Preliminary Views of JITPL on the Approach Paper issued by the Staff of the CERC

General-

1. Para No.4.15- Two different approaches for return on equity v/s Return on capital employed.
   We are of the view that the Interest cost should be calculated on capital employed, which includes other equity also and ROCE might be better one (detailed elaboration provided in the subsequent paragraphs)
2. Para no 7.1.26- Proposal for increasing life from 25 Years to 35 Years
   We are of the view that the life may be considered for 25 years only, as depreciation will be higher (detailed elaboration provided in the subsequent paragraphs).
3. Point no 7.1.24 – Tax rate- Tax may be allowed only in case, where income tax has actually paid, under no circumstances tax can be allowed to be recovered if the company has not paid any tax for the year under consideration-
   We are of the view that since the tax liability always survives, it must be allowed and considered as part of tariff. Such liabilities may get deferred due to lesser/higher depreciation. (detailed elaboration provided in the subsequent paragraphs)
4. No where mentioned regarding cost of transmission Loss and transmission charges
   We are of the view that the cost of transmission loss and transmission charges may form part of the variable cost.

Comments sought by the Staff of the Commission on Approach-1:

5. Whether clustering the components of AFC based on their nature to increase/decrease will allow better projections? Any other possible method to cluster the AFC components?

   Our response: Prima facie we agree. However, we reserve our rights and contentions to furnish our detailed comments.

6. Whether the impact of additional capitalization can also be allowed through the same indexation mechanism or through a separate revenue stream?

   Our response: Yes, indexation might be better.

Comments sought by the Staff of the Commission on Approach-2:

Simplification of the existing Performance Based Hybrid Approach, wherein Interest on Working Capital on a normative basis which can factor in the variations due to actual fuel prices and interest rates?

Our Response: This approach is more conducive for regulatory oversight, with few changes to the existing regulations by way of normative additional capitalization, normative working capital, and normative interest on loan for achieving further simplification.

Financial Aspects Impacting Tariff

1. Capital Cost (Clause 7.1.4)	Preliminary views of JITPL
Procurement of Equipment and Services Need to award work and services contracts for developing projects through a competitive bidding process.	Acceptable, with exemption to the under-construction projects acquiredthrough NCLT where it may not be possible to follow the above process, as the vendor / manufacturer cannot be changed in midway of the procurement process.

2. Capital Cost (Clause 7.1.5)	Preliminary views of JITPL
Reference Cost for prudence check Other efficient reference cost than Investment Approval costs for prudence check of capital cost of new projects	Depreciated Historical Cost should be considered for computation of capital cost. The word "Acquisition Value" should be removed. It is proposed to continue with the current approach of prudence of capital costs based on the investment approval cost and reference to hard cost of recently commissioned projects of similar specifications

3. Capital Cost (Clause 7.1.7)	Preliminary views of JITPL
Projects Acquired post NCLT Proceedings 1. Historical Cost or Acquisition Value, whichever is lower, should be considered for tariff post approval of Resolution Plan.	Historical price may be considered as consideration of acquisition price would reduce the revenues and thereby result in continued financial stress against the acquired asset. This would add further

2. Tariff provisions to be included to address the issue of the cost of debt servicing, that were allowed as a part of the tariff during the CIRP process	difficulties in process of revival of the stranded projects. Specific provision for non-consideration of any additional cost /expenses on account of servicing on loans or liabilities towards procurement of fuel, goods, etc. relating to the past periods in case of truing-up or future tariff determination may be considered. The main emphasis of the Government/Policy makers has always been to reduce the Stress prevailing in the Coal Based Thermal Power Plants in our country. However, with the given intent of the present Staff paper, such Stress would on a contrary increase on the Coal based thermal power plant. Therefore we are of the preliminary view that no actions may be initiated which would create even more stress to the thermal power generation sector.

4. Additional Capitalization (Clause 7.1.15)	Preliminary views of JITPL
Inclusion of "Cost towards Railway infrastructure augmentation" in existing provisions of additional capitalization.	1. Inclusion of "Cost towards Railway infrastructure augmentation" in existing provisions will result in better fuel management. 2. It is suggested to include "Cost towards Coal Conveyor Belt Construction" in the existing provision. 3. It is also suggested to include "Any modification in Dedicated Transmission Line of the Generating Station" in the existing provision. 4. Suitable regulatory provisions also needs to be provided to deal with following requirements: a. Ash disposal and utilization as per MOEF Notifications / Statutory Notifications

	b. Biomass co-firing (FGD)

5. GFA/ NFA/ Modified GFA Approach (Clause 7.1.18)	Preliminary views of JITPL
Gross Fixed Assed/ Net Fixed Asset/ Modified Gross Fixed Asset Net Fixed Assets = Gross Fixed Assets – Accumulated Depreciation	Existing GFA Approach may be continued in the interest of the entire power sector and to facilitate future capacity addition.

