**Kakinada – Plant and Machinery:**

NFCL’s Plant I is 30 years old, and Plant II is 24 years old, the plants are fully depreciated. During the CDR period, as the priority was given for debt reduction, the Company could not adequately spend on the maintenance and replacement of plant and machinery. Just after exiting CDR, due to GAIL pipeline accident, due to non-release of funds assessed by the lenders for CAP led to financial stress disabling the Company capability to spend on maintenance and replacements of plant and machinery which has led to substantial impairment of the life and value of the plants.

The Government revised the energy norm for industry necessitating investment to reduce the energy. Non-investment in maintenance (reliability measures) and investment in energy saving project resulted in operating the plant at higher energy consumption than the norm, leading to cash losses in excess of Rs 30 Crores per month with expenses higher than the revenues. The Company is unable to meet the production cost despite producing at full capacity.

The requirement of investment for meeting the energy norm was estimated by M/s Saipem (technology supplier) during 2015-16 study. Since then, the plant has substantially deteriorated, and project costs have increased. The requirements now for replacements to avoid breakdowns and to improve the reliability, based on equipment life, present health conditions and energy saving project was estimated by M/s Mott Macdonald in 2020-21(Banker’s consultant).

The Written Down Value of plant and machinery as on 31 March 2021 is Rs 79.58 Crs as per Income Tax Act 1963 (calculated based on actual acquisition cost of plant and machinery).

Due to continued cash losses from the operations, the company has engaged a valuer as per Ind-AS to test impairment of cash generating assets. The details will be shared upon closure of accounts.

Methodology used by valuer is produced below for ready reference.

The investment for the recently commissioned urea plant was considered for replacement value after the following adjustments.

* 1. Capacity difference
	2. Energy efficiency difference (technology obsolescence)
	3. Incurable obsolescence (depreciation)
	4. Curable obsolescence (cost of replacement required for continuing safe and economical operations assessed by M/s Mott Macdonald)

Value as per above steps or realisable salvage value whichever is higher is considered.

**Plant and Machinery Liquidation Value:**

Based on the above methodology, the replacement value is coming negative, therefore salvage value of the asset was considered. While considering the salvagevalue, being a hazardous, chemical plant with very heavy equipment, catalysts and other hazardous materials, the cost involved in dismantling, disposing off the hazardous materials were partially considered while arriving at the realizable value.

**Excerpts from the impairment testing report (draft) on Kakinada plant and machinery are produced below:**

**Computation of Replacement Cost**

PLANT & MACHINERY (From Balance sheet of RFCL)

|  |  |
| --- | --- |
| **DESCRIPTION** | **AMOUNT (in Cr.)** |
| Gross Book Value as on 31/3/2021 | 4459.9 |
| Capital Work in Progress | 179.7 |
| Other Equipment | 159.81 |
| SUB TOTAL | 4799.41 |
| Adjustment factors: |  |
| (i) @6% for capacity difference | 4031.50 |
| ii) @ 10% for energy consumption |
| Electricals | 84.4 |
| TOTAL | 4115.90 |
| **REPLACMENT COST NEW (rounded off)** | **4116.00** |

|  |  |  |  |  |
| --- | --- | --- | --- | --- |
| **S.No** | **DESCRIPTION** | **REPLACEMENT COST NEW- (RCN)** | **INCURABLE OBSOLESCENCE (DEPRECIATION) RATE** | **RCN less INCURABLE OBSOLESCENCE(1)** |
| 1 | PROCESS PLANTS & ACCESSORIES | 2863.63 | 82.8% | 493.69 |
| 2 | OFFSITE FACILITIES & UTILITIES | 1167.87 | 81.7% | 213.72 |
| 3 | ELECTRICALS | 84.36 | 85.7% | 12.06 |
|  | **TOTAL** | **4115.86** |  | **719.47** |

The total capital expenditure estimated to be about INR 760 Cr includes reliability improvement measures This amount is deducted as curable deterioration from (1) above. However, after the depreciation factors are applied to RCN, the resultant total asset value less depreciation amounts to 719 Cr. As per the sequence outlined in above table, the deduction of curable obsolescence amount of 760 Cr will result in a negative asset value. As this is not logical, the conclusion is that the assets have only salvage value at best.

Computation of Fair Value

|  |  |
| --- | --- |
| **DESCRIPTION** | **AMOUNT (in Cr.)** |
| REPLACMENT COST NEW | 4115.86 |
| SALVAGE VALUE @ 5% | 205.79 |
| Less COST TO SELL @ 15% | 30.87 |
| FAIR VALUE LESS COSTS TO SELL | 174.92 |

**Kakinada – Buildings:**

Plant buildings are fully depreciated. Owing to inadequate spend on maintenance of civil structures, there has been severe deterioration of integrity of various civil structures across the complex. Due to proximity to seashore and corrosive atmosphere of chemical plant many concrete structures like pipe rack are showing damages and needs repair. The estimated cost (by M/s. Mott Macdonald) of the above repairs is Rs 87.5 Cr.

**Excerpts from the impairment testing report (draft) on Kakinada buildings are produced below:**

It has to be noted that the immovable assets of buildings & other civil structures have been built for the express purpose of housing the plants, equipment and/or providing the administrative/support, enabling movement of material, personnel etc. Any diminution in the value of plant will result in a similar impact on the value of the fixed assets too. Without the plant, the civil structures/immovable assets are also of salvage value.

|  |  |
| --- | --- |
| **DESCRIPTION** | **AMOUNT (in Cr.)** |
| REPLACMENT COST NEW | 339.46 |
| SALVAGE VALUE @ 5% | 16.97 |
| Less COST TO SELL @ 15% | 2.55 |
| **FAIR VALUE LESS COSTS TO SELL** | **14.43\*\*** |

\*\*This valuation does not consider the land contract terms which states that if the plant is not operational (plant and buildings), the Government of Andhra Pradesh can resume the land and ask the Company for removal of the plant and machinery and the buildings at its own cost