3~~2~~

GVK

MIAL/EVPF/17-18/01

10th July, 2017

The Secretary,
Airports Economic Regulatory Authority of India,
AERA Building, Administrative Complex,
Safdarjung Airport,
New Delhi – 110 003

Madam,

Sub: Determination of Useful life of Airport Assets

Ref: Consultation Paper No. 9/2017-18 dated 19th June, 2017 ("Consultation Paper/CP")

At the outset, we thank the Authority for giving us an opportunity for providing comments on the Consultation Paper issued by the Authority on determination of useful life of airport assets.

Schedule II of the Companies Act, 2013, which prescribes the useful life of the assets, came into effect from financial year commencing April 1, 2014. Schedule II of the Companies Act, 2013 corresponds to Schedule XIV of the erstwhile Companies Act, 1956. Ministry of Corporate Affairs has further amended Schedule II (Useful lives to compute depreciation) of the Companies Act, 2013 by issuing notification dated August 29, 2014.

The Authority has, while finalizing its proposals on useful life of airport assets, mainly relied on the 'Report on Study of Useful Life and Depreciation rates for Airport Assets' by the 'Corporate Law & Corporate Governance Committee' of the Institute of Chartered Accountants of India (ICAI), which was attached as Annexure II to the Consultation Paper issued by the Authority.

Before we provide specific comments on each of the proposal, we would like to highlight the fact that airport development projects are highly capital intensive in nature and continuously require capital for upgradation of the facilities and infrastructure. Therefore it is essential that airports are able to generate adequate cash flows to meet increasing requirement of capital for investment. If cash flows are not adequate, airports will have to borrow more funds for which higher charges will have to be recovered from the users. It may be noted that NPV of cash flows to an airport operator, over the useful life of an asset, remains same irrespective of rate of depreciation and therefore it will be very important for the Authority to strike right balance between the need for adequate cash flows for debt servicing and investment needs vis-à-vis user charges so that airports are able to service its debt and meet funding requirement for investments.

Mumbai International Airport Pvt Ltd
Chhatrapati Shivaji International Airport
1st Floor, Terminal 1B, Santacruz (E), Mumbai 400 099, India
T +91 22 6685 0900 / 6685 0901 F +91 22 6685 2059
www.csia.in
CIN : U45200MH2006PTC160164

ENERGY
RESOURCES
AIRPORTS
TRANSPORTATION
HOSPITALITY
LIFE SCIENCES

Our specific comments on the Consultation Paper are as under:

1. **Proposal No. 1 (a) – To determine useful lives for key Airport Assets under Part B of Schedule II to Companies Act as stated in Part – I of Annexure -5 of the CP**

   a) Terminal Building including VIP terminal and other buildings (Item No. 2 to 7 of the Part I of Annexure 5)– Useful life of 30/60 years mentioned by the Authority does not take into account the following:

      i) **Concession Period of the concerned Airport under respective Concession Agreement** - Authority should take into account only primary concession period of the concerned airport while determining useful life of assets for that particular airport since useful life cannot be more than economic life. Economic life for any airport under concession cannot be more than its primary concession period.

      We draw attention of the Authority to para 1 of Part A of Schedule II of the Companies Act, which specifically mentions that useful life of an asset is the ***period over which an asset is expected to be available for use by an entity***, or the number of production or similar units expected to be obtained from the asset by an entity. Since any asset cannot be available to the airport operator for use beyond its concession period, it is necessary that useful life is capped with the period available under primary concession period.

      Please also refer to Table 4.5 of ICAO Airports Economic Manual (2013 edition) of Annexure 3 of Consultation Paper which clearly mentions that **depreciation for leasehold buildings is to be provided over the period of the lease.**

      We also draw your attention to the requirements under Ind AS 16 and 17 **which requires provision of depreciation over lease term**, relevant extract of which is attached as Appendix 1 for your ready reference.

      ii) **Component accounting as required under Companies Act, 2013** - We draw attention of the Authority to the Schedule II of Companies Act which requires that where cost of a part of the asset is significant to total cost of the asset and useful life of that part is different from the useful life of the remaining asset, GVK

useful life of that significant part shall be determined separately (refer note 4 to the Schedule II).

In the case of airport terminal building there are various items such as Glass works and facades, canopies, wall and column cladding, planters and landscaping etc. which have useful lives (5 to 15 years) significantly different from civil works (30 years) and hence Authority should either provide different useful lives for such components or flexibility to decide on a case to case basis while determining aeronautical tariffs.

