition of windmill plant as property, plant and equipment (PPE) as per Ind AS 16 is appropriate or the same should be considered as a finance lease of the asset. If not, how to recognise the above assets?

C. Points considered by the Committee

11. The Committee notes that the basic issue raised in the query relates to appropriateness of recognition of windmill plant as a property, plant and equipment or whether the same should have been considered as a finance lease. 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, revenue recognition from sale of power through windmill, accounting for transition to Ind AS 116, 'Leases', depreciation of PPE/RoU asset including determination of useful life of windmill plants and rate of depreciation used, accounting for land for windmill plant, accounting in the books of developer, measurement of PPE/RoU asset, accounting for contract between the developer/OEM/O&M contractor and the Company, applicability of Ind AS 114, 'Regulatory Deferral Accounts', etc. Further, the Committee has examined the issue purely from accounting perspective and not from the legal perspective, such as, legal interpretation of various agreements, such as land lease agreement, PPA, etc. Furthermore, it is presumed from the Facts of the Case that the Company in the extant case is acting in the capacity of a principal and not as an agent of Indian Railways or wind farm developer. The Committee also wishes to state that the Company should first examine whether the arrangement between the Company and Railways in the extant case is within the scope of Appendix D, 'Service Concession Arrangements' to Ind AS 115, 'Revenue from Contracts with Customers'. If the arrangement is within the scope of Appendix D, then the same should be followed. However, since the issue has not been raised from that perspective, the Committee has not examined the same. Rather, this opinion is based on the presumption that Appendix D to Ind AS 115 is not applicable. The Accounting Standards referred to in the opinion are Indian Accounting Standards (Ind AS) notified under the Companies (Indian Accounting Standards) Rules, 2015, as revised or amended from time to time.

12. The Committee notes that the Company owns a wind power plant of 26 MW (13 Wind Terminal Generator of 2 MW each) and entire energy of plant is being transmitted at stipulated traction sub-station of Indian Railways in terms of PPAs with Nodal Railways. The Committee further notes that the Company has entered into PPA with WCR on 29.10.2014 and then entered into PPA with NWR on 17.04.23 for wheeling and supply of 26 MW power. The Committee has examined the issue from the perspective of latest PPA entered with NWR and has not examined the PPA entered into with WCR.

13. With regard to accounting for windmill plant as PPE, the Committee notes that the issue involves determination of whether the agreement to sell energy/electricity to the NWR can be treated as a finance lease under Ind ASs or it is a normal transaction of sale and purchase of electricity units generated by the Company from its own PPE. In this context, the Committee notes the following relevant clauses from the PPA between the Company and NWR:

“2 OBLIGATIONS & UNDERTAKINGS OF THE COMPANY

2.1 The Company shall ensure date of commencement of the wheeling after successful commissioning of the Wind Farm by the developer and commencement of the commercial operation date and it is necessary that during the duration of the contract period, the Company shall continue wheeling and supply from 26 MW Power through XYZ/ State DISCOM till the validity of this Agreement, subject to Force Majeure conditions.

2.2 The Company shall ensure supply of entire wind energy generated from the 26 MW Wind Farm to **NWR** for their captive. Power will be injected from 26 MW

Windmill Plant in the State and the Utility will use the entire power for traction use at its Traction Substation points (TSSs) 132 KV & above voltage level emanating from the respective RVPN substations. ...

- 2.3 The Company shall ensure that all the requisite permissions/statutory clearances, as per relevant provisions, required for setting up the 26 MW wind farm will be obtained from SRECL.”

“3.0 OBLIGATIONS & UNDERTAKINGS OF NWR

NWR shall ensure consumption of entire wind energy from 26 MW Wind Farm for their captive use. ...

- 3.2 NWR shall pay the monthly bills raised by the Company.”

- “4.1 From and after the date of commencement of wheeling, (the Company shall wheel the power through respective state electricity authority and NWR shall consume the entire power (delivered from the 26 MW wind Farm) at all times as per schedule 1 of this Agreement. As per earlier agreement with WCR, the Price of Power was kept to be paid by WCR at the tariff as per CERC guidelines with modifications (based on actual expenditure) and equity IRR @19% before tax, as per the tariff mechanism given in the enclosed Financial Model at Annexure 3(A) & 3(B). Now, as proposed by the Company vide their recent letter ...dated 22.06.2022 that the NWR shall pay the price of power from 26 MW wind power plant at the rate of Rs. 6.27/kWh with an equity IRR of 10.69% before tax instead of 19%.

