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DELHI INDIRA GANDHI INTERNATIONAL AIRPORT

Delhi International Airport (P)Limited

633 16/5/11

GMR

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DIAL/2011-12/Fin-Acc/286

16/5

Mr. Sandeep Prakash

Secretary,

Airports Economic Regulatory Authority of India

Administrative Complex

Safdarjang Airport

New Delhi – 110 003

Dated: May 13, 2011

AGM (AOS)

May pls Consolidate

16/5/11

Recd. at 7.20PM 13.5.11

Sub: Submission of response on Consultation paper No.2/2011-12: Review and levy of Development Fee at IGI Airport.

Dear Sir,

This is in reference to the above Consultation paper issued by Airport Economic Regulatory Authority "AERA" on 21st April 2011.

We thank the Authority for the efforts taken to review the request of Delhi International Airport Ltd. (DIAL) for approving the additional ADF to meet the financing gap of the project to modernize, upgrade and expand the Delhi Airport.

Our response to the consultation paper is submitted herewith. Please let us know if you need any further information or clarifications. The Authority is requested to expeditiously approve the ADF after favorably considering our response.

Yours Sincerely,

For Delhi International Airport Private Limited

Sidharath Kapur

(Chief Financial Officer-Airports)

CC: MINISTRY OF CIVIL AVIATION,

Delhi International Airport Private Limited

Response to
Consultation Paper No 2/2011-12
On

Review of Levy of Development Fee
IGI Airport
New Delhi

Contents

I. INTRODUCTION

The Airport Economic Regulatory Authority of India 'Authority' has come out with a consultation paper on Review of Levy of Development Fee –IGI Airport, New Delhi.

We thank the Authority for the efforts taken to review the request of Delhi International Airport Ltd. (DIAL) for approving the additional ADF to meet the financing gap of the project to modernize, upgrade and expand the Delhi Airport. We welcome the steps taken by the Authority to invite comments and suggestion on the draft guidelines and present our comments in the following sections. We request the Authority to favourably consider our submissions in finalizing the ADF.

II. DISALLOWANCES

The consultation paper has proposed disallowances of Rs. 96.99 crores on account of the following 3 items:

1. **Additional apron Area:** On the basis of benchmarked costs suggested by EIL, disallowance of Rs. 23.82 crores has been proposed.
2. **Runway rehabilitation:** On the basis of benchmarked costs suggested by EIL, disallowance of Rs. 20 crores has been proposed. KPMG in its observation has said that as per Accounting Standard 10, only expenditure that increases the future benefits from the existing assets beyond its previously assessed standard of performance is included in the gross book value. Accordingly KPMG have suggested that Rs.17.5 crore be excluded from capitalization (and be included as an operating expenditure). The above add up to a disallowance proposed of Rs. 37.5 Crores.
3. **Escalation for Reinforcements:** EIL have suggested that the impact of price increase may be restricted to Rs. 174.33 crores as against Rs. 210 crores claimed by DIAL. The above ends up in a disallowance of Rs. 35.67 Crores.

In our opinion it would not be appropriate to disallow these expenses and the rationale for the same is provided as under:

1. **Additional Apron Area:** The basis for the cost calculation provided by DIAL for the increase in apron costs is the actual costs as per the packages awarded for these works. On a project of this nature and executed within critical timelines, bench marked costs from other unrelated projects should not be taken as the basis for evaluation of costs that had to be incurred.

   DIAL therefore requests a reconsideration of the position taken in this regard.

2. **Rehabilitation of Runway 10-28:**
   a. **Disallowance of Rs.20 Crore:** The basis for the cost calculation provided by DIAL is the actual costs competitively determined as per the packages awarded. These works are being executed in a busy operational airport area wherein substantial additional costs are required to be incurred due to extraneous factors like limited working time, access, security issues and many other contingencies and unforeseen issues. Thus theoretical calculations made by auditors should not be considered as basis for dis-allowing project cost.

      Subject works were tendered out on an EPC basis and the following bidders participated:
      1. Larsen & Toubro Ltd
      2. Oriental Structural Engineers Pvt. Ltd
      3. NAPC Ltd
      4. Roman Tarmat Ltd

      Based on the techno commercial evaluation, NAPC was the lowest bidder for execution of the entire works on lump sum basis. Accordingly the contract was awarded to NAPC. These works are being executed in an operational airport area wherein substantial additional costs are required to be incurred due to limited working time, access, security issues etc.

