Query No. 15

Subject: Timing of capitalisation of partly completed gas pipeline (Phase I) under Ind AS framework. [1]

A. Facts of the Case

1. In March 2015, the Ministry of Petroleum and Natural Gas (MoP&NG), Government of India (GoI), had constituted a committee to prepare a vision document, namely, Hydrocarbon Vision 2030 for North-East India.

2. The objectives of the vision document were to leverage the region's hydrocarbon potential, enhance access to clean fuels, improve the availability of petroleum products, facilitate economic development and link common people to the economic activities in this sector. The states covered in the vision document include Arunachal Pradesh, Assam, Manipur, Meghalaya, Mizoram, Nagaland, Sikkim and Tripura.

The phase-wise implementation of the gas pipelines envisaged in the vision document for Northeast was reviewed by the sub-committee during its meetings from April to July 2016, and the development plan of the North-East Gas pipeline Grid (NEGG) was finalised.

In December 2017, MoP&NG convened a meeting of oil and gas public sector undertakings (PSUs) to discuss the modalities for developing the natural gas pipeline grid in the Northeast.

As per the plan, gas pipeline grid to be developed in the Northeast connecting Guwahati to state capital/major cities in the Northeast viz. Itanagar, Numaligarh, Dimapur, Imphal, Aizawl, Agartala, Shillong, Silchar, Gangtok, etc. (excluding Barauni-Guwahati pipeline section). Further, it was decided to also connect to Kohima, the state capital of Nagaland and which is about 80 Kms away from Dimapur.

3. NITI Aayog's approval for the formation of Joint Venture Company (JVC) has been granted on 19.6.18. Accordingly, the Joint Venture Agreement for formation of a JVC (hereinafter referred to as 'the Company') has been signed by the five companies on 20.7.2018 to develop and operate natural gas pipeline grid in North-East and the Company has been registered on 10.8.2018.

4. The Company has requested MoP&NG to issue the necessary policy directive to Petroleum and Natural Gas Regulatory Board (PNGRB) for grant of authorisation to the Company for laying of the pipeline grid. MoP&NG has accordingly issued policy directive to PNGRB for grant of authorisation. The same was granted by PNGRB on 17.11.2020.

Implementation strategy

5. Due to its rich flora and fauna, laying of this pipeline grid attracts various statutory permissions like wildlife clearance (EC) and forest clearance apart from other crossing permissions like railways, irrigation, road etc. in different mainline sections. In view of the complexities involved in this pipeline grid for availability of right of way and associated clearances/permissions, there was a need to identify the sections/stretches and grade them

[1] Opinion finalised by the Committee on 10.7.2025.

as per the ease of laying pipeline. As per the difficulty level associated with various sections, an implementation strategy was prepared to implement the project in phase-wise manner.

Upon review of the route details, it was assessed that the entire North-East Gas Grid may be planned to be implemented in 3 phases based on requirement of statutory clearance, route terrain, linkage with highway corridor widening works, difficulty in work execution etc. Phasing of various sections of North-East Gas Grid was proposed as under:

Phase I: Sections with plain agricultural terrain and no requirement of EC

a. Guwahati- Numaligarh with branch line to Itanagar and Spur line to Numaligarh (estimated length-421 Km)
b. Numaligarh/Dergaon (Jorhat) - Dimapur section and 5 feeder lines from one of the investor in the Company, O Ltd.'s fields (estimated length-147 Km)

Phase II: Sections in hilly terrain and having requirement of EC

a. Guwahati- Shillong- Silchar – Panisagar and Banaskandi feeder line (estimated length -386 Km)
b. Panisagar-Agartala and feeder lines (2 No.) and spur line to N Ltd., a power generation company in the North-Eastern Region (estimated length 231 Km)
c. Panisagar-Aizawl branch line (estimated length 111 Km)

