

## Explanatory Memorandum

### **Draft Central Electricity Regulatory Commission (Procedure, Terms and Conditions for grant of trading licence and other related matters) (First Amendment) Regulations, 2020**

#### **1. Introduction**

- 1.1. In exercise of the powers conferred under section 178 of the Electricity Act, 2003 (Act) read with all other relevant provisions, the Central Electricity Regulatory Commission (hereafter referred to as “the Commission”) notified the Central Electricity Regulatory Commission (Procedure, Terms and Conditions for grant of trading license and other related matters) Regulations, 2020 (hereafter referred to as “Trading Licence Regulations 2020”) which came into effect in January 2020.
- 1.2. Thereafter, on receipt of stakeholder comments in respect of two clauses, the Commission after due consideration and analysis considers it necessary to propose amendments as discussed below.

#### **2. Proposed Amendments**

##### **2.1. Trading margin in respect of banking of electricity transactions: Regulation 8(1)(e)**

- 2.1.1. The Commission in Trading Licence Regulations 2020 notified the following under Regulation 8(1)(e):

*“For banking of electricity, the Trading Licensee shall charge a cumulative trading margin of not less than zero (0.0) paise/kWh and not exceeding seven (7.0) paise/kWh.”*

- 2.1.2. After the notification of the Trading Licence regulations, 2020, some of the stakeholders have sought clarification as to whether a trader can charge negative margin on any one leg of the banking transaction as long as the cumulative trading margin remains between zero (0.0) and seven (7.0) paise/kWh.

- 2.1.3. The Commission has noted that as per clause 5.1.4.1 of the Statement of Reasons issued on 2<sup>nd</sup> January 2020: *“There should be a cap and a floor on the trading margin for short term contracts and banking contracts.”*. Accordingly, Regulation 8 of the Trading Licence Regulations, 2020, provides for cap and floor on the trading margin. By charging negative trading margin from one party, though the trading licensee can comply with the cumulative trading margin of not less than zero (0.0) paise/kWh and not exceeding seven (7.0) paise/kWh as per regulation 8(1)(e) of the Trading License Regulations, the cap and floor

would be indeterminate. For example, for the same cumulative trading margin, say five (5.0) paise/kWh, the cap and floor can be fifteen (15.0) paise/kWh and minus ten (-10.0) paise/kWh or twenty (20.0) paise/kWh and minus fifteen (-15.0) paise/kWh. The Commission is of the view that such an arrangement would lead to market distortion and therefore, neither party to the banking transaction should be charged trading margin of less than (0.0) paise/kWh. In order to get clarity in the regulation, the following proviso is proposed to be added to sub-clause (e) of clause (1) of Regulation 8:

*“Provided that the trading margin shall not be less than zero (0.0) paise/kWh from either of the parties to the banking transaction.”*

## **2.2. Value of Letter of Credit in respect of short term contracts: Regulation 9(10)(b)**

2.2.1. The Commission in Trading Licence Regulations 2020 notified the following under Regulation 9(10):

(10) *“The Trading Licensee shall make payment of dues by the agreed due date to the seller for purchase of the agreed quantum of electricity through an escrow arrangement or irrevocable, unconditional and revolving letter of credit in favour of the seller. Such escrow arrangement or irrevocable, unconditional and revolving letter of credit in favour of the seller shall be equivalent to:*

*(a) one point one (1.1) times the average monthly bill amount (estimated average of monthly billing amounts for three months or actual monthly billing amount for preceding three months as the case may be) with a validity of one year for long term contracts;*

*(b) one point zero five (1.05) times of contract value for short term contracts.”*

2.2.2. Some of the stakeholders have brought to the notice of the Commission that Regulation 9(10)(b) requiring trading licensees to maintain escrow arrangement or letter of credit equivalent to 1.05 times of the value of the contract requires huge finance from the end of the trading licensee. They have suggested that the escrow arrangement or letter of credit should be commensurate with the value of the transaction for a monthly billing cycle and not for the value of the transaction as a whole.

2.2.3. The Commission is of the view that for transactions of less than one month, 1.05 times of the contract value should be considered for the purpose of escrow arrangement or letter of

credit irrespective of the billing cycle. This requirement is taken care of by the provisions of Regulation 9(10)(b) of the Trading Licence Regulations, 2020. However, in case of short term transactions for a duration of more than one month, escrow arrangement or letter of credit equivalent to the contract value for the entire duration of the contract will be onerous to the trading licensees, particularly when the transactions are usually settled on the basis of monthly billing cycle. Accordingly, the value of escrow arrangement or letter of credit for transactions with a duration of more than one month should be equal to 1.05 times of the monthly contract value irrespective of the duration of the contract. Accordingly, the following proviso is proposed to be added after sub-clause (b) of clause (10) of Regulation 9:

*“Provided that where the duration of the short term contract is more than one month, the letter of credit in favour of the seller shall be equivalent to one point zero five (1.05) times of the monthly contract value with validity period equal to validity of the contract.”*

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