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To,
The Secretary
Central Electricity Regulatory Commission
Chanderlok Building,
36 Janpath,
New Delhi – 110001, Fax no. - 011-23753923

Sub: Draft Central Electricity Regulatory Commission (Terms & Conditions of Tariff) Regulations, 2019 for period from 1.4.2019 to 31.3.2024 – Reg.

Sir,

This has reference to Hon'ble CERC's public notice dated 14.10.2018 inviting comments / suggestions / objections on the Draft Regulation on CERC Terms and Conditions of Tariff Regulations, 2019 for the tariff period from 1.4.2019 to 31.3.2024.

In this regard, the views, suggestions & recommendations of GUVNL are as under:

- The objective of Multi Year Tariff Regulations is to determine tariff for 5 year period taking into consideration the prevailing economic scenario, financial framework and challenges & issues faced by Stakeholders. There has been gradual increase in the power purchase cost during last 5 years owing to various operational issues which has been further escalated due to multifold increase in transmission cost.

- The proposed Draft Tariff Framework by CERC does not envisages measures / steps for promoting progressiveness & efficiencies and rather retains most of the norms of Tariff Regulations 2014-19. The continuous increase in generation and transmission cost is offsetting the benefit accrued to Distribution Companies due to efficiency and administrative measures over the years.

- For framing the Tariff Regulations for 2019-24 period, CERC had floated a Consultation Paper in May-18 seeking preliminary views of stakeholders. The comments / views submitted by various stakeholders particularly Distribution

Companies stretches upon fine tuning the tariff fixation methodology to strengthen the compliance norms for promoting efficiency instead of allowing cost pass through which enforces limited accountability. GUVNL vide letter dated 07.07.2018 has forwarded its comments to the same. However, CERC has not taken into consideration the same while releasing the Draft Regulations.

In the above context, the provision wise comments / suggestions of GUVNL is as under:

(a) Bank Rate

In the draft Regulation, 1 year SBI MCLR + 350 basis points have been proposed for allowing cost of debt.

In this regard, it is to state that 1 year Marginal Cost of Lending Rate is the reference rate based on which Banks / Financial Institutions lends money to borrowers. In wake of superior credit profile and large scale borrowing, majority of Utilities for whom the tariff is being determined under these Regulations would be availing loans at MCLR rate only. In view of the same, allowing 350 basis point margin over and above MCLR would lead to deemed increase in cost of borrowing which would have an impact on project tariff. Accordingly, it is suggested that there shall not be allowance above 1 Year SBI MCLR.

(b) Debt: Equity Ratio

In the draft Regulation, normative debt: equity ratio of 70:30 has been retained.

In this regard, Commission may review the normative debt:equity ratio taking into consideration the fact that GENCO/ TRANSCo having improved credit profile, comfortable balance sheet and lower risk profile, are having access to credit close to base interest rate. Various projects have been financed with 80:20 debt:equity ratio. Therefore, revising the same would enable lower fixed burden on beneficiaries as cost of debt capital would be lower than cost of equity. The same would also insulate beneficiaries from sharp increase in tariff on account of compliance to revise Environmental norms for which considerable capital expenditure would be incurred by projects in phased manner. Accordingly, the Equity should be lower of actual or 20% for the purpose of tariff determination.

(c) Time & Cost overrun on account of Land Acquisition as Uncontrollable factor:

In the Draft Regulation, Time and cost over-runs on account of land acquisition except where the delay is attributable to generating company or the transmission licensee has been proposed to be considered as an Uncontrollable factor as against Controllable factor as per existing Regulation.

In this regard, GUVNL is of the view that allowing time / cost over run towards delay in land acquisition activity under uncontrollable parameter will enable GENCo / TRANSCo. to seek delay condonation for the same. Since land acquisition is undertaken as per provisions of relevant acts/rules, instead of considering such cost / time overrun as un-controllable upfront, it would be appropriate to allow the same after considering justifications and prudent check on case to case basis by CERC.

In view of above, the existing provision may be retained.