Phase III: Sections in hilly terrain, requirement of EC and feasibility of laying of pipeline linked to highway width widening

a. Dimapur-Kohima Section (estimated length -94 Km)
b. Kohima- Imphal Section (estimated length-105 Km)
c. Siliguri-Gangtok Section (estimated length – 195 Km)

Gas Injection points

6. Following gas injection points have been considered in the Detailed Feasibility Report (DFR):

Injection from Guwahati with upcoming Barauni-Guwahati pipeline (BGPL)

The gas received through the upcoming Barauni-Guwahati Natural Gas (NG) Pipeline (BGPL) of G Ltd. (one of the investor in the Company) would be injected into the North-East Gas Grid (NEGG). Barauni-Guwahati pipeline would have the flexibility/connectivity to receive gas either from Dahej/Hazira/Dabhol through G Ltd.'s existing gas pipeline network along with Jagdishpur-Barauni section of Jagadishpur-Haldia-Bokaro-Dhamra Pipeline (JHBDPL) or from Dhamra R-LNG terminal through JHBDPL.

From Guwahati, R-LNG (Re gasified liquid natural gas) will be made available to the remaining north-eastern states through the proposed pipeline network.

Guwahati-Numaligarh section would originate from a tap-off point at a suitable location on G Ltd.'s BGPL at north bank of Brahmaputra. *Guwahati-Shillong-Silchar section* would originate from G Ltd.'s BGPL terminal at the south bank. Thus, there would be 2 dispatch terminals at Guwahati.

Injection from marginal gas fields

The natural gas pipeline grid would have the facility for injection of indigenously produced gases also. Connectivity from local marginal fields as well as source line/spur lines into North-East Gas Grid has been considered in this DFR. The upstream source/pipeline operator would make necessary arrangements for availability of requisite pressure at source for gas injection into the Grid, as per the hydraulics.

The domestic gas sources (9 nos.) of O Ltd. have been considered in the DFR for connectivity to the Grid including laying of connectivity pipeline.

7. The original phase-wise estimated cost approved as per DFR by MOP&NG through Cabinet Committee of Economic Affairs (CCEA) are given in table below:

Heads of Expenses	Phase-I	Phase-II	Phase-III	Total
RoU (Right of Use)	250	837	265	1352
Civil work	38			38
Land Purchase	25	16	18	59
Land	10			10
Line Pipes	1049	877	428	2355
Laying cost	1186	763	512	2460
Compressor station	400			400
Station (IP, Sectional Valves & Terminal station)	252	340	224	816
SCADA	13	6	2	22
Telecom equipments	30	23	33	86
Permanent Cathodic Protection for Line Piep coating	11	14	8	33
Contingency	12	3	14	29
Project Management cost	61	62	7	130
Owner Management Expenses	139	112	76	328
Head office expenses	148			148
Interest During construction	501	335	164	1000
Grand Total	4124	3388	1752	9265

Sources of Fund

The Company's Board in its 15th meeting held on 6th June 2020 had approved the NEGG Project with the estimated capital expenditure (CAPEX) of Rs. 9265.20 crores with 60% viability gap fund (VGF) from GoI to the tune of Rs. 5559 crores. The balance 40% of the project cost was to be arranged with debt and equity in the ratio of 70:30. The equity contribution was considered for Rs. 1111.80 crore and debt in the form of OIDB loan for Rs. 2594 crores.

Completion Schedule

8. Phase-wise milestones along with completion schedule as initially approved by MoP&NG has been separately supplied by the querist for the perusal of the Committee. On 17.10.2023, PNGRB has issued the extension letter for completion of all the three phases by 31.03.2025. Further, the completion schedule for all the three phases along with revised timeline has been provisionally granted by MoP&NG vide letter dated 07.03.2025.

