Before the Appellate Tribunal for Electricity

(Appellate Jurisdiction)

Appeal No. 134 of 2009

Dated : 7th April, 2011

Present: Hon'ble Mr. Justice M. Karpaga Vinayagam, Chairperson.

Hon'ble Mr. V.J. Talwar, Technical Member

In the matter of:

Power Grid Corporation of India Ltd.
Suadamani, Plot No 2. Sector 29
Gurgoan 122001
Haryana

……Appellant

VERSUS

1 Central Electricity Regulatory Commission
4TH Floor, Chandralok Building
Janpath, New Delhi -110001

2 Madhya Pradesh State Electricity Board
(Formerly Madhya Pradesh Electricity Board)

P.O. Box No. 34, Rampur
Jabalpur – 482 008

3 Maharashtra State Electricity Board
Prakashgad, 4TH Floor
Bandra (East), Mumbai – 400 052

4 Gujarat Electricity Board
Vidyut Bhawan, Race Course
Baroda – 390 007

5 Electricity Department
Government of Goa,
Vidyut Bhawan, Panaji, Goa – 403 001

6 Electricity Department
Administration of Dadra Nagar Haveli
U.T. Silvassa – 396 230

7 Chhatisgrah State Electricity Board
P.O. Sunder Nagar, Danganiya, Raipur
Chhatisgarh – 492 013

8 Electricity Department
Administration Of Daman & Diu, Daman – 396 210

9 Karnataka Power Transmission Corporation Ltd.
Cauvery Bhawan, Bangalore – 560 009

10 Transmission Corporation of Andhra Pradesh
Vidyut Soudha, Hyderabad – 500 049

11 Kerala State Electricity Board (KSEB)
Vaidyuthi Bhavanam, Pattom,
Trivandrum – 695 004

12 Tamil Nadu Electricity Board (TNEB)
800, Anna Salai, Chennai – 600 002

13 Electricity Department Of Pondicherry
Pondicherry – 605 001

…..Respondents

Counsel for Appellant: Mr. M.G. Ramachandran
Ms. Sneha Venkatramni
Mr. Rohit Shukla

Counsel for Respondents: Mr. Sakesh Kumar for R-2
Mr. P.R. Kovilan Pongkuntran
for Respondent-12

Judgment

Per Hon'ble Shri V.J. Talwar, Technical Member

1. Power Grid Corporation of India (POWERGRID) is the Appellant.

2. Central Electricity Regulatory Commission (Central Commission) is the 1st Respondent. Respondents no 2 to 8 are State Electricity Boards or power Utilities of constituents of Western Region. Respondents no 9 to 13 are State Electricity Boards or Power Utilities of Southern Region.

3. Appellant, POWERGRID had setup HVDC back-to-back station along with associated 400 kV transmission line at Chandrapur, Maharashtra at an estimated cost of Rs 1028.59 crore. Prior to enactment of Electricity Regulatory Commission Act 1998, tariff for this asset was being fixed by Ministry of Power through Notification. After enactment of Electricity Regulatory Commission

Act, 1998 and establishment of Central Commission, Appellant filed the petition before the Central Commission for fixation of tariff for this asset. The Central Commission passed the Order dated 20.08.2002 approving final tariff. However, it did not consider Oversees Development Agency (ODA) grant of Rs 321.55 Crore for calculation of depreciation.

4. Aggrieved over this, the Appellant has filed this appeal, challenging the impugned order.

5. Brief facts of the case are as under:

6. Government of India had approved establishment of HVDC Chandrapur Transmission project at an estimated cost of Rs 900.28 Crore. The scope of the project included

i) Establishment HVDC back-to-back station of 1000 MW (consisting of two poles of 500 MW each) at Chandrapur, Maharashtra and

ii) 400 KV S/C AC transmission line between Ramagundam and Hydrabad and extension of substations at Ramagundam, Hydrabad.