MIAL has already complied with this statutory requirement and accordingly provided depreciation in its books of accounts at different rates for different components as mentioned above.

Authority should also provide specifically that useful life being proposed for this category is only for the civil works related to these buildings. We wish to draw your attention to the para 7.3.2 of ICAI Report where in it has referred to Civil Works only of the Terminal Building under this category and has not referred to other components of the Terminal Building.

b) Baggage handling system / Escalators / Elevators / Travelators / HVAC equipment / Gen-set / Power equipment / Cargo ASRS / ETV equipment (Item No. 10), X-ray machine / RT Set / DFMD/HHMD/Security Equipment etc. (Item No. 11) and eargo equipment / dollies /PPT etc. (Item No. 14) and CFT ((Item No. 20) – Authority has mentioned in the remark column "As per Companies Act" but it has not taken into account the following provisions of the Schedule II of the Companies Act, 2013:

i) **Schedule II has two distinct categories as Plant & Machinery (Item No. IV) and Electrical Installations and Equipment (Item No. XIV)** – Schedule II provides a useful life of 15 years for general category of Plant and Machinery with a provision for extra shift depreciation while for Electrical Installations and Equipment it provides a useful life of 10 years.

Authority has clubbed items like Generators and Power Equipments etc. (such as transformers, sub-stations, HT and LT Panels, switch gears and distribution system etc.), whieh are part of Electrical Installations and Equipments, with other items of Plant & Machinery. Since there is a specific category for Electrical Installations and Equipment these items should not be clubbed with general category of Plant and Machinery.

Mumbai International Airport Pvt Ltd
Chhatrapati Shivaji International Airport
1st Floor, Terminal 1B, Santacruz (E), Mumbai 400 099, India
T +91 22 6685 0900 / 6685 0901 F +91 22 6685 2059
www.csia.in
CIN: U45200MH2006PTC160164

We therefore request the Authority to move items such as Generators and Power Equipment etc. (such as transformers, sub-stations, HT and LT panels, switch gears and distribution system etc.) from general category of Plant & Machinery to Electrical Fittings (Item No. 17) and change the nomenclature of Item No. 17 to Electrical Installations and Equipments in line with the Schedule II of the Companies Act, 2013.

ii) Note 6 to the Schedule II provides for **extra shift depreciation for all items of Plant & Machinery,** other than continuous process plant, covered under (IV)(i)(a) of the Schedule depending upon whether asset is used for double or triple shift. We request Authority to provide for extra shift depreciation, as prescribed under the Companies Act, for the airports which are required to be operated on 24*7 basis for 365 days in a year.

It may be pertinent to note that MIAL has already provided depreciation in its books of account as detailed above under point (i) and (ii) and on the sane basis tariff for 2[nd] control period were determined by the Authority.

c) Computer / Servers – Schedule II has two distinct categories i.e. Server, Networks and End user devises such as desktop, laptops etc. with different useful lives. Authority has however combined both Computer and Servers with same useful life of 6 years. Further Authority has separately provided useful life of 5 years for intangible assets such as software which is specifically not mentioned in the Schedule II and therefore was being amortised over 6 years, on the lines of Servers and Networks.

We request the Authority to provide useful life for End user devises such as desktops, laptops etc. as 3 years in accordance with the Schedule II instead of clubbing the same with the Server and Networks considering the fact that useful life of these devises are much shorter due to higher obsolescence vis-à-vis servers and networks.

2. **Proposal No. 1(b) – To determine useful lives for key Airport Assets (not stated under Part B of Schedule II of Companies Act) as stated in Part – II of Annexure -5**

Runway, Taxiway and Aprons - Authority in Part II of Annexure 5 has suggested useful life of 30 years for Runway, Taxiway and Aprons. MIAL has considered useful life of 20 years for Runways due to the following reasons:

a) MIAL assumed operations and development of CSIA from 3rd May 2006 and took control of AAI's existing assets including Runways. Since Runways were originally constructed by AAI and MIAL has only done the strengthening and substantial restoration works of these runways, it has considered useful life of 20 years.