Description of Guwahati Numaligarh Pipeline Section –(Phase-I)

9. This pipeline is to be constructed from Dispatch Terminal (DT) at Baihata (Guwahati) at 0.00 Km chainage and will stretch up to Receipt Terminal (RT) at Numaligarh refinery. The total distance between DT Baihata to RT at Numaligarh is around 392 Km. As per the prevalent practice being followed by established pipeline operators (i.e. G Ltd.), along with the pipeline network, various infrastructure facilities are also required to be set up for monitoring the pipeline. These infrastructure facilities include setting up of sectional valves, Dispatch Terminal station (DT), Intermittent Pumping station (IP), Receipt Terminal station (RT). Basically, intermittent station is constructed at an interval of 80 Km to 100 Km i.e. the distance between two intermittent station shall be 80 Km to 100 Km. Similarly sectional valves are constructed at an interval of 16 Km to 24 Km i.e. between two sectional valves the distance shall be 16 to 24 Km (depending upon the availability of land or density of population inhabited in the area). Apart from these, there shall be Dispatch Terminal (DT) Station at the starting point and Receipt Terminal (RT) station at the exit point.

IP stations are like control room which are equipped with infrastructure facilities like supervisory control and data acquisition (SCADA) for controlling and monitoring of natural gas movement on real time data basis by directly interfacing with gas flow. Apart from this, there will be electrical equipment, UPS, solar panels for power supply, telecom systems etc. These stations are operated with manpower.

Sectional valves station also includes electrical equipment, UPS, solar panels, but this station is smaller in size compared to IP station. This station can be operated automatically without manpower deployment. Sectional valves are constructed at an interval of 16 Km to 24 Km to monitor and control the gas flow and help in cleaning and disconnecting/isolating the particular pipeline section in case of any hazards on account of fire.

Guwahati-Numaligarh Pipeline section, which is 392 Km long (revised from 386 Km) constitutes a compressor station, 3 IP stations, 23 Sectional valves, 1 Dispatch Terminal Station at starting point (Baihata) and 1 Receipt Terminal station at ending point (Numaligarh).

The total cost of the Guwahati-Numaligarh pipeline section considered at the initial DFR stage was Rs. 4124 crore.

Accounting treatment

10. Accounting policy of the Company:

Expenses exclusively attributable to NEGG Project and incurred during construction or development period are considered as Capital Work-in-Progress (CWIP) which includes:

i) Construction Stores including material in transit/equipment/services received at site for use in the projects, including advance payment for land not yet capitalised etc.

ii) Crop compensation is accounted under Capital Work-in-Progress on the basis of actual payments/estimated liability where right of use (RoU) is acquired.

iii) All expenses incurred during construction period until the asset is ready for intended use, which are exclusively attributable to acquisition/construction of the asset.

iv) Borrowing costs incurred during construction and development period on loans borrowed and utilised for project upto date of capitalisation of the relevant portion are considered as CWIP.

Property, Plant and Equipment (PPE) (Ind AS 16)

a) The Costs of an item of PPE is recognised as an asset if, and only if:

   i) it is probable that the future economic benefits will flow to the entity; and

   ii) the cost of an item can be measured reliably.

b) Property, plant and equipment are stated at their original cost net of eligible tax credit availed. The cost of PPE comprises its purchase price, freight and directly attributable costs and any incidental expenses relating to acquisition, installation, construction, and decommissioning costs as the case may be. *These costs are capitalised until the asset is brought into the location and condition necessary for it to be capable of operating in the manner intended by management.* Assets during construction are initially kept under assets under construction and capitalised when the assets are available for use in the manner as intended by the management.

Incidental expenses are incurred in connection with the construction or development of item of property, plant and equipment and are necessary to bring the item to the location and condition necessary for it to be capable of operating in the manner intended by management. This incidental expenditure may occur before or during the construction or development activities for example, expenditure of Head Office which are incurred before or in the course of construction or development of property, plant and equipment are recognised based on their carrying value standing at the time of apportionment to PPE.