7. Prior to enactment of Electricity Regulation Commission Act, 1998, Ministry of Power, Government of India had been notifying the norms, factors etc. for fixation of tariff in consultation with the Central Electricity Authority. Ministry of Power had also been issuing notifications fixing the tariff for the transmission system built, operated and maintained by POWERGRDID, the Appellant. On 16.12.1997 Ministry of Power issued a Notification requiring the Central Commission (R-1) to fix the transmission tariff as per the policy laid down by the Government of India in this Notification.

8. The estimated cost of project was revised to Rs 1028.59 crore and was approved by Government of India on 10.01.2000. Actual completion cost of the project amounted to Rs 1010.60 Crore. The project was financed through Debt of Rs 530.69 Crore, equity of Rs 79.26 crore and ODA grant of Rs 321.55 Crore.

9. On 19.06.2000 the Appellant filed the petition no 46/2000 before Central Commission for approval of tariff. The petition included tariff calculations based on the notification dated 16.12.1997 to be effective from the date of commercial operation up to 31.03.2002.

10. During pendency of the petition, the Central Commission directed the Appellant, through an interim order dated 22.08.2001, to explain, inter alia, the justification for Oversees Development Agency (ODA) grant being treated as part of capital attracting Return on Equity (RoE) and depreciation etc.

11. Accordingly, on 21.12.2001 POWERGRID, the Appellant submitted its justification for treating ODA grant as capital giving detailed explanation for the same.

12. The Central Commission ultimately passed final Order on 20.08.2002 approving transmission charges for Chandrapur HVDC project. However, Central Commission did not allow depreciation and Operation & Maintenance component of the tariff for Chandrapur HVDC project to the extent of completion cost funded by ODA grant.

13. Being aggrieved by the Central Commission's Order dated 20.08.2002 POWERGRID, the Appellant filed a Review Petition No. 145/2002 in Petition no. 46/200 before the Central Commission (R-1) praying for depreciation and O&M expenses to be allowed on ODA grant.

14. The Review Petition was finally disposed of by the Central Commission through its Order dated 31.03.2003 partly allowing the Review Petition. Though the Central Commission allowed claim of the Appellant with respect to ‘Operation and Maintenance’ charges through this order dated 31.3.2003, but did not allow depreciation on ODA grant component.

15. Aggrieved by the portion of the order dated 31.3.2003, the Appellant filed an Appeal on 30.05.2003 being FAO No. 466 of 2003 before the High Court of Delhi.

16. The Electricity Act 2003 was enacted on 10.06.2003. Appellate Tribunal for Electricity was constituted in May 2005 in terms of Section 110 of the Act.

17. Therefore, the High Court of Delhi transferred the FAO 466 of 2003 to be decided by this Tribunal.

18. In pursuance of the said transfer order, the Appellant has filed the present appeal before this Tribunal.

19. Appellant has raised following grounds in favour of his claim:

   A. Depreciation is to be charged for the purpose of replacement of assets at the end of their useful life. The depreciation is treated as an element of cost based on actual capital expenditure incurred on completion of the project. Therefore this is the appropriate criterion for fixation of tariff.

   B. In case of Chandrapur HVDC back to back station, though a portion of project cost was financed through ODA grant, it nevertheless formed part of the total 'actual capital expenditure' incurred on completion of the project. Therefore a sum of Rs. 321.55 Crores on

account of ODA grant was required to be taken into account while computing the depreciation.

C. The impugned Order is contrary to the law laid down by the Hon'ble Supreme Court in Commissioner of Income Tax Vs. Tata Iron Steel Company Ltd. reported in 1998 (2) SCC 366, wherein the Hon'ble Supreme Court held that:-

> *"Coming to the questions raised, we find it difficult to follow how the manner of repayment of loan can affect the cost of the assets acquired by the assessee. What is the actual cost must depend on the amount paid by the assessee to acquire the asset. The amount may have been borrowed by the assessee. But even if the assessee did not repay the loan it will not alter the cost of the asset. If the borrower defaults in repayment of a part of the loan cost of the asset will not change. What has to be borne in mind is that cost of an asset and*

cost of raising money for purchase of the asset are two different and independent transactions. Even if an asset is purchased with non-repayable subsidy received from the Government the cost of the asset will be the price paid by the assessee for acquiring the asset".