6. O&M Expenses (Clause 7.1.19)	Preliminary views of JITPL
1. Normative O&M expenses may becontinued. 2. Capital Spares may be allowed on a normative basis. 3. Alternatively, low value spares ~ Rs. 20 lakhs may be made part of O&M norms, while capital spares with value in excess of Rs. 20 lakhs, reimbursement based on CERC consideration. 4. Inclusion of provision for allowing impact of change in law in O&M.	1. Existing mechanism of allowing normative O&M expenses may becontinued. 2. Approach of allowing capital spares on a normative basis is principally accepted. 3. The proposal of including Capital Spares below Rs 20 lakh, as a part of O&M expenses and capital spares costing above Rs. 20 lakhs as a part of the reimbursement are generally acceptable. 4. Provision to deal with the impact ofchange in law events may be provided in the O&M expenses

7. Depreciation (Clause 7.1.20)	Preliminary views of JITPL
Depreciation rate of 15 years instead of 12 years. Further, additional provision may also be specified that allows lower rate of depreciation to be charged by the generator in the initial years if mutually agreed upon with the beneficiary(ies).	1. In case of existing stations, it would be appropriate to continue with the existing depreciation schedule as any changes in depreciation would result in loan payment difficulties under the existing loan tenures. 2. The dispensation of increase in depreciation spread from 12 to 15 years may be adopted prospectively for new stations commissioned in the upcoming tariff period.

8. Interest on Term Loan (Clause 7.1.21)	Preliminary views of JITPL
1. Based on actual Interest rate of loan of Company instead of project specific. 2. The cost of hedging related to foreign loans be allowed on actual basis, without allowing any actual FERV (Foreign Exchange Rate Variation).	1. Instead of considering weightedaverage rate of interest, the MCLR (Marginal cost of funds-based lending rate) with suitable margin can be considered for approving the interest on capital loan. 2. Existing provisions of recovery ofthe cost of hedging and FERV variation on year-to-year basis may becontinued. In case of shifting to normative interest rate on loan, Suitable margin may be provided over MCLR to incorporate the FERV risk on account of External Commercial Borrowings.

9a. Return on Equity (ROE) vs Return on Capital Employed (ROCE) (Clause 7.1.22)	Preliminary views of JITPL
a. ROE = Net Income / Shareholders' Equity Net Income = Net Revenue – All Expenses including Interest & Taxes	ROCE works especially well when comparing the performance of companies in capital-intensive sectors, such as power generation.
b. ROCE= EBIT/Capital Employed $\text{Return on Capital Employed} = \frac{\text{EBIT}}{\text{Total Assets} - \text{Total Current Liabilities}}$ $\text{Return on Capital Employed} = \frac{\text{EBIT}}{\text{Shareholder's Equity} + \text{Long Term Liabilities}}$	Unlike other fundamentals, ROCE considers debt and other liabilities as well. This provides a better indication of financial performance for companies with significant debt.

9 b. Rate of Return on Equity (ROE) (Clause 7.1.23)	Preliminary views of JITPL
1. The average of 10-year GOI securitiesrate over a one-year horizon may be considered a risk-free rate 2. Daily data on the SENSEX and BSE Power Index for the latest 5 years may beconsidered for equity beta estimation. 3. The Market Risk Premium (MRP) reflecting the historical returns for a period of 30-years or beyond instead of the existing practice of considering 20 years may be considered for MRP estimation. 4. Alternatively, MRP may be computed using any other method including the Survey Method	The following factors need to be taken into consideration while fixing the rate of return on equity: i. The expected increase in risk-free rate of return in the wake of unprecedented global as well as domestic inflation and greater peril ofincrease in interest rates in the forseeable future. ii. The overall risks in the thermal generation business. iii. Additional economic and business risks caused by persistent COVID, resulting supply chain crisis, and continuing Ukraine war. iv. The need of capacity addition in the thermal sector and the requirement of overall investment and equity. Higher returns attract larger capital. v. Compensation of loss of return to equity investor during the large gestation period. vi. Parity of returns with transmission and RE business basedon corresponding risks and effective equity IRR. vii. Provisions for not only current risks but future risks also as the regulation is based on a multi-year tariff framework. Therefore, a favourable climate needs to be provided through an enhanced rate of return on equity for the tariff period 2024-29, so that thermal generation becomes attractive for investment.