11. *Current status of the Guwahati-Numaligarh pipeline section (392 Km revised from 386 Km)*

Phase-I: The estimated pipeline length of phase-I is 553 Km which comprises of following sections:

Sections include Guwahati-Numaligarh (392 Km in Assam), Gohpur-Itanagar (13 Km Assam, 14 Km Arunachal Pradesh), Dergaon-Dimapur (97 Km Assam, 26 Km Nagaland), and O Ltd. feeder line (11 Km Assam).

The Company has awarded to M/s M Ltd., contract of project management consultancy (PMC) services for NEGG project. The following pipelines along with terminals are to be executed initially under NEGG project:

A. Section 1 Guwahati- Numaligarh (NRL) 24" NB x 392 Km (approx.) mainline.

B. Section 2 Gohpur- Itanagar-8" x 27 Km (approx.) spurline in states of Assam and Arunachal Pradesh.

The brief scope of work includes supply of materials (other than free issue), pipe laying work including but not limited to construction management, HSE & quality management, survey, RoU management, clearing of RoU, grading, stringing, bending, welding (manual/semi-automatic/automatic), trenching, joint coating, lowering, crossings, crossings by HDD (wherever specified), tie-ins, NDT and destructive testing, backfilling, laying of pipeline along-with OFC & HDPE ducts, TCP works, site restoration, hydro-testing, dewatering, swabbing, drying, nitrogen purging (as applicable), pre-commissioning, commissioning and gas-in of 24"/8" dia pipeline including construction/installation of related facilities like scraper launching/receiving facilities and piping works at dispatch/receiving terminals, IP stations and piping works at sectionalising valve stations, tap-off station & injection points etc. including associated mechanical, cathodic protection, corrosion monitoring works, electrical works, telecom works, firefighting works, instrumentation, civil works (including boundary wall and building works), architectural and structural works at all stations and pipeline information management system.

12. For ease of execution, keeping in view the initial scheduled timeline prescribed by the MoP&NG, the scope of work for Guwahati-Numaligarh pipeline section has been divided into 4 (four) Parts:

Part A: 24" x 97.5 Km (Assam State)	Laying and terminal works from *DT at Ch. 0.00* (including pipeline from top on BGPL line to DT) *to IP-1 at Ch. 97.5 Km* including associated works at four (04) SV stations, one (01) IP station and one (01) Dispatch Terminal.
Part B: 24" x 93.6 Km (Assam State)	Laying and terminal works from *IP-1 at Ch. 97.5 Km to IP-2 at Ch 191.1 Km* including associated works at four (04) SV stations and two (02) IP stations excluding terminal works at IP-1.
PART C: 24" x 105.539 Km and 8" x 27 km. Approx. (Assam and Arunachal Pradesh State)	*For 24" (Mainline)* Laying and terminal works from *IP-2 at Ch. 191.1 Km to IP-3 at Ch. 296.639 Km* including associated works at five (05) SV stations and two (02) IP stations excluding terminal works at IP-2. *For 8" (Itanagar Spurline)* Laying and terminal works from *SV-10 cum DT at Barphalong Gaon at Ch.0.00 Km to RT- Itanagar at Ch. 26.994 Km* including associated works at one (01) SV Station, one (01) DT and one (01) RT at Itanagar.
Part D: 24" x 89.629 Km (Assam State)	Laying and terminal works from *IP-3 at Ch. 296.639 Km to RT Numaligarh at Ch. 386.264 Km* including associated works at three (03) SV stations, one (01) IP Station and one (01) RT at Numaligarh excluding terminal works at IP-3.

As on 31.03.2025, total costs incurred for Phase -1 are given in the table below:

Section	Cost Incurred (amount in crores)
Guwahati-Numaligarh section (392 Km)	2514.00
Gohpur-Itanagar (27 Km)	57.00
Dergaon-Dimapur (123 Km)	370.00
O Ltd. feeder lines (11 Km)	19.00
Total cost incurred till date	2960.00

Detailed break-up of the cost incurred till date for Phase-I is given in table below:

(In Cr.)