b) Besides above, various reports and data relied upon by ICAI as mentioned below, also justify useful life of Runways (even new Runways) as 20 years only instead of 30 years proposed by the Authority since Runways are considered as Flexible Pavements against Apron which are considered as Rigid Pavements (concrete):

i. ICAO Airports Economic Manual (2013 edition) has suggested useful life of Runways and Taxiways in the range of 15-30 years.
ii. UK government – CAA in "A guide to Airfield Pavement design and evaluation – Design and Maintenance Guide (February 2011)" recommends that structural design life be 20-30 years. The upper end of this range being for concrete pavements and the lower end for flexible pavements.
iii. US Department of Federal Aviation Administration in its Advisory circular AC No. 150/53206E has stated that Pavement and other facilities built to FAA standards are designed to last at least 20 years.
iv. FAA Airport Compliance Manual – Order 5190 B – 2009 also states that Pavement and other facilities built to FAA standard are designed to last at least 20 years.
v. Aerodrome Design Manual Part 3 (2003 edition) states that pavement designed in accordance to these standards are intended to provide a structural life of 20 years.
vi. Concession Agreement of BIAL also states that design life of flexible pavement is 20 years.
vii. ICAI itself in para 6.2.18 of its Report mentioned that useful life of 20 years can be considered for Flexible Pavements (Runway and Taxiway) and 30 years for Rigid Pavements (Apron)
viii. Authority has also mentioned in para 2.2.5 (B) (i) that in view of the international prescriptions on standards of design life, the practice followed by certain airports in Asia and other parts of the world, useful life of 10-15 years for Runways and Taxiways surfaces and 30 years for Runways and Taxiways bases can be prescribed which means Authority should provide useful life for Runways and Taxiways either as average of 10 to 30 years or provide different useful lives for bases and surfaces but providing useful life of 30 years for both i.e. bases and surfaces would be incorrect and inappropriate.

Mumbai International Airport Pvt Ltd
Chhatrapati Shivaji International Airport
1st Floor, Terminal 1B, Santacruz (E), Mumbai 400 099, India
T +91 22 6685 0900 / 6685 0901 F +91 22 6685 2059
www.csia.in
CIN : U45200MH2006PTC160164

3. **Effective date of Authority's order**

Authority has proposed to make the order effective 1st April 2016. However, it may be noted that it will not be possible to implement Authority's order retrospectively for FY 16-17 as accounts for that year have already been duly audited and signed. Further as per part B of Schedule II, useful life or residual value of any specific asset, as notified for accounting purposes by a Regulatory Authority ***shall be*** applied in calculating the depreciation to be provided irrespective of the requirement of the Schedule II, henee we requests the Authority to implement the order from FY 19-20 only since Authority has already determined tariffs for MIAL for 2nd Control Period up to FY 19.

Thanking you,

For Mumbai International Airport Private Limited

Vinod Hiran
Executive Vice President- Finance

Encl.: As above

Appendix 1

A) Ind AS – 16 "Property Plant and Equipment" states that useful life of an asset can be shorter than its economic life. The depreciation method used shall reflect the pattern in which the asset's future economic benefits are expected to be consumed by the entity.

Extract of paras pertaining to depreciation under Ind AS – 16 "Property, Plant and Equipment" is as below:

"Depreciable amount and depreciation period

50. The depreciable amount of an asset shall be allocated on a systematic basis over its useful life.

56. The future economic benefits embodied in an asset are consumed by an entity principally through its use. However, other factors, such as technical or commercial obsolescence and wear and tear while an asset remains idle, often result in the diminution of the economic benefits that might have been obtained from the asset. Consequently, all the following factors are considered in determining the useful life of an asset:

(a) expected usage of the asset. Usage is assessed by reference to the asset's expected capacity or physical output.
(b) expected physical wear and tear, which depends on operational factors such as the number of shifts for which the asset is to be used and the repair and maintenance programme, and the care and maintenance of the asset while idle.
(c) technical or commercial obsolescence arising from changes or improvements in production, or from a change in the market demand for the product or service output of the asset.
(d) legal or similar limits on the use of the asset, such as the expiry dates of related leases.

57. The useful life of an asset is defined in terms of the asset's expected utility to the entity. The asset management policy of the entity may involve the disposal of assets after a specified time or after consumption of a specified proportion of the future economic benefits embodied in the asset. ***Therefore, the useful life of an asset may be shorter than its economic life. The estimation of the useful life of the asset is a matter of judgment based on the experience of the entity with similar assets."***

B) Provisions pertaining to depreciation in Ind AS-17 on "Leases", also relevant for this purposes are reproduced below:

> *"27. A finance lease gives rise to depreciation expense for depreciable assets as well as finance expense for each accounting period. The depreciation policy for depreciable leased assets shall be consistent with that for depreciable assets that are owned, and the depreciation recognised shall be calculated in accordance with Ind AS 16 Property, Plant and Equipment and Ind AS 38 Intangible Assets. If there is no reasonable certainty that the lessee will obtain ownership by the end of the lease term, the asset shall be fully depreciated over the shorter of the lease term and its useful life."*