10. Tax Rate (Clause 7.1.24)	Preliminary views of JITPL
Base Rate of RoE may be grossed up as follows: 1. At MAT rate (If not opted for Section 115 BAA) 2. At effective tax rate (if not opted for Section 115BAA) subject to ceiling of Corporate Tax Rate; or 3. At reduced tax rate under Section 115BAA of the Income Tax Act or any other relevant categories notified from time to time subject to ceiling of rate specified in the relevant Finance Act. 4. Further, tax shall be allowed only in cases where the company has actuallypaid taxes for the year under consideration.	The Following are suggested: 1. The Effective Tax Rate should beconsidered without capping atceiling rate except in cases whengenerating company is paying Minimum Alternate Tax (MAT). 2. In case generating company is paying Minimum Alternate Tax (MAT), Effective Tax Rate shall be MAT rate including surcharge and cess.t

11. Interest on Working Capital (Clause 7.1.25)	Preliminary views of JITPL
1. Retaining existing norms of Coal/ Oil Stocks/Receivable etc. a. Actual fuel stock position maintained by plants – Pit Head (10 days) and Non- Pit Head (20 Days) b. Average Credit Cycle – 45 days Receivables. 2. Any alternative than Normative Interest Rate of SBI 1 Yr MCLR +350 BPS	1. a. It is suggested to change the Fuel Stock Position to be maintained by Pit Head to 15 days from 10 days and Non-Pit Head to 24days from 20 days based on "Revised Coal Stocking Norms for Coal Based Thermal Power Plants" issued by CEA vide dated 6th December 2021. b. It is suggested that receivables of 45 + 6 days may be considered for computation of working capital or provision of raising of provisional bill on 1st of each month by the generating company to compensate the loss on account of carrying cost due to delay in issuance of REAs. 2. It is submitted that the existing dispensation of considering one-year MCLR of SBI plus 350 basis points for computation of IoWC is more efficient and may be retained.

Life of Generation Assets (Clause no.7.1.26)	Preliminary views of JITPL
May be increased to 35 years from current specified life of 25 years.	1. The tenure of PPA with the Discoms is 25 years. 2. The depreciation will not be entirely recovered If the useful life is increased from 25 years to 35 years & the Discoms refuses to continue to offtake power from the station after 25 years. 3. In such case, regulations may provide for recovery of residual depreciation and other costs remaining un-serviced. 4. Alternatively, regulations may provide for extension of PPA from 25 years to 35 years on same terms and conditions
Treatment of Arbitration Awards (Clause No. 7.1.29) Principal amount may be capitalised, and the interest amount may be allowed to be recovered in instalments from the beneficiaries. However, such a recovery of interest may also involve carrying cost.	The Genco may not be denied capitalization of the principal and interest amount in a cost-plus regulatory framework as there is no imprudence on the part of it. In view of the above, treatment as per existing practice may be continued.

Treatment of Interest on Differential Tariff after Truing-up (Clause No. 7.1.30) 1. Interest allowed on differential tariff after truing up. 2. No interest during recovery in six instalments	The provision of instalment is provided so that the Discoms do not face a tariff shock. However, considering the time value of money for the generating company and that he is deprived of the money due on issuance of order, the same may be recovered in six equated monthly instalments along with the interest. In any case, there are specific Rules named Late Payment Surcharges Rules framed and notified by the ministry which clarifies the position that late payment surcharges are to be paid by DISCOMs.