Any change in the variables forming parts of financial model will have direct bearing on tariff. Such variation and any other losses as applicable will also be loaded in financial model and tariff will be modified accordingly.”

“7.0 TENURE OF AGREEMENT

- 7.1 This agreement shall become effective upon its execution and delivery thereof to both the Parties. All provisions of this Agreement shall continue to be in force for a period of Twenty Five Years from the date of Commencement of Supply of power or till the life of the Wind Farm, whichever is later.

- 7.2 This Agreement may be renewed for such additional period(s) and on such terms and conditions as may be mutually agreed upon between the parties.”

14. The Committee now examines whether the arrangement in the extant case can be considered as a ‘lease’ within the scope of Ind AS 116, ‘Leases’. In this context, the Committee notes the following paragraphs from Ind AS 116:

“LeaseA contract, or part of a contract, that conveys the right to use an asset (the **underlying asset**) for a period of time in exchange for consideration.”

“9 At inception of a contract, an entity shall assess whether the contract is, or contains, a lease. A contract is, or contains, a lease if the contract conveys the right to control the use of an identified asset for a period of time in exchange

for consideration. Paragraphs B9–B31 set out guidance on the assessment of whether a contract is, or contains, a lease.”

“B9 To assess whether a contract conveys the right to control the use of an identified asset (see paragraphs B13–B20) for a period of time, an entity shall assess whether, throughout the *period of use*, the customer has both of the following:

- (a) the right to obtain substantially all of the economic benefits from use of the identified asset (as described in paragraphs B21–B23); and
- (b) the right to direct the use of the identified asset (as described in paragraphs B24–B30).”

“Right to obtain economic benefits from use

B21 To control the use of an identified asset, a customer is required to have the right to obtain substantially all of the economic benefits from use of the asset throughout the period of use (for example, by having exclusive use of the asset throughout that period). A customer can obtain economic benefits from use of an asset directly or indirectly in many ways, such as by using, holding or sub-leasing the asset. The economic benefits from use of an asset include its primary output and by-products (including potential cash flows derived from these items), and other economic benefits from using the asset that could be realised from a commercial transaction with a third party.

B22 When assessing the right to obtain substantially all of the economic benefits from use of an asset, an entity shall consider the economic benefits that result from use of the asset within the defined scope of a customer’s right to use the asset (see paragraph B30). For example:

- (a) if a contract limits the use of a motor vehicle to only one particular territory during the period of use, an entity shall consider only the economic benefits from use of the motor vehicle within that territory, and not beyond.
- (b) if a contract specifies that a customer can drive a motor vehicle only up to a particular number of miles during the period of use, an entity shall consider only the economic benefits from use of the motor vehicle for the permitted mileage, and not beyond.”

“Right to direct the use

B24 A customer has the right to direct the use of an identified asset throughout the period of use only if either:

- (a) the customer has the right to direct how and for what purpose the asset is used throughout the period of use (as described in paragraphs B25–B30); or
- (b) the relevant decisions about how and for what purpose the asset is used are predetermined and:
 - (i) the customer has the right to operate the asset (or to direct others to operate the asset in a manner that it determines) throughout the period of

use, without the supplier having the right to change those operating instructions; or

- (ii) the customer designed the asset (or specific aspects of the asset) in a way that predetermines how and for what purpose the asset will be used throughout the period of use.