D. Accounting Standard-6 of Institute of Charted Accountants , inter alia, provides as under:-

"Depreciation is a measure of the wearing out consumption or other loss of value of a depreciable asset arising from use efflux of time or obsolescence through technology and market changes. Depreciation is allocated so as to charge a fair proportion of the depreciable amount in each accounting period during the expected useful life of the asset. Depreciation includes amortization of assets whose useful life is predetermined".

E. The conclusion arrived at by the Central Commission on the basis of its earlier order dated 21.12.2000 in Petition No. 4/2000 to the effect that the historical cost of the assets is to be considered for depreciation in the tariff and not the replacement cost of the assets is contrary to law.

The Appellant has also relied on Hon'ble Supreme Court's Judgment in DERC v. BSES Yamuna Power Limited & Others (2007) 3 SCC 33.

Appellant has also enclosed relevant extracts from commentaries defining the term 'depreciation' viz.,

a. "Financial Accounting – Concepts and Applications – J.R. Monga, Reader in Commerce"

b. "Financial Accounting – Foundation Course Study Material – The Institute of Company Secretaries of India."

20. In reply to above contentions, the Tamil Nadu Electricity Board – Respondent – 12 have submitted the following:

I. Central Commission has considered the accounting standard 6 of the Institute of Chartered Accountants in its right perspective and has held that according to para 3.4 of Accounting Standard 6 the depreciable amount of an asset is its historical cost (or) other amount substituted historical cost in the financial statements less the estimated residual value;

II. As per Para 4 of Institute of Charted Accountants of India's Accounting Standard 6, depreciation has a significant effect in determining and presenting the financial position and results of operation of an enterprise and is charged in each accounting period by reference to the extent of the depreciable amount irrespective of an increase in the market value of the assets;

III. Accounting Standard 12 lays down that:

" Government grants related to specific fixed assets should be presented in the balance sheet by showing the grant as a deduction from the gross value of the assets concerned in arriving at their book value. Where the grant related to a specific fixed asset equals the whole, or virtually the whole, of the cost of the assets, the asset should be shown in the balance sheet at a nominal value. Alternatively, government grant related to depreciable fixed assets may be treated as deferred income which should be recognized in the profit and loss statement on a systematic and rational basis over the useful life of the asset, i.e. such grant should be allocated to income over the periods and in the proportion in which depreciation on those assets is charges."

IV. While referring to Accounting Standard 12 (reproduced above), the Central Commission has rightly pointed out

in para 34 of impugned order that there are two methods of presentation in financial statement of grants related to specific assets, which are:-

"(i) *The grant is shown as deduction from the gross value of the assets concerned in arriving at its book value. The grant is thus recognized in the profit and low statement over the useful life of a depreciable asset by way of a reduced depreciation charge. Where the grant equals the whole virtually the whole of the cost of the asset, the asset is shown in the Balance sheet at a nominal value.*

(ii) *Grant related to depreciable assets are treated as deferred income, which is recognized in the profit and loss statement in a systematic and rational basis over the useful life of the asset. Such allocation to income is usually made over the*

periods and in the proportions in which depreciation on related assets is charged.”

The Central Commission has allowed the tariff in accordance with the first alternative,

Further, in case the Appellant herein is said to be entitled to depreciation on the ODA grant, under the second alternative, the amount equal to the depreciation on the specific assets related to grant has to be shown as income in the respective year in the profit and loss account and would be deductible from the tariff.

V. Central Commission, in the impugned order dated 31.03.2003, has categorically held that even for the sake of argument it is presumed that the depreciation is the replacement cost of the assets but still the end result would not be different.

VI. If appellant permitted to recover Rs. 321,55 crores or equivalent to ODA grant afresh as an element of depreciation through tariff, it would mean double recovery and result in unjust enrichment at the cost of user transmission system (Or) the ultimate consumer and hence did not allow ODA grant to be recovered afresh through depreciation.