(d) Availability Declaration, Capacity Charge for peak and off-peak period, Normative Annual Plant Availability Factor, & Incentive

i. **Availability Declaration:** The proposed methodology for giving separate availability for each fuel source along with its variable charge to be considered for scheduling of power under Merit Order is very much essential in order to ensure off-take of power as per merit order protocol. However, there needs to be clarification that the indicated rate for each fuel source shall be considered as ceiling for the purpose of payment of energy invoices as otherwise it would lead uneconomic operations of plants on real time basis if subsequent claim under Energy invoices are higher than as declared in advance under merit order.

ii. **Capacity Charge for peak and off-peak period:** In the draft Regulation, it is proposed to allow recovery of fixed cost of generation in two parts, separately for Peak Period and Off-Peak Period for a day. Total Peak period during a day shall not be less than 4 hours and the remaining hours will be Off-Peak Period. Concerned RLDCs will specify the peak and off-peak periods on monthly basis.

In this regard, it is to mention that Commission needs to specify the duration of peak hours i.e. specific hours. Moreover, the total Capacity charge for peak and off-peak shall not be more than the Capacity charge determined by Commission for the project.

iii. **Normative Annual Plant Availability Factor:** In the draft Regulation, it is proposed to reduce the same from 85% to 83%.

In this regard it is to state that average actual availability of NTPC plants is above 90%. Moreover, the plants have been using imported coal for the purpose of blending which ensures declaration of full availability even during fuel shortage scenario. Accordingly, it is suggested that reducing the normative availability to 83% would lead to proportionate increase in capacity charges on beneficiaries while promoting inefficiency due to reduced availability limits.

In wake of historic average availability of more than 90% and considering the fact that duration of outages (forced + planned) are not more than 10% in a year, it is suggested to revise Normative Availability at 90%.

iv. **Incentive:** In the draft Regulation, it is proposed to increase incentive to 65 paise / unit for dispatch during peak period against existing 50 paise/ unit.

It is to mention that higher incentive during peak period may lead to gaming / arbitrary availability declaration for maximizing revenue recovery by Generator which could affect availability of round the clock power to beneficiaries specifically during fuel shortage scenario. Moreover, by allowing higher incentive for particular time blocks in a day, Distribution Companies would end up paying additional cost over and above rate under Merit Order leading to uneconomical operation. In order to avoid such gaming the incentive rate for both peak and off-peak may be retained at 50 paise / unit as per existing Regulation.

(e) Gross Calorific Value of Fuel, Transit & Handling loss for computation of Energy Charge

i. **GCV:** In the Draft Regulation, GCV as received basis has been defined as measured at unloading point of plant in accordance with IS 436 (1964) to be carried out through third party sampling appointed by GENCo. Further, while working out weighted average GCV of fuel as received basis, 85 kcal/kg reduction is proposed to be allowed towards variation due to storage of fuel.

In this regard, it is to mention that as per fuel details uploaded on NTPC portal, there is wide variation between “Billed GCV” and “As received GCV” for coal based projects i.e. more than 10%. The cost of such inefficiency is being borne by consumers at present. Accordingly, it is suggested that “GCV As billed” for which payment is made as certified by CIMFR minus allowance of 72 kcal/kg (as per IS 1924) should be considered for computation of Energy Charges since it is the responsibility of Generator to ensure that quality of coal received is commensurate with quality for which payment is made. With regard to allowing 85 kcal/kg towards storage variation, it is to state that Generator is responsible to ensure that the fuel is appropriate stored and handled at plant premises. In addition, the coal stock at majority of plant is for 5-7 days only and hence upfront 85 kcal/kg reduction should not be allowed.

In view of the same, it is suggested to appropriately modify the definition of GCV As Received Basis and formula for computation of Energy Charge for avoiding unfettered pass through of inefficiency towards coal GCV variation.

ii. **Transit & Handling loss**: In the draft Regulation, it is proposed to be increased to 1.2% from 0.8% (beyond 1000 km) and for imported coal from 0.2% to 0.8-1.2%.