How and for what purpose the asset is used

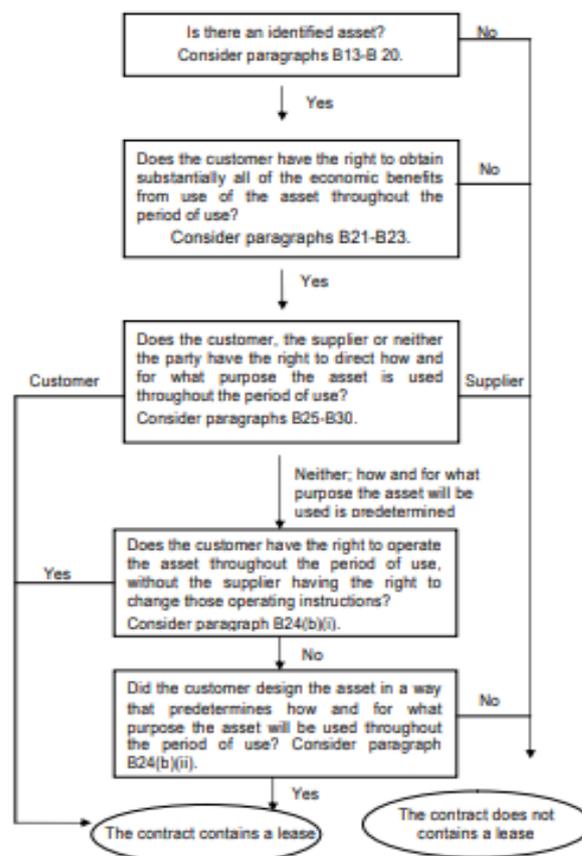
- B25 A customer has the right to direct how and for what purpose the asset is used if, within the scope of its right of use defined in the contract, it can change how and for what purpose the asset is used throughout the period of use. In making this assessment, an entity considers the decision-making rights that are most relevant to changing how and for what purpose the asset is used throughout the period of use. Decision-making rights are relevant when they affect the economic benefits to be derived from use. The decision-making rights that are most relevant are likely to be different for different contracts, depending on the nature of the asset and the terms and conditions of the contract.
- B26 Examples of decision-making rights that, depending on the circumstances, grant the right to change how and for what purpose the asset is used, within the defined scope of the customer's right of use, include:
- (a) rights to change the type of output that is produced by the asset (for example, to decide whether to use a shipping container to transport goods or for storage, or to decide upon the mix of products sold from retail space);
 - (b) rights to change when the output is produced (for example, to decide when an item of machinery or a power plant will be used);
 - (c) rights to change where the output is produced (for example, to decide upon the destination of a truck or a ship, or to decide where an item of equipment is used); and
 - (d) rights to change whether the output is produced, and the quantity of that output (for example, to decide whether to produce energy from a power plant and how much energy to produce from that power plant).
- B27 Examples of decision-making rights that do not grant the right to change how and for what purpose the asset is used include rights that are limited to operating or maintaining the asset. Such rights can be held by the customer or the supplier. Although rights such as those to operate or maintain an asset are often essential to the efficient use of an asset, they are not rights to direct how and for what purpose the asset is used and are often dependent on the decisions about how and for what purpose the asset is used. However, rights to operate an asset may grant the customer the right to direct the use of the asset if the relevant decisions about how and for what purpose the asset is used are predetermined (see paragraph B24(b)(i)).

Decisions determined during and before the period of use

B28 The relevant decisions about how and for what purpose the asset is used can be predetermined in a number of ways. For example, the relevant decisions can be predetermined by the design of the asset or by contractual restrictions on the use of the asset.

B29 In assessing whether a customer has the right to direct the use of an asset, an entity shall consider only rights to make decisions about the use of the asset during the period of use, unless the customer designed the asset (or specific aspects of the asset) as described in paragraph B24(b)(ii). Consequently, unless the conditions in paragraph B24(b)(ii) exist, an entity shall not consider decisions that are predetermined before the period of use. For example, if a customer is able only to specify the output of an asset before the period of use, the customer does not have the right to direct the use of that asset. The ability to specify the output in a contract before the period of use, without any other decision-making rights relating to the use of the asset, gives a customer the same rights as any customer that purchases goods or services.”

“B31 The following flowchart may assist entities in making the assessment of whether a contract is, or contains, a lease.



From the above, the Committee notes that a contract is, or contains, a lease if it conveys the right to control the use of an identified asset for a period of time in exchange for consideration. Further, to assess whether a contract conveys the right to control the use of an identified asset for a period of time, an entity shall assess whether, throughout the period of

use, the customer has the (i) right to obtain substantially all of the economic benefits from use of the identified asset and (ii) right to direct the use of the identified asset. In this context, the Committee analyses the arrangement in the extant case as follows:

(i) *Is there an identified asset:* In this regard, the Committee notes that in the extant case, the asset, viz., the windmill plant of 26 MW capacity is specified in the PPA and the supplier, viz., the Company, does not have substantive right to substitute the specified plant. *Thus, an identified asset exists in the extant case.* Further, the PPA defines the term of the agreement (which is 25 years) and the consideration for the electricity generated from the use of such asset.