21. Learned Counsel for Tamil Nadu Electricity Board (R-12) has reiterated the above arguments in his written submission contending that if the depreciation is allowed on ODA grant, Appellant would become richer by an amount equal to ODA grant of Rs 321.55 crores.

22. Learned Counsel for MP Electricity Board (R-2) would submit the following:

I. An asset is made of two components i.e. Debt and Equity, which shall form the cost of assets. A tariff is fixed taking into account both the components. A grant may be part of the expenditure for acquiring an asset but the same is neither the part of equity or debt and therefore cannot become part of cost for depreciation, which would be part of tariff to be recovered from the consumer. ODA grant does not qualify for inclusion in 'actual capital expenditure" for the purpose of computation of depreciation and O&M expenses in tariff.

II. As per Accounting Standard 12 issued by the Institute of Chartered Accountants of India, grant – in aid is to be deduced from the gross value of the assets in arriving at its book value which is in line with the provisions of the Explanation – 10 to section 43 (1) of the Income Tax Act which provides for treatment of grants for working out the actual cost and is reproduced below:

"Explanation 10 – Where a portion of the cost of an asset required by the assessee has been made directly or indirectly by the Central or State Government or any authority shall be under law, or by any other provision, in the form of subsidy or grant or reimbursement (by whatever name called) then, so much of the cost as is related into such subsidy or grant or reimbursement shall not be included in the actual cost of the asset to the assessee. If the assessee receiving inextricably linked with the process of setting up its plant and machinery, such receipts will go to reduce the cost of its assets."

III. The tariff is to be calculated based on the actual cost of asset to the appellant. If the entire asset is coming to the licensee as donation, can the licensee still claim depreciation or the cost of asset to be computed for the purposes of tariff determination.

IV. If the grant is allowed to be included in the total cost for the purpose of depreciation, it will result into unjust enrichment to the appellant and avoidable, shocking and unnecessary rise in the tariff for the consumer, against the sprit of the Electricity Act and the Electricity Policy.

V. Respondent -2 in its written submission has also reproduced definition of term ‘depreciation’ as per Accounting Standard 6 the Charted Accounts of India in support of his argument that historical cost of the asset is to be taken in to account for the purpose of depreciation. Respondent -1 has relied on judgment of Hon’ble Supreme Court in Commissioner of Income Tax, U.P. Vs. Nainital Bank Ltd. (1976) 1 SCR 349 where in Hon’ble Supreme Court has held that normal meaning of the expression “expenditure” denotes

"spending" or "paying out or away" i.e. something that goes out of the coffers of the assesse.

23. We have heard the Learned Counsel for the parties and carefully considered the submissions made by the rival parties. In view of the rival contentions referred to above urged by the learned counsel for parties, following questions would arise for consideration:

I. Whether depreciation is meant for repayment of loan or it is for replacement of asset.

II. Whether ' *Ratio decidendi'* of various cases relied upon by the rival parties is applicable to the present case?

III. Whether the ODA grant of Rs 321.55 Crores which is admitted as a part of capital expenditure can be excluded while determining the depreciation admissible to the Appellant for the entire capital asset?

24. We shall now deal with each question one by one.

25. First question for our consideration is relating to the purpose and usage of depreciation in Indian Power Sector. Whether it is meant for repayment of loan or it is meant for replacement of asset after expiry of its useful life? For this purpose we shall examine the definition of depreciation as enunciated by various Authorities.

26. The definitions of depreciation published by different authorities submitted by Appellant in pleadings before Central Commission are as under:

> ***"Mandatory Accounting Standard 6:*** *"Depreciation is allocated so as to charge a fair proportion of the depreciable amount in each accounting period during the useful life of the asset. Depreciable includes amortization of asset whose useful life is predetermined".*
>
> ***International Accounting Standard 4****: The term depreciation has been defined as "allocation of the depreciable amount of an asset over its estimated*

useful life. Depreciation for the accounting period is charged to income either directly or indirectly".