In this regard, it is to state that existing limit of 0.8% shall be retained towards Transit & Handling loss irrespective of distance. Moreover, the transit loss for imported coal should not be more than 0.2% for projects located at coastal area and 0.8% for non-coastal power projects.

(f) Allowable variation in Design Heat Rate and Auxiliary Energy Consumption:

In the draft Regulation, it is proposed to allow variation in design heat rate at 5% from 4.5% at present. In view of advanced technology with improved efficiency, the existing allowable variation of 4.5% may be retained.

In the draft Regulation, it is proposed to revise the Auxiliary Energy Consumption for 300-500 MW, 600 MW & above from 5.25% to 5.75% (for steam driven) and from 7.75% to 8.00% (for electrically driven). The proposed change in Auxiliary is based on previous 5 year data.

In the above context, it is to state that in May-2017, CERC has already notified separate Regulation laying detailed procedure for compensation to plants for station heat rate, auxiliary energy consumption for low unit loading and secondary fuel oil consumption for additional start-ups. As the above mechanism addresses the issue of compensation to Generators towards technical parameters, the existing provision may be retained to avoid duplication and CERC while prescribing the norms for future period may reduce the impact on account of operation for which compensation is separately given.

(g) Return on Equity:

In the draft Regulation, the earlier provision of additional 0.5% ROE for completion of project within specified timeline along with the completion timelines has been deleted.

While the deletion of additional RoE of 0.5% is appropriate, it is necessary that the timelines to ensure timely completion of project are stipulated to avoid cost and time overrun as it has been observed that there has been delay in commissioning of various units/ projects owing to which Distribution Licensee has to arrange alternate power for such period.

In the draft Regulation, 15.5% ROE post tax (i.e. around 22% on pre-tax) is proposed to be retained. In this regard, it is to point out that Govt. of India is promoting and emphasizing competitive bidding mode for Generation, Transmission and Distribution segment as well. In the scenario, when power tie up is mandated through competitive bidding, allowance of 22% pre-tax ROE for projects which are having every cost element as pass through including income tax with identified buyers, backed with payment security mechanism, the overall risk is minimum. Moreover, the risk free rate of return (Govt Securities etc.) during last decade has remained in the range of 7-8% and actual return for various large scale business / sectors are contingent to market return which has remained around 12-15%.

In such a scenario, for projects having favorable attributes as stated above, the assured return of around 22% throughout the project life is way higher and imposes cost burden on beneficiaries / consumers for the high profitability of such projects discouraging stringent efficiency measures. In view of the same, it is suggested that RoE shall be divided into two parts i.e. (i) Guaranteed 7-8% RoE based on Risk Free Rate of Return and (ii) Risk premium of around 4-5% being made part of component of tariff for ensuring that the post-tax ROE does not exceed 12% in any case.

(h) Depreciation:

Depreciation is allowed as a tariff component for recovery from beneficiaries being a deductible expense towards repayment of capital investment for an asset over its useful life. Thus, deprecation shall be allowed only upto the repayment of investment under the tariff component.

It is suggested to adopt one of the following approaches for allowing depreciation:

(i) Allowing depreciation upto debt amount – actual amount of debt subject to ceiling of 70%/80%

(ii) Allowing depreciation upto 90% of asset value and after repayment of debt, the equivalent reduction should be made in equity till the equity becomes equivalent to salvage value i.e. 5%

This will help in significantly reducing the tariff burden on stressed Distribution Companies.

(i) Interest on Working Capital:

In the draft Regulation, for the purpose of computing Interest on Working Capital, it is proposed to revise the cost of fuel considered for non-pit head plant to 20 days from 30 days at present. While, the provision of allowing maintenance spares at 15% of O&M expenses has been retained.

In the above context, it is suggested that in view of coal shortage scenario and scanty coal availability at power stations and non-availability of adequate cheaper gas, it would be appropriate that the fuel stock for purpose of working capital interest is considered at 7 days for Pit Head & Gas and 10 days for Non-pit head.