Particulars	Line Pipes & Material (Inlcuding Line Pack)	Mainline Construction & HDD	RoU & Survey**	Owners management exp.**	PMC	Land	Interest during Construction	Pump, Station & Terminals	Compressor Station package	Grand Total
Guwahati - Numaligarh Pipeline	825	910	142	195	28	44	35	166	168	2,514
Gohpur - Itanagar Pipeline	20	12	10	1	1	9	0	5	-	57
Dergaon - Dimapur pipeline	112	63	156	7	3	7	3	19	-	370
Feeder Lines	16	3	-	0	-	0	0	1	-	19
	973	988	307	203	32	60	38	191	168	2,960

It is to be noted that Guwahati-Numaligarh pipeline section (392 Km, revised from 386 Km) has been planned for connecting the Numaligarh Refinery which is the anchor customer for this NEGG project as per DFR. Numaligarh Refinery is presently undergoing expansion from 3MMTPA capacity of crude to 9MMTPA of crude for which, it requires natural gas of 2.4 MMSCMD for its captive power plant consumption. As per original DFR, NEGG pipeline will be used for transportation of natural gas from integrated G Ltd.'s pipeline at Baihata to Numaligarh refinery which is situated at a distance of 392 Km (revised from 386 Km). The Company will construct Receiving Terminal (RT) at Numaligarh Refinery from where the natural gas will be received and further transported to Numaligarh Refinery through hook up facility within its premises.

On 10.03.2025, 50% of the laying of pipeline i.e. 195.898 Km was mechanically completed and certificate of completion issued along with infrastructure facilities like sectional valves, control building, SCADA, UPS and electrical equipment. However, the balance 50% is in construction stage and projected to be completed by July 2025. One of the important criteria for commissioning of the pipeline is inspection by Petroleum and Explosives Safety Organisation (PESO). This inspection was completed for 195.898 Km in March 2025 and for balance portion i.e. 195.898 Km, inspection by PESO is expected to be completed by June 2025. Moreover, the completion of Phase-I as mandated by MoP&NG is July 2025 so that commercial operation will start from July 2025.

As on date, although laying of pipeline of 195.898 Km has been mechanically completed and completion certificate issued but the completion of Guwahati-Numaligarh section which is of 392 Km (revised from 386 Km) is not fully completed and commissioned. Ideally, completion and commissioning of half portion of the Guwahati-Numaligarh section will not meet the objective of transporting natural gas from Baihata (G Ltd.'s Dispatch Terminal) to Numaligarh

Refinery until and unless entire 392 Km of pipeline is mechanically completed and commissioned. The pipeline section of Guwahati-Numaligarh is the main section of Phase-I as evident from the DFR where Numaligarh will be the anchor customer for taking the natural gas. Moreover, the commercial operation of the Guwahati-Numaligarh pipeline section will start once complete 392 Km (revised from 386 Km) pipeline is commissioned. This pipeline asset is intended to be used for meeting the natural gas requirement of Numaligarh Refinery only which is the anchor customer as envisaged in the DFR.

13. As per the Company's audited accounts for financial year (F.Y.) 2024-25, Rs. 2514.00 crore (table above) has been incurred towards Guwahati-Numaligarh pipeline section. These costs are kept under CWIP. Out of this Rs. 2514 crore, the cost incurred for 195.898 Km which is mechanically completed and completion certificate issued is Rs. 1056 crore excluding cost of freehold land and RoU cost which are perpetual in nature. The cost of Rs. 1056 crore includes line pipe cost, laying cost, 8 SV station cost, 2 IP station cost, 1 Dispatch terminal cost (Baihata).

As per the querist, it is to be noted that commercial operation of the Guwahati-Numaligarh pipeline will commence only when the entire pipeline of 392 Km (revised from 386 Km) is completed and commissioned as envisaged in original DFR since Numaligarh Refinery will be the anchor customer for taking the gas through the Company's pipeline network.