According to the Committee on Terminology of the American Institute of Certified Public Accountants *"Depreciation accounting is a system of accounting which aims to distribute the cost or other basic value of tangible capital assets, less salvage (if any), over the estimated useful life of the unit (which may be a group of assets) in a systematic and rational manner. It is a process of allocation not of valuation.*

Australian Accounting Standard 4 *"Depreciation of Non-Current Assets issued by the institute of Chartered Accountants in Australia and the Australian Society, states: "Depreciation charge means a systematic charge against revenue made for the purpose of allocating the depreciable amount of a depreciable asset over its useful life".*

National Association of Regulatory Utility Commission *has clarified that the "Depreciation is a process of cost allocation and not of valuation whose primary objective is to allocate in a systematic and rational manner, the cost of utility property to the period during which the property is used in utility operation".*

*According to **Shri Kamal Gupta**, a well known-authority in the field of accounting and auditing has described depreciation as "the amount set aside by the company for replacement of its assets".*

*As per the definition of depreciation by **M/s. Sukla & Grewal** renowned author under the head "The need for and objective of providing depreciation" inter alia mentioned that it is necessary to provide for depreciation for retaining enough funds for replacement of the assets at the end of commercial life."*

27. On a perusal of the above definitions, it is clear that there is an almost unanimity of opinion on the nature of depreciation, the differences are more semantic than conceptual. In short the term Depreciation can be viewed as signifying the process by which the difference between the cost of a depreciable asset (or some other appropriate measure of its value) and its estimated residual value is written-off in a systematic and rational manner over the useful life of the asset by means of periodic charge against revenue.

28. Depreciation is defined as the measure of wearing out, consumption or other reduction in the useful economic life of an asset, whether arising from use, passage of time or obsolescence through technological or market changes. Depreciation accounting is the recovery of the original cost of assets and not the economic, market or any other non-original cost measures of value. The original cost of assets can be taken as its *historic cost*, which represents the amount of cash or cash equivalents paid or the fair value of the consideration given to acquire them at the time of their acquisition.

29. Generally the cost of asset is allocated, as depreciation expense, during the useful life of the asset. Depreciation is however a non-cash expense as the expense is not actually incurred. Such expense is recognized by businesses for financial reporting and tax purposes. Rate of depreciation varies for different assets classes

depending of useful life of the assets and method of depreciation utilized. Methods may be specified in accounting and/or tax rules in a country. Several standard methods of computing depreciation expense may be used, including fixed percentage, straight line, and declining balance methods. Depreciation expense generally begins when the asset is placed in service.

30. However, under the regulatory framework, only regulated returns are allowed to the utility. Appropriate Commission is expected to determine the Annual Revenue Requirement (ARR) and tariffs for the regulated utility in such a manner so as to allow it to recover all its legitimate & genuine costs that are assignable to the business. This would ensure that the utility has sufficient funds at any point of time to meet its liabilities. Thus interest for meeting the interest payment liability of the utility on the loan raised is allowed.

31. Similarly Return on Equity (RoE) for providing Equity for creating an asset is also allowed. However, no allowance is made for repayment of principle amount of loan. Depreciation is thus linked to principle repayment liability of the utility. Since the life span of asset created (in power sector generally 25 years or more) is higher than term of loan raised to create the asset (around 10 years), the depreciation allowed on straight line method would be less than principle loan repayment liability of the utility. So as to allow the utility to have sufficient funds to repay its interest and principle repayment liability, the concept of Advance Against Depreciation (AAD) had been introduced by various Electricity Regulatory Commissions in the country. Under this concept in addition to allowable depreciation, the distribution licensee is allowed to claim an advance against depreciation (AAD).

32. In this regard it would be pertinent to mention that Central Commission and some of the State Commissions have notified new Tariff Regulations. Under these Regulations, in line with Tariff Policy, the provision of advance against depreciation has been done away with and rates for depreciation have been reworked in such a manner so as to take care of repayment of debt obligations. In other words higher rate of depreciation have been provided for first 10 years to take care the loan repayment liability. After initial period of 10 years, remaining depreciation would be spread over the balance useful life to keep the tariff reasonable.