Hence it is requested that no deduction be made in this regard.

b. **Disallowance of Rs.17.5 crore:** As regards to KPMG contention that an amount of Rs.17.50 crores be excluded from Capex and be allowed as operating expenditure, we agree to the above and shall be treating the same as operating expenditure in our tariff filing.

3. **Escalation for reinforcement:** The basis for the cost calculation provided by DIAL is the actual costs as per the packages awarded. The cost worked out by the auditors is based on the market rate for these works which is normally carried out through manual means with minimal mechanization. To meet the project time schedule, reinforcement steel of about 8000 MT / month was required. To achieve this required output by regular conventional (manual) process would have required large skilled labour force (scarce resource during that period due to huge development works in NCR mainly to gear up for Commonwealth games) which in turn would have required extensive coordination, for both design and fabrication. Hence the only practical solution available was to set up automated reinforcement cutting, bending plant capable of producing the required quantities to be installed on site to meet the project deadlines. Had we adopted conventional methods, it would not have been possible to complete project of this size within the Deadline.

   Based on the above, L & T had setup automated reinforcement plant to make available required quantities. For this purpose, L & T had the following major equipment, imported from Germany & Denmark:

   1. Cadormatic Main Auto Shearline RS 500 (1 Nos)
   2. Permatic N Double Bender (2 Nos)
   3. Mini shear line 60 HV (1no)
   4. Stirrup Making Machine various types (2 Nos)
   5. Single Bender – Table top bender (2 Nos)

   Further to the above, various equipment like material handling equipment, etc. had been purchased locally. A complete steel service shed also had to be erected. After thorough analysis and negotiations, the overall costs incurred by DIAL towards equipment depreciation, operation costs etc. were reasonable and competitive.

   Conclusion: The above amount has been actually spent by us and as such disallowance of this legitimate amount will adversely impact the financing of the airport.
   Keeping in view the requirement to complete the project before Commonwealth Games and given the fact that all of the above activities were carried out in the most Busiest operational Airport of the country wherein costs always are high compared to a benchmark industry average, we request that the proposed deduction of Rs. 79.49 crores should not be made to the project cost on aforesaid accounts. As regards to treatment of Rs.17.5 crores disallowed by KPMG, we would be treating the same as operating expenditure in our tariff filing.

   However in the eventuality if the Authority in their wisdom disallow the amount for DF determination, we request that the Authority may allow the above to be included as part of RAB for the purpose of Tariff determination.

III. DISCOUNTING RATE: TAX SHELTER ON DF INTEREST

The consultation paper proposes that the discount rate should be determined with reference to the rate of interest of debt securitized against the DF after netting corporate tax rate so as to account for the tax shield due to interest payment.

However there appears to be some misunderstanding of the accounting treatment of DF and we shall like to clarify as under:

The receipt and payment methodology followed by DIAL is as follows:

A. Receipts from Bridge Loans against DF have been transferred to Separate Escrow Account.
B. At the receipt of information on number of passengers travelled, a bill is raised for the DF amount on airlines.
C. Any receipts from billing of DF to Airlines are deposited into Escrow Account.
D. Interest and Principal Repayment towards DF bridge loans are paid from the above Escrow Account.

Accounting and Disclosure Methodology: We have disclosed the DF Receipts, Interest and Bridge Loans as follows:

(i) Based on the passenger information submitted by airlines, DF invoice is raised by DIAL on the airlines and the amount of invoice raised is credited to "DF Billed Account".
(ii) Interest paid towards loans is netted off from the "DF Billed Account" as explained in clause (i).
(iii) DF Billed and unbilled accrued amounts have been reduced from the gross block of fixed assets.
(iv) DF loans have been shown as Secured Loans.

We confirm that interest on DF Loan is not charged to Profit and Loss Account and the Company is not entitled for any tax shield in the interest.

We are enclosing a certificate received from DIAL statutory auditors confirming the compliance of above procedure and also confirming that the treatment being given in books is the correct accounting treatment.

Conclusion:
Thus given the fact that DF is not an item of the Profit and Loss Account and has no bearing to computation of income tax, the discounting of the DF must be done at the actual rate of interest and not on a rate derived net of tax.

IV. INFUSION OF ADDITIONAL EQUITY.

As regards the financing of the project, we reiterate our earlier submission already made to AERA as follows.

In case of DIAL, infusion of Equity is governed by the "Shareholders Agreement" dated 4th April 2006 signed amongst the shareholders of DIAL. DIAL is bound to abide by the aforesaid agreement.

As per Para 3.3.3.1, of the shareholders agreement

"The Parties hereby further acknowledge and agree that, subsequent to the initial subscription AAI (alongwith AAI nominees) shall have the right, but not the obligation, to subscribe to such number of Equity Shares in any subsequent capitalization of JVC ("Option").....