B. Query

14. In view of the above, the opinion of the Expert Advisory Committee is sought as to whether the Company should capitalise the total cost (including interest on OIDB loan) incurred till date for 195.898 Km (part of the Guwahati-Numaligarh section) even though (a) part completed pipeline along with infrastructure facilities of 195.898 Km is not brought into the location and condition necessary for it to be capable of operating in the manner intended by management as per original DFR mandate from the Ministry on completion of project phases and section and (b) line is not commercially operated as envisaged.

C. Points considered by the Committee

15. The Committee notes that the basic issue raised in the query relates to the timing of capitalisation of partly completed gas pipeline section (constructed during Phase I of NEGG project) as a completed item of PPE when the construction of the other part or section of the pipeline is not completed and accordingly, the commercial operation of the completed section of pipeline, as envisaged has not yet started. The Committee has, therefore, considered only this issue, and has not examined any other issue that may arise from the Facts of the Case, such as, accounting for individual items of expenditure incurred during the construction (for example, cost of land, cost of various clearances/permissions, construction stores, crop compensation, tax credit availed, incidental expenses, RoU cost, head office expenditure, owner management expenses etc.) as to whether these are directly attributable or can be included or recognised as an item of PPE or pipeline project cost or not, accounting for expenditure incurred during Phase II and III of the pipeline project, accounting for inflow from various sources of funds, including viability gap funding from government, debt, equity etc., accounting for transactions between the Company and the PMC, accounting in the financial statements of investor entities, etc. The Committee wishes to point out that the opinion expressed hereinafter is in the context of Indian Accounting Standards, notified under the Companies (Indian Accounting Standards) Rules, 2015 as amended from time to time. Further, the opinion expressed hereinafter is purely from accounting perspective and not from any other perspective, such as Income-tax Act, Goods and

Services Tax Act, interpretation of vision document of MoP&NG, policy directives issued by MoP&NG to PNGRB for grant authorisation, detailed feasibility report (DFR), extension letter issued by PNGRB, etc.

16. The Committee notes that the Company is constructing Guwahati-Numaligarh pipeline section (392 Km) for connecting the Numaligarh Refinery, which is the anchor customer during Phase I of NEGG project as per DFR. Numaligargh Refinery is undergoing expansion and requires natural gas for its captive power plant consumption. As per original DFR, NEGG pipeline will be used for transportation of natural gas from integrated pipeline of G Ltd. (who is one of the investor entity in the Company) at Baihata to Numaligarh refinery (who is also investor entity in the Company) which is situated at a distance of 392 Km. The Company will construct Receiving Terminal (RT) at Numaligarh Refinery from where the natural gas will be received and further transported to Numaligarh Refinery through hook up facility within its premises.

On 10.03.2025, 50% of the laying of pipeline, i.e. 195.898 Km was mechanically completed along with infrastructure facilities like sectional valves, control building, SCADA, UPS and electrical equipment in place and certificate of completion issued. However, the balance 50% is in construction stage and projected to be completed by July 2025. Further, since the completion of Guwahati-Numaligarh section which is of 392 Km is not fully completed and commissioned, the querist has stated that ideally, completion and commissioning of half portion of the Guwahati-Numaligarh section *will not meet the objective* of transporting natural gas from Guwahati to Numaligarh Refinery until and unless entire 392 Km of pipeline is mechanically completed and commissioned. Moreover, as per the querist, the *commercial operation* of the Guwahati-Numaligarh pipeline section will start once complete 392 Km (revised from 386 Km) pipeline is commissioned and that this pipeline asset is intended to be used for meeting the natural gas requirement of Numaligarh Refinery *only*, which is the anchor customer.

17. With regard to the issue raised, the Committee notes the following paragraphs of Indian Accounting Standard (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."**
>
> "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."