33. Thus in practice, depreciation is utilized to meet loan repayment liability of the utility arisen out of creation of an asset. When such an asset is required to be replaced after expiry of its useful life, fresh financial arrangements are made. POWERGRID, the Appellant, in its pleadings

before the Central Commission has also accepted that it is utilizing depreciation amount to meet loan repayment liability. The statement made by Appellant on para ‘P’ on page 12 of the petition is as under:

> *“POWERGRID utilized the depreciation component for servicing the debts as the amount of cash generation through operation is not sufficient to meet the debt servicing obligation because of poor revenue realization from SEB’s. This does not mean that POWERGRID shall be deprived of depreciation as an element of tariff, as depreciation is a recognized cost element and has nothing to do with repayment of loan.”*

34. In the light of above discussions it is clear that as per definition, depreciation is replacement cost of an asset but in practice it is utilized for repayment of loan.

35. Now we will examine *the ratio decidendi* of various cases relied upon by the rival parties and their applicability in the present case.

36. Appellant and Respondents have relied upon following decisions:

    i. 'Commissioner of Income Tax v Tata Iron and Steel Company Ltd (1998) 2 SCC 366',

    ii. 'Challapalli Sugar Ltd v The Commissioner of Income Tax A,P, Hydrabad (1975) 3 SCC 572,

    iii. 'Commissioner of Income Tax v Nainital Bank Ltd (1966)1 SCR 349.

37. On perusal of cases cited above we are of the view that the ratio of these cases would not apply to the present case on two counts. (i) These cases decide the term 'capital cost or capital expenditure' which is not in question in the present case before us. (ii) All these cases are related to income tax and scope of explanation 10 of

Section 43 of Income Tax Act. Hon'ble Supreme Court in the case of 'Ahmedabad Miscellaneous Industrial Workers Union v Ahemdabad Electricity Co. Ltd AIR 1962 SC 1255 has held that:

> *"in the context of Electricity Supply Act, depreciation enables the utility to work out the charges to be recovered from consumers for supply of electricity, one has to follow the provisions of the Electricity Supply Act and **that one has not to follow the provisions of Income Tax Act."** {emphasis added}*

38. Appellant has also relied heavily on the judgment of Hon'ble Supreme Court in the case of Delhi Electricity Regulatory Commission v BSES Yamuna Power Ltd and others, (2007) 3 SCC 377. In this case Delhi State Commission has reduced rate of depreciation from 6.69% to 3.75 % on the ground that licensee has no loan repayment liability during that year and thus not entitled for accelerated rate of depreciation as specified in

Government of India's 1997 notification. On this issue Hon'ble Supreme Court held that Delhi State Commission was bound to follow provisions of Sixth Schedule of Electricity Supply Act 1948 and ought to have allowed depreciation at rate specified in 1997 notification. The issue of depreciation on grant was not before the Hon'ble Supreme Court in this case.

39. Next question for our consideration is Whether the ODA grant of Rs 321.55 Crores which has been admitted as a part of capital expenditure by Central Commission can be excluded while determining the depreciation admissible to the Appellant for the entire capital asset.

40. In this regard let us refer to the findings of the Central Commission in the impugned order. Relevant portion of the impugned order is as given below:

"33. The parties have also referred to the Accounting Standard 12 of the Institute of Chartered Accountants of India, which lays down the procedure for treatment of Government grants in the accounts. Government grants are assistance by Government in cash or kind to an enterprise for past or future compliance with certain conditions. They exclude those forms of government assistance which cannot reasonably have a value placed upon them and transactions with government which cannot be distinguished from the normal trading transactions of the enterprise. Accounting Standard 12 provides the following method for accounting of Government grants in the financial statements:

"Government grants related to specific fixed assets should be presented in the balance sheet by showing the grant as a deduction from the gross value of the

assets concerned in arriving at their book value. Where the grant related to a specific fixed asset equals the whole, or virtually the whole, of the cost of the asset, the asset should be shown in the balance sheet at a nominal value. Alternatively, government grant related to depreciable fixed assets may be treated as deferred income which should be recognised in the profit and loss statement on a systematic and rational basis over the useful life of the asset, i.e. such grant should be allocated to income over the periods and in the proportion in which depreciation of on those assets is charged."