Operational Aspects Impacting Tariff

Particulars of Clause numbers	Preliminary views of JITPL
NAPF (Clause No. 7.1.31) Normative Annual Plant Availability Factor (NAPF) Existing norms of NAPAF may need review by considering past years PAF, the procurement of coal from alternate sources, other than designated fuel supply agreements, changes in hydrology, etc.	It is proposed that NAPAF may be relaxed from the current level of 85%. In case NAPAF is retained at 85%, following liberty may be allowed to generators: • Disincentive shall be limited to the value of ROE in case of non-availability of station up to 85% due to coal shortage. • Regulatory framework to address the impact of fuel shortage situations on NAPAF may be incorporated as it was done in initial three years of 2014-19 Tariff Regulations.
Peak & Off-Peak Tariffs (Clause 7.1.32) Peak and Off-Peak Tariff 1. Whether limit the tariff recovery based on daily peak & off-peak periods or 2. National versus Regional Peak as a reference point for recovery of Fixed Charges.	1. It is suggested that the existing dispensation of achieving target availability separately in high demand and low demand conditions may be discontinued. 2. It is therefore suggested that the peak and off-peak hours should be considered on cumulative basis for the year for recovery of fixed charges.
Operational Norms (Clause 7.1.33)	Following factors may be considered: 1. For units achieving COD after 01.04.2009, 5% margin over design heat rate may be provided as per CEA recommendation irrespective of minimum boiler efficiency limit.

	2. Specific Norms for special features such as pipe conveyor, and Dedicated Transmission Line may be incorporated in the Regulations.
Emission Control System (Clause 7.1.36) 1. Current norms may be continued in absence of sufficient actual data. 2. Incentivizing proper operations of ECS.	1. It is suggested that the existing norms may be retained till sufficient operational data is built up for review of these norms based on actual data. 2. Supplementary Energy Charges for emission control system should not be considered for merit order dispatch.
Compensation for Part Load Operation (Clause 7.1.37) Comments on the earlier norms and any changes that may be required to compensate the generators to operate the plants in a flexible manner to support the Grid.	Part load compensation between 85% to 55% loading factor may be provided on normative basis & and not on "lower of normative and actuals". (details furnished in our note on flexible operation sheet which may be referred)
GCV of Fuel (Clause 7.1.38) Even though the loss in GCV "as received" vis-à-vis "as billed" has reduced, there have not been considerable efforts made by generators in minimising the loss. Comments sought on ways to reduce the gap between GCV "as billed" and "as received"	1. The generating company has been taking all efforts to reduce the grade slippages such as taking up issues with the coal companies, coal controller, and at various ministerial forums, etc. 2. Coal Company may transfer title of coal to the generator at the plant end. This change in methodology will require modifications of existing FSAs and also intervention at the level of the Ministry of Coal (GOI), and the Ministry of Power (GoI). 3. Facilitation and support of CERC in this regard is sought so that interest of consumer and generator is protected.

Preliminary comments on the Compensation methodology for operating a Thermal (Coal) Generating unit below 55% minimum power level-

1. 3A (a) (i)- Is not applicable.
2. 3A (a) (ii)- already covered under (iii)
3. 3A (a) (iii)-

-the units commissioned after 1.1.2004 having 600 MW capacity, their capital cost is not captured under Table-I under 3 (a)(ii).

-Since as on date there are no proven records for minimum load of 40% and increased ramp rate which substantiates that the expenditure(s) available for 600 MW unit size, therefore it would be more prudent not to consider the numbers of 6 Crs/10 Crs, which anyway seem to be extremely less or almost little with respect to the unit size of 600 MW. This should be compensated based on actual expenditure for implementing above measures as these measures would be different for different unit size/design/OEM.

In any case, even the present paper also does not provide any indication towards the 600 MW unit sizes.

4. 3A (a) (iv)- Not applicable
5. 3A (b)- The details pertaining to 600 MW unit size is not provided in this staff paper and thus, we would not be able to comment on this. We would therefore also request that all necessary details pertaining to 600 MW unit size units/plants may kindly be provided for our comments/inputs.

6. 3(B)(a): The details pertaining to 600 MW unit size is not provided in this staff paper and thus, we would not be able to comment on this. We would therefore also request that all necessary details pertaining to 600 MW unit size units/plants may kindly be provided for our comments/inputs.
7. 3(B)(b): Cost of fuel (oil) is dynamic and hence compensation should be given on actual cost of fuel (oil) basis for 0.2ml per kWh increase in consumption.
8. 4 – Since the present staff paper does not provides any details pertaining to 600 MW unit size, therefore it would not be possible to provide any comment at this early stage. We would therefore also request that all necessary details pertaining to 600 MW unit size units/plants may kindly be provided for our comments/inputs.
9. This staff paper provides the details to be considered for NHR increase from 55% upto 40%, so it is suggested to include norms for increase in NHR from 85% to 55% in three different categories like 85% to 75%, 75% to 65%, 65% to 55% as the suggested numbers of NHR in CERC Regulations is also not sustainable for above part load operations.
10. The assumptions captured under Annexure-I of this note seems to capture the details covered under other unit sizes.