"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;

(b) initial operating losses, such as those incurred while demand for the item's output builds up; and

(c) costs of relocating or reorganising part or all of an entity's operations."

"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 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 recognition of costs in the carrying amount of an item of property, plant and equipment (PPE) (including self-constructed asset) should cease at the time when the item is *in the location and condition necessary for it to be capable of operating* in the manner intended by management. Thus, from such point in time, the item under construction should be transferred from capital work in progress to the gross block of PPE. The Committee is of the view that the point in time when an asset is *in the location and condition necessary for it to be capable of operating* in the manner intended by management is a question of fact which should be determined in the specific facts and circumstances on the basis of various factors, such as, technical evaluation of the readiness of the asset, completion of test runs to ensure that the asset is functioning properly etc. Further, as per paragraph 20 of Ind AS 16, 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 are not included in the

carrying amount of an item of PPE. Thus, when an item of PPE is in the location and condition necessary for it to be *capable of operating in the manner intended by management, but has yet to be brought into use, the costs incurred subsequently are not included in the cost or carrying amount of PPE.* Accordingly, the Committee notes that what is important is when the PPE/asset is in the location and condition necessary for it to be *capable of operating in the manner intended by management* and not the actual operation/use or the intended capacity or standard of performance to be achieved.

In this context, the Committee also notes the following requirements of Ind AS 23, 'Borrowing Costs', which although addresses the issue from the point of view of borrowing costs, however, the Committee is of the view that the principle enunciated in those paragraphs can be applied to other expenditures also:

> **"24 When an entity completes the construction of a qualifying asset in parts and each part is capable of being used while construction continues on other parts, the entity shall cease capitalising borrowing costs when it completes substantially all the activities necessary to prepare that part for its intended use or sale.**
>
> 25 A business park comprising several buildings, each of which can be used individually, is an example of a qualifying asset for which each part is capable of being usable while construction continues on other parts. An example of a qualifying asset that needs to be complete before any part can be used is an industrial plant involving several processes which are carried out in sequence at different parts of the plant within the same site, such as a steel mill."

From the above, the Committee is of the view that in case of an integrated PPE/project having several units/parts, those units/parts of the PPE/project which are capable of being used individually (while the construction continues for the other units/parts), and can be operated independently of the remaining units/parts, should be considered to be in the location and condition necessary for them to be capable of operating in the manner intended by management and further capitalisation of costs should be ceased (viz., the completed units/parts should be transferred from CWIP to gross block of PPE).

In this regard, the Committee notes from the facts supplied in the extant case that 195.898 Km of the Guwahati-Numaligarh pipeline section has been mechanically completed and associated infrastructure facilities (like sectional valves, control building, SCADA, UPS and electrical equipment) are in place. Further, the relevant inspection by PESCO (which as per the querist, is one of the important relevant criteria for commissioning) in respect of this section of pipeline has already been completed and completion certification has also been issued by the relevant authorities. However, as per the querist, completion and commissioning of half portion of the Guwahati-Numaligarh section will not meet the objective of transporting natural gas from Guwahati to Numaligarh Refinery until and unless entire 392 km of pipeline is mechanically completed and commissioned. Moreover, as per the querist, the pipeline asset is intended to be used for the requirements of Numaligarh Refinery *only* whereat the Company will construct one receiving terminal (RT) for the entire 392 km pipeline. Thus, it appears from the facts supplied by the querist that the completed pipeline stretch of 195.898 Km could be put to its ultimate use only when the entire pipeline stretch of 392 kms is completed and ready for use and this section (195.898 km) is not independently capable of being operated in the manner intended by management. In other words, the partially completed line cannot be considered as

ready for its intended use till the complete stretch of 392 Km is ready. In view of the aforesaid assertions made by the querist, the Committee presumes that the Company has carefully evaluated on the basis of technical evaluation based on its own facts and circumstances that the completed section of pipeline is not yet ready for commercial operation and is not capable of being used individually, independent to other parts. Accordingly, the Committee is of the view that in the extant case, the partially completed section (195.898 Km), despite physical completion, does not appear to be in the location and condition necessary for it to be capable of operating in the intended manner as per the requirements of Ind AS 16 and thus, capitalisation of further costs on this section should not be ceased and it should remain as capital work in progress (CWIP).