34. From the above, it is observed that there can be two alternative methods of presentation in financial statements of grants related to specific assets, which are:

(i) The grant is shown as a deduction from the gross value of the asset concerned in arriving at its book value. The grant is thus recognised in the Profit &

Loss statement over the useful life of a depreciable asset by way of a reduced depreciation charge. Where the Grant equals the whole or virtually the whole of the cost of the asset, the asset is shown in the Balance sheet at a nominal value.

(ii) Grant related to depreciable assets are treated as deferred income, which is recognized in the profit and loss statement on a systematic and rational basis over the useful life of the asset. Such allocation to income is usually made over the periods and in the proportions in which depreciation on related assets is charged.

35. The Commission in its order dated 20.8.2002 had allowed the tariff in accordance with the first alternative. However, it may be observed that although treatment of grant for the purpose of depreciation is different in both the alternatives but the net impact on tariff on account of depreciation is same. Under first alternative, the gross block is

reduced by the amount of grant and the depreciation is provided on reduced gross block. Under second alternative, depreciation is provided on the total gross block but the amount equal to the depreciation on the specific assets related to grant is shown as income in the respective year in the Profit and Loss Account and would be deductible from the tariff."

41. The grants received by POWERGRID, the Appellant from Central Government or other authorities towards capital expenditure for Projects and betterment of transmission systems are to be first shown under as Capital Reserves under Reserves and Surplus till the utilization of grant which may be for creation of an asset. After the assets are capitalised there can be two treatment of the grant identifiable to the asset as per the Accounting Standards issued by the Chartered Accountants of India.

1. The Government grants related to specific fixed assets is reduced from the gross value of the assets concerned in arriving at the book value. Where the grant related to a specific fixed asset is equal to the complete or virtually the complete cost of the asset, the asset can be shown in the balance sheet at a nominal value. This implies that no depreciation would be allowed on the grant used to finance the asset. This methodology is adopted by most of Regulatory Commissions in their Tariff Regulations. Depreciation on asset financed through grants is not allowed by them.

2. Alternatively, government grants related to depreciable fixed assets may be treated as deferred income which is recognised in the profit and loss statement on a systematic and rational basis over the useful life of the asset, i.e., such grants should be allocated to income over the periods and in the proportions in which

depreciation on those assets is charged. Grants related to non-depreciable assets should be credited to capital reserve under this method.

42. Thus, under 2nd alternative, the grant is considered as deferred income amortized over the life of the asset. Every year till the useful life of the asset a sum equal to the amount of depreciation on the grant utilized for financing the asset is taken as income and the value of grant is reduced by this income amount. This will continue till the useful life of the asset.

43. Both the alternatives are almost similar, basically it is a method of presentation of grants in the accounts. In the first alternative depreciation is not allowed on that portion of asset financed through grants and in the second alternative, an amount equal to the depreciation on grant is considered as income, meaning thereby that an expense is recognised by way of depreciation on asset

financed by grant which is offset by the income equal to the amount of depreciation on grant portion.

44. The Appellant had also reiterated same in its written submission before the Central Commission in review petition number 145/2002 in petition no 46/2000 as under:

> *"In response to the direction of Hon'ble Commission at Sl. No. 2 (b) above, i.e. Accounting of grant in aid, following is submitted :*
>
> *The Company is following the policy No. 1.0 on grant in aid which is reproduced below:*
>
> *"Grants-in-aid received from Central Government or other authorities towards capital expenditure for Projects and betterment of transmission systems are shown as grants-in-aid under 'Reserves and Surplus' till the utilization of grant. However, grants received for specific depreciable assets are shown under 'Reserves and Surplus' while the assets are under construction. On capitalization of assets, such grants-in-aid are treated as deferred income and recognized in the Profit and Loss*

Account over the period and in the proportion in which depreciation on these assets is provided".

