केन्द्रीय विद्युत विनियामक आयोग
CENTRAL ELECTRICITY REGULATORY COMMISSION

सत्यमेव जयते

के. वि. वि. आयोग
C.E.R.C.

Dr. Pramod Deo
Chairperson

D.O.No.Chmn/CERC/2009
Dated : 19th February, 2010

Subject : Advice of the Commission on issues relating to regulation of electricity forward contracts and electricity derivatives markets.

Dear Shri Brahma,

This is in continuation of the statutory advice given by the Commission to the Central Government on the above mentioned subject matter vide D.O. No. Chmn/CERC/2009 dated 18.11.2009. After considering various relevant aspects, the Commission had advised de-notification of electricity under section 15 of Forward Contract (Regulation) Act, 1952 (FCRA) and also to consider appropriate amendment to section 14A or section 18(1) of FCRA so that electricity Non-Transferable Specific Delivery (NTSD) contracts are excluded from the purview of FCRA.

2. In exercise of its powers under section 66 of the Electricity Act, 2003, the Commission has notified the Power Market Regulations, 2010 in January 2010. These regulations cover all aspects of the electricity markets comprehensively.

3. The Commission has also considered the minutes of the meeting regarding notification on electricity under section 15 of the FCRA held in the Ministry of Power on 15th January, 2010.

4. While the Commission has decided to reiterate its advice given to the Central Government vide its letter dated 18.11.2009, it would further advise the following interim measures so as to enable orderly development of electricity markets in the country:

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(A) Exempting dealings in Term Ahead delivery based electricity contracts from the provisions of FCRA.

After following the due process, Commission had allowed the two power exchanges to launch Term Ahead contracts in August 2009. Though the Term Ahead contracts fall in the category of forward contracts as per the definition given in FCRA, these contracts are non-transferable specific delivery (NTSD) contracts which are to be mandatorily physically delivered and where the parties to the contract and price fixed in the contract cannot be changed. These contracts help power sector participants to manage both volumetric risk and price risk. The volumetric risk is mitigated as these contracts bring surety of supply / procurement for a defined period as these are mandatorily for physical delivery. The price risk is managed as electricity price is fixed for a future date for both buyer and seller at the time transaction is executed. The central point being that these contracts are to be solely transacted by power sector participants and designed for their benefit. From the physical delivery viewpoint, the scheduling of these contracts requires a smooth and coordinated functioning between power sector participants, power exchanges and system operator (National/ Regional Load Despatch Centre). The scheduling of power under Term Ahead contracts is done in compliance with Open Access Regulations and Indian Electricity Grid Code both of which are under the purview of CERC.

From the above, following two conclusions emerge:

i) Presently the power exchanges are dealing in only such forward contracts which are non-transferable specific delivery contracts. In the Power Market Regulations, 2010, Commission has specifically provided that any other type of electricity derivatives would be permitted at a future date to be notified by Commission after considering the demand supply situation and to ensure reasonable price of electricity with due regard to liquidity and volatility in the market. Therefore, till such notification permitting forward contract other than NTSD, the power