(ii) *Does the customer have the right to obtain substantially all of the economic benefits from use of the asset throughout the period of use:* The Committee notes that paragraph B21 of Ind AS 116 specifies that a customer can have that right, for example, by having exclusive use of the identified asset throughout the period of use. In this regard, the Committee notes that clause 2.2 of the PPA states that the Company shall ensure supply of *entire wind energy generated from the 26 MW wind farm* to NWR for their captive use. This indicates that *NWR has the right to obtain substantially all of the economic benefits from the use of identified asset over the 25-year period of use.*

(iii) *Does the customer, the supplier or neither the party have the right to direct how and for what purpose the asset is used throughout the period of use:* The Committee notes that as per paragraph B25 of Ind AS 116, a customer has the right to direct how and for what purpose the asset is used if, within the scope of its right of use defined in the contract, it can change how and for what purpose the asset is used throughout the period of use. In making this assessment, an entity considers the decision-making rights that are most relevant to changing how and for what purpose the asset is used throughout the period of use, such as, rights to change the type of output that is produced by the asset, when/where/whether the output is to be produced and quantity of output produced, etc. The Committee notes that in the extant case, as per PPA, location of wind plant is fixed; and considering the nature of asset, the type of output that is produced by asset, viz., power is fixed/predetermined. Further, since the plant is to be operated on must-run basis, decisions regarding when and whether the output is to be produced are fixed/ predetermined. Therefore, the Committee is of the view that in the extant case, *relevant decisions about how and for what purpose the asset is used are predetermined* and neither the customer (NWR) nor the supplier has any right to change how and for what purpose the plant is used throughout the period of use.

In this context, the Committee notes that paragraph B24 specifically provides that if the relevant decisions about how and for what purpose the asset is used are predetermined, a customer has the right to direct the use of an identified asset throughout the period of use if:

- (a) the customer has the right to operate the asset (or to direct others to operate the asset in a manner that it determines) throughout the period of use, without the supplier having the right to change those operating instructions or
- (b) the customer designed the asset (or specific aspects of the asset) in a way that predetermines how and for what purpose the asset will be used throughout the period of use.

The Committee analyses these points as follows:

(a) Whether the customer has the right to operate the asset (or to direct others to operate the asset in a manner that it determines) throughout the period of use, without the supplier having the right to change those operating instructions: The Committee notes that in the extant case, the customer (NWR) does not operate the plant and the Company makes all the decisions about how the plant is operated throughout the period of use. Thus, NWR has the same rights regarding the use of the plant as if it were one of many customers obtaining power from the plant. Therefore, *NWR does not have the right to operate the asset throughout the period of use.*

(b) Whether the customer designed the asset (or specific aspects of the asset) in a way that predetermines how and for what purpose the asset will be used throughout the period of use: In this regard, the Committee is of the view that the assessment should be made as to whether the customer made the design decisions that most significantly affect the economic benefits to be derived from the use of the asset, such as, determining the technical functionality or overall capacity, selecting the specific equipments to be installed, make and number of equipments to be installed, selecting the site location and layout, etc. The Committee notes that in the extant case, the customer's involvement was limited to giving broad guidelines to be respected by the supplier (the Company); however various decisions significantly affecting economic benefits from use of the asset (for example, in terms of its exact engineering, locations, etc.) are left to the discretion of the supplier. Therefore, it seems from the facts supplied that *the customer did not design the plant.*

Thus, the customer (viz., NWR) in the extant case does not have the right to direct how and for what purpose the plant is used. Therefore, the Committee is of the view that in the extant case, the PPA cannot be considered as a lease agreement of windmill plant and should not be accounted for as per the requirements of Ind AS 116.

Further, since the Company owns and controls the windmill plant and fulfills the recognition conditions of Ind AS 16, as reproduced below, it should be considered as PPE of the Company:

“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.”

D. Opinion

15. On the basis of the above and subject to paragraph 11 above, the Committee is of the opinion that the PPA cannot be considered as a lease agreement of windmill plant in the extant case and should not be accounted for as per the requirements of Ind AS 116, as discussed in paragraph 14 above. Further, windmill plant should be accounted for as PPE of the Company, as per the requirements of Ind AS 16, as discussed in paragraph 14 above.