This policy is as per para 14 of the mandatory accounting standard 12 issued by the Institute of Chartered Accountants of India. The relevant extracts of para 14 is as given below:

"Government grants related to specific fixed assets should be presented in the balance sheet by showing the grant as a deduction from the gross value of the assets concerned in arriving at their book value. Where the grant related to a specific fixed asset equals the whole or virtually the whole of the cost of the asset, the asset should be shown in the balance sheet at a nominal value. Alternatively government grants related to depreciable fixed assets may be treated as deferred income which should be recognized in the profit and loss statement on a systematic and rational basis over the useful life of the asset i.e. such grants should be allocated to income over

the periods and in the proportions in which depreciation on those assets is charged".

As may be seen the standard provides both the methods of accounting of grant. The alternative method adopted by the corporation is normally followed by most of the companies as the gross value of the asset is determined and the O & M cost on the gross value of the asset is reflected in the accounts. ***It is also to mention here that the profitability remains the same under both the methods****. {emphasis added}*

45. Having accepted that appellant's profitability would remain same under both alternatives described above by POWERGRID, the Appellant, it is evident that there is a clear convergence of views of Appellant and Respondents on this issue. The difference is only in the method of presentation of grants in accounts. TNEB (R-12) have also reflected the same views in its written submission. The concerns of other respondents are restricted to tariff

neutrality which admittedly would remain unaffected by adoption of any of the two alternatives.

46. To sum up Accounting Standard 12 of Institute of Charted Accountants of India permits two methods of presentation of grants in accounts as explained in para 41 above. Whereas Central Commission (R-1) has adopted 1st alternative in the impugned order, Appellant adopts 2nd alternative in its accounting policy. Both Appellant as well as Respondent has acknowledged that net impact of both methods would be same. We feel that having obtained the information about accounting policy of Appellant, Central Commission could have also adopted 2nd method in the impugned order, more so since it would not have any impact on transmission tariff. On other hand Appellant could have accepted the impugned order as it was not going to affect his profitability.

47. Summary of our findings.

I. To issue no 1: Whether depreciation is meant for repayment of loan or it is for replacement of asset?

Our answer is: In the light of above discussions it is clear that as per definition depreciation is replacement cost of an asset but in practice it is utilized for repayment of loan taken for creation of that asset.

II. To issue no. 2: Whether '*Ratio decidendi'* of various cases relied upon by the rival parties is applicable in the present case?

Our answer is : Ratios of various case referred to by rival parties are not applicable to the present case.

III. To issue no 3: Whether the ODA grant of Rs 321.55 Crores which is admitted as a part of capital expenditure can be excluded while determining the depreciation admissible to the Appellant for the entire capital asset?

Our Answer is: Accounting Standard 12 of Institute of Charted Accountants of India permits two alternative methods of presentation of grants in accounts. Whereas Central Commission (R-1) has adopted 1st method in the impugned order, Appellant adopts 2nd method in its accounting policy. Both Appellant as well as Respondent have admitted that net impact of both methods would be the same. We feel that having obtained the specific information about accounting policy of Appellant, Central Commission could have also adopted 2nd method in the impugned order, more so since it would not have any impact on transmission tariff. On other hand POWERGRID,

the Appellant could have accepted the impugned order as it is since it was not going to affect his profitability.

48. In view of our above findings, we do not find any ground to interfere with the impugned order of Central Commission dated 20.08.2002. Hence, Appeal being devoid of merit is dismissed. However, there is no order as to cost.

49. Pronounced in the open court today the 7th April 2011.

(V J Talwar)
Technical Member

(Justice M Karpaga Vinayagam)
Chairperson

INDEX : REPORTABLE/NON-REPORTABLE

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