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Power

Ref.: APL/CERC/03082024
Date: 03.08.2024

To
The Secretary,
Central Electricity Regulatory Commission,
World Trade Centre, 6th, 7th and 8th floor, Tower -B,
Nauroji Nagar, New Delhi - 110029

Sub.: Submission of additional comments on Draft CERC Order dated 03.07.2024 in Suo-Motu Petition No. 4/SM/2024, sought vide notification No. L-1 /259/2021/CERC dated 03.07.2024.

Dear Sir,

With reference to the comments invited by the Hon'ble Commission on the subject draft order, we had submitted our comments on 24.07.2024. Upon further internal deliberation, we hereby submit our additional comments on the same with a request to kindly take the same on record.

Thanking You,
Yours Sincerely,

For **Adani Power Limited**

M. R. Krishna Rao
President

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APL Additional Comments on Draft CERC suo-motu order for recovery of tariff by Sec. 63 projects for Emission Control System

Sr. No.	Aspect	CERC Draft Order 4/SM/2024 dated 03.07.2024	APL Additional Comments
1	Cost of Debt and cost of Equity	NFA basis (derived by adjusting cumulative depreciation of emission control system). Rate of Interest **– Normative rate of 1-year SBI MCLR + 2.50%.** **Rationale:** • The existing approach of net fixed assets and servicing investment through cost of capital employed is appropriate, being consistent with the principle of economic restitution. • The objective of the reduced normative rate of interest is to provide flexibility to the generating company and not to create an extra surplus. It will balance	1. Draft Order dated 03.07.2024 in 4/SM/2024 proposes Return on Equity (RoE) at the same rate as interest on Debt with the justification that compensation for the change in law cannot be a mechanism to improve the financial position of generating companies. This approach of CERC appears to be based on incorrect assumption that the developer would be able to get equity capital at same cost as interest on debt. Such an assumption is fundamentally wrong and if RoE is kept equal to cost of debt, the generating companies will face huge loss for following reasons: a) Financing of such large size projects is not possible from internal accruals. Thermal generating companies with PPA awarded under Section 63 are already facing financial hardships due to various uncontrollable factors and are somehow managing their operations. Thermal power developers are hardly able to generate any surplus due to increase in interest rates and inflation in O&M expenses. Most of these companies are incurring huge loss in fixed costs and hence have to rope in equity investors for funding FGD Capex who will expect the return as per market conditions. As per current market trend, the 1 year, 3 year and 5 year CAGR for Nifty 50 index are 26.61%, 16.64% and 17.6% respectively. Therefore, it is not possible to muster equity at Debt rate. b) When a change in law event occurs necessitating capital expenditure, the power generating unit usually funds it by bringing in additional capital. Even funding of this capex solely through debt would be difficult as sufficient debt service coverage will not be available if the capital cost recovery is limited to only the cost of debt. c) Further, the return on equity provided needs to be higher than the cost of equity to attract investments in a capital-intensive sector such as thermal

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		the interests of the generating company and procurer(s).	power, which also has a high degree of exposure to policy risks apart from other inherent risks. d) Presently, the coal-based power generation plants are finding it difficult to arrange financing for any new capex in the plants. The lenders and investors have become conscious about the climate impact of coal-based plants. In such a situation, the cost of financing for this sector has gone up and equity investors are expecting return of around 18% per annum. 2. CERC in the Draft Order has noted that it is not mandatory requirement for bidders to follow debt-equity norms for competitively bid projects and also it is not required to disclose debt – equity therefore, separate servicing of equity for installation of FGD under Section 63 projects has not been considered by CERC. This assumption of CERC is also not correct since any Change in Law compensation including installation of FGD is to be allowed based on actuals, as per which the developers under Section 63 PPAs will be required to provide the actual capital cost and details of funding. It is also settled position of law that the compensation for change in law is based on actuals to restitute the affected party to same economic position as if the change in law has not occurred. The restitution principle has also been recognized by the Hon'ble Supreme Court in Energy Watchdog case. Under these circumstances, if equity is not allowed at least at normative 15.5%, the generating companies on one hand would not be restituted as provided under PPA and on the other hand would be subjected to financial loss leave alone earning any return on equity. 3. In this context, it is necessary to bring to the notice of Hon'ble CERC that for granting relief/compensation under change in law towards energy charges for Projects awarded under Section 63, this Commission as well as many other SERCs have been considering the normative operational parameters

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			as specified under the Tariff Regulations. For example, CERC has allowed the compensation towards domestic coal shortfall by considering normative parameter such as Station Heat Rate and Auxiliary Consumption. The consideration of normative parameters has been upheld by the Hon'ble Supreme Court also. On the same lines, the financial norms such as normative return on equity of 15.5% as specified in the Tariff Regulations, should be considered for approving the change in law compensation towards installation of FGD for Projects awarded under Section 63. 4. The Return on Equity (ROE) allowed by Hon'ble CERC as per CERC (Terms and Conditions for determination of Tariff) Regulations, 2024 is 15.5% on a post-tax basis for capex in thermal generating station, which is considered to be reasonable for attracting investments in the power sector. Even this ROE for FGD capex is inadequate considering both the cost of capital and the inherent risks in setting up capital intensive and long-term investments. 5. For Projects awarded under Section 62, the CERC (Terms and Conditions for determination of Tariff) Regulations, 2024 provides for grossing up of base Return on Equity with effective tax rate towards additional capitalization on account of emission control system. However, the grossing-up of base return on equity is not allowed towards installation of FGD for Projects awarded under Section 63. This aspect also needs review. 6. In view of the aforementioned submissions and the comments submitted earlier on 24.07.2024, it is humbly submitted that the return on equity should be considered at least 15.5% towards installation of FGD for Section 63 projects along with tax gross up to restitute the thermal power generators.