With regard to Maintenance Spares as a part of Working Capital, it is to mention that O&M expenses allowed for one month period under IWC already takes care of the cost towards spares for preventive maintenance as well as carrying cost while other major spares cost is already a part of

Capital cost. Accordingly, it is suggested that Maintenance spares at 15% of O&M shall not be allowed and be eliminated from the component of IWC to avoid duplication of cost.

(j) Operation & Maintenance Expenses (O&M):

In the draft Regulation, Commission has derived normalized O&M expenses actually incurred by the Generating stations for arriving at the value of base year (2019-20) which is proposed to be escalated at 3.20% for subsequent period upto 2023-24.

In this regard, it is to state that adequacy O&M norms needs to be reviewed as fixing of base O&M for this control period based on actual expenditure with already permitted escalation tantamount to O&M pass through ignoring the need for improvising /economizing O&M expenses.

Moreover, the O&M on normative basis does not demarcate the expenditure requirement based on vintage factor and residual life. Thus, it would be prudent to benchmark the O&M cost of top efficient plants in order to economize O&M cost amongst other projects incurring higher O&M cost in a phased manner instead of allowing normative cost in general.

(k) Refund for excess tariff recovered towards additional Capital Expenditure:

In the Tariff Regulation (2014-19), where capital cost considered for tariff on basis of projected additional CAPEX exceeds actual additional CAPEX by more than 5%, Regulation provides for refund towards over-recovered amount along with interest at 1.20 times of bank rate. In the Draft Regulation, it is proposed to revise the criteria from 5% to 10%.

It is suggested that existing provision of variation of more than 5% may be retained otherwise it would lead to advance recovery for such differential cost putting additional cost burden on stressed Distribution Companies.

(l) Sharing of savings in interest due to re-financing:

In draft Regulation it is proposed that the benefits accrued on account of savings in interest due to re-financing of loan shall be shared in the ratio of

1:1 as against existing norm of 2:1 between Beneficiary and GENCo/ TRANSCo respectively.

In this regard, it is suggested that re-financing of loan is a prudent Utility financial practice for reducing interest outgo. Since entire cost towards plant / debt has to be borne by beneficiary, there is no rationale of providing additional incentive to GENCO/TRANSCo towards such generic function and hence existing norms of sharing benefit in ratio of 2:1 shall be retained.

(m) Three part Generation Tariff:

As suggested in the CERC Consultation Paper (May-18), Commission may revise tariff framework for having 3 part tariff which would impart flexibility to beneficiaries and rationalized fixed cost burden, in view of increasing difference between Plant Availability Factor & Plant Load Factor due to considerable RE integration. Tariff may comprise of (i) Capacity Charge – Interest on Loan, Depreciation, Part of O&M and Guaranteed ROE (say 8%) linked to Availability (ii) Variable Capacity Charges (Incremental return above Guaranteed RoE say 4% and Incremental O&M based on scheduled energy and (iii) Energy charges linked to Scheduled energy.

(n) Two part Transmission Tariff

In the proposed Tariff Regulations, the two part tariff structure for the transmission system has not been considered, which was proposed in the consultation paper and supported by beneficiaries.

CERC may consider determination of Transmission tariff in 2 parts viz. Based on (a) Access charges linked with entire capacity of generation project capacity and (b) transmission service linked with capacity of LTA sought which would have long term impact and bring efficient and prudent investment. Access charges shall include Annual Fixed Cost of line constructed for granting connectivity and system strengthening for enabling such connectivity whereas transmission service charges shall be for the pooled assets.

Certain high capacity transmission assets have been created to overcome ROW issues or considering scale of economy. However such lines are partially used and having huge redundant capacity. The entire cost of such assets should not be passed on to existing beneficiaries and there is need of deferring the recovery till such unused capacity is utilized. Recovery from present beneficiaries is leading to cross subsidization by existing beneficiaries for the future transmission users. Accordingly, Commission may devise a suitable mechanism for differing the cost of unused capacity.

Thanking you,

Yours faithfully,

(K. P. Jangid)
General Manager (Comm.)