Clause no. 3.3.1 of the said agreement states as under:

".....if The Trigger Debt Equity Ratio is not maintained, the JVC shall not issue any fresh Equity Shares till such time as the Trigger Debt Equity Ratio is in place. Towards the end, the Private Participants (without diluting AAI (alongwith AAI Nominees) equity shareholding) hereby covenant and agree to infuse funds in such form and quantity as may be necessary to ensure that Trigger Debt Equity Ratio is maintained immediately prior to the time of any fresh issue of Equity Shares....."

Therefore DIAL is required to maintain a Debt to Equity ratio of at least 2:1 and it cannot raise further equity if this ratio is breached below this level. Also it cannot (without support of AAI) bring in fresh equity as this will result in dilution of the shareholding of AAI and AAI Nominees thereby contravening the Shareholders Agreement. Airports Authority of India vide its letter dated January 13th 2011 have expressed their inability to commit further equity contribution. DIAL lenders' lead by ICICI Bank have stated that any additional debt will lead to debt serviceability issues and cannot be supported.

You will appreciate that as the Trigger Debt Equity Ratio referred to in the aforesaid clauses of the Shareholders Agreement is in the context of raising further Equity Shares, the reference to Trigger Debt Equity Ratio is based on actual debt and equity raised and not quasi equity by way of deposits (which lenders may treat as quasi equity for funding purpose). Raising further debt is not possible. Even if we stretch the untenable argument that quasi-equity is equity for Shareholder Agreement purposes, DIAL would thus be already in breach of the Trigger Debt Equity norm as the debt equity ratio after considering quasi-equity will be below 2:1; thus in any case impairing DIAL ability to raise further equity shares. Further as AAI has expressed inability to contribute further equity, it will not be possible to raise further equity to dilute them.

V. TIMELINE FOR ATC TOWER

The Authority in the consultation paper have referred to the timelines for construction of ATC Tower as mentioned in AAI letter.
It is mentioned therein that

> *" AAI in their comments have stated that the ATC tower and associated facilities would be completed by November, 2012."*

At present DIAL is finalizing the tender documents for the construction of the tower. The works are to be awarded by end June 2011.The timeline of November 2012 for the construction of ATC tower is not practically possible. As per the overall schedule the ATC tower including installation / commissioning of equipment as finalized in consultation with AAI, ATC tower is to be completed by November 2013.

Conclusion: In view of above it is requested that the timeline for completion of the project be revised to November 2013.

VI. DURATION OF DF

We request AERA to review the duration of DF periodically and based on actual collection, finalize the final duration of levy of DF. AERA may Cap the amount of DF as determined herein. However for the purpose of calculation of the initial estimate of the duration of DF the following need to be given due weightage:

1. **Delay due to finalization of Rules**: AERA may need to factor delays due to procedure as may be laid down in the rules being framed by Ministry of Civil Aviation (MOCA) as regards to DF. This delay, beyond DIAL control, will involve additional interest burden and accordingly enhance the duration of DF.
2. **Discounting rate:** The duration of DF also needs to be revised based on the submission being made by us in Section III regarding rate of discounting and disallowances.
3. **Collection Charges**: The DGCA had directed DIAL to pay Rs. 5/- per DF receipt towards collection charges to airlines. A copy of the directive number 2/2009 dated 28th February 2009 is enclosed. While calculating duration of DF this should also be borne in mind.
4. **Exempt Passengers:** DGCA vide above directive has also directed us as regards to a list of exempted class of passengers. As per our estimation the chargeable passengers are 90% of the total travelling passengers which may be used for duration estimation purposes.

VII. REQUEST FOR IMMEDIATE RELIEF

We shall like to reiterate that the current DF is continuation of process of DF first approved by Ministry of Civil Aviation on February 9, 2009 and subsequently reviewed by the Authority. The finalized Project Cost was filed with AERA on March 31, 2010. As on March 31, 2010, after factoring in the security capex, the project cost had a funding gap of Rs.1793 crores which is continuing and needs to be bridged through ADF. The funding gap, pending finalization of ADF, has been temporarily bridged by raising short term loans and withholding project payments. Thus approving DF at this stage will be a pre-funding to regularize the project financing gap. Since the process of Project Cost finalization has taken more than a year, the financial position of the company is under stress; hence an immediate relief is requested.

VIII. APPENDIXES

Enclosed are the following for your kind reference:

Appendix 1: Directive number 02/2009 dated 28th February 2009 issued by DGCA.