18. Now, the Committee examines the issue with regard to capitalisation of interest cost on OIDB loan in respect of partly completed pipeline. In this regard, the Committee notes the following paragraphs of Ind AS 23, 'Borrowing Costs':

> **"8 An entity shall capitalise borrowing costs that are directly attributable to the acquisition, construction or production of a qualifying asset as part of the cost of that asset. An entity shall recognise other borrowing costs as an expense in the period in which it incurs them."**
>
> **"A *qualifying asset* is an asset that necessarily takes a substantial period of time to get ready for its intended use or sale."**
>
> **"22 An entity shall cease capitalising borrowing costs when substantially all the activities necessary to prepare the qualifying asset for its intended use or sale are complete."**

From the above, the Committee notes that the borrowing costs that are directly attributable to the acquisition, construction or production of a qualifying asset are to be capitalised, and other borrowing costs are to be expensed. Further, a qualifying asset is an asset that necessarily takes a substantial period of time to get ready for its intended use or sale. Since the pipeline project in the extant case takes substantial period of time for its construction, it is a qualifying asset and therefore, the borrowing costs that are directly attributable to the acquisition or construction of the same, as per the principles of Ind AS 23 should be capitalised. Further, as per paragraph 22 of Ind AS 23, the borrowing costs should cease to be capitalised when substantially all the activities necessary to prepare the qualifying asset for *its intended use* are complete. The Committee also notes from paragraphs 24 and 25 of Ind AS 23 (as reproduced and discussed in paragraph 17 above) that capitalisation of borrowing costs to the completed section of the pipeline should cease when that completed section is capable of being used individually, independent of the other section of pipeline. Since, as discussed above, after careful technical evaluation of the facts and circumstances, it has been concluded by the Company that the partially completed pipeline/section is not capable of being used individually, independent to other parts and therefore, cannot be considered to be in the location and condition necessary for it to be capable of operating in the intended manner till the complete stretch of 392 Km of pipeline is completed and ready for use, the Committee is of the view that the capitalisation of borrowing cost to the partially completed pipeline will continue till such time.

D. Opinion

19. On the basis of the above, the Committee is of the opinion that it appears from the facts supplied by the querist that the completed pipeline stretch of 195.898 Km could be put to its ultimate use only when the entire pipeline stretch of 392 kms is completed and ready for use and this section (195.898 km) is not independently capable of being operated in the manner intended by management. In other words, the partially completed line cannot be considered as ready for its intended use till the complete stretch of 392 Km is ready. In view of the aforesaid assertions made by the querist, the Committee presumes that the Company has carefully evaluated on the basis of technical evaluation based on its own facts and circumstances that the completed section of pipeline is not yet ready for commercial operation and is not capable of being used individually, independent to other parts. Accordingly, the partially completed section (195.898 Km), despite physical completion, does not appear to be in the location and condition necessary for it to be capable of operating in the intended manner as per the requirements of Ind AS 16 and thus, capitalisation of further costs on this section should not be ceased and it should remain as capital work in progress (CWIP).

Furthermore, as discussed in paragraph 18 above, since after careful technical evaluation of the facts and circumstances, it has been concluded by the Company that the partially completed pipeline/section is not capable of being used individually, independent to other parts and therefore, cannot be considered to be in the location and condition necessary for it to be capable of operating in the intended manner till the complete stretch of 392 Km of pipeline is completed and ready for use, the Committee is of the view that the capitalisation of borrowing costs to the partially completed pipeline will continue till such time.

****