Appendix 2: Certificate from the Statutory Auditors as regards to accounting treatment of DF.

"APPENDIX-1"

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GOVERNMENT OF INDIA
AERONAUTICAL INFORMATION SERVICES
DIRECTOR GENERAL OF CIVIL AVIATION
OPPOSITE SAFDARJUNG AIRPORT
NEW DELHI-110 003

SI. No. 2/2009

28th February 2009

File No. 9/18/2008-IR

The following AIC is issued for the information, guidance and compliance.

(A.K. Chopra)
Acting Director General of Civil Aviation

COLLECTION OF DEVELOPMENT FEE

In exercise of power conferred under Section 22A of the Airports Authority of India Act, 1994, the Central Government have approved the levy of Development Fee by Delhi International Airport (P) Limited purely on an adhoc basis @ Rs. 200/- per domestic passenger and @ Rs. 1300/- per international passenger departing IGI Airport, New Delhi w.e.f. 01-03-2009 for a period of 36 months.

2. In order to obviate inconvenience to the passengers and for smooth and orderly air transport/airport operations, it has been decided that all the airlines shall collect the Development Fee (DF) from the passengers at the time of issue of the air ticket and remit the same to DIAL in line with the system/procedure in vogue in respect of collection of PSF. For this, collection charges not exceeding Rs. 5/- per passenger shall be receivable by the airlines from DIAL, which shall not be passed on to the passengers in any manner.

3. DIAL may exempt following persons from levy of Development Fee

(a) Infants, i.e., those persons who are travelling on infants tickets issued by the airlines.

(b) Holders of Diplomatic Passport.

(c) Airlines crew on duty;

(d) Persons travelling on official duty on aircraft operated by Indian Armed Forces;

(e) Transit/transfer passengers (less than 6 hrs. stay at IGI Airport, Delhi)

(f) Passengers departing from IGI Airport, Delhi due to involuntary rerouting, i.e., technical problems or whether conditions etc.

4. The accounting modalities shall be decided by DIAL with the approval of Airports Authority of India.

"APPENDIX – 2"

BRAHMAYYA & CO.,
CHARTERED ACCOUNTANTS

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KHIVRAJ MANSION'
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Auditor's Certificate

We M/s. Brahmayya & Co., being Joint Statutory Auditors of M/s. Delhi International Airport Private Limited (the Company) having its registered office at New Udaan Bhavan, Opp: Terminal 3, New Delhi – 110037 have reviewed the books of accounts and relevant records pertains to Development Fee (DF) of the Company as on March 31, 2011. Ministry of Civil Aviation (MoCA) vide its letter No.F.No.24011/002/2008-AD has approved levy of Development fee, on passengers embarking from Indira Gandhi International Airport, by the Company at the rates of Rs.200/- for domestic passenger and Rs.1,300/- for international passenger for a period of 36 months with effect from 01st March, 2009 subject to a maximum amount of Rs.1,827/- Crores (determined on Net Present Value Basis as on 01st March, 2009). The Company has taken bridge loans against the DF Receivable and started utilisation of such loans towards the project. The accounting treatment followed by the Company is as follows:

A. Receipts from Bridge Loans have been transferred to Separate Escrow Account maintained.

B. All receipts from billing of DF to Airlines are deposited into Escrow Account.

C. Interest and Principal Repayment towards DF bridge loans are paid from the above Escrow Account.

D. The Company discloses the DF Billed, Future Receivables, Receipts, Bridge Loans and interest paid in the Financial Statements as follows:

   (i) Based on the passenger information submitted by the Airlines, DF invoice is raised by DIAL on the Airlines and the amount invoiced after reducing collection charges is credited to "DF Billed Account".

   (ii) Interest Paid towards Bridge Loans is netted off from the "DF Billed Account" as explained in clause (i).

   (iii) DF Billed and future receivable DF amounts are reduced from the Gross Block of Fixed Assets.

   (iv) Bridge Loans are shown as Secured Loans.

BRAHMAYYA & CO. Chartered Accountants BANGALORE

Based on the above and as represented by the Management we hereby Confirm that the Company is following appropriate accounting policy in respect of DF, DF Loan and interest thereon and We hereby certify that interest on DF Loan is not charged to Profit and Loss Account and the Company has not availed any tax shield for the interest .

For Brahmayya & Co.,
Firm Registration No.000515S
Chartered Accountants

BRAHMAYYA & CO. Chartered Accountants BANGALORE

(G.Srinivas)
Partner
Membership No.086761

Place: Bangalore
Date : 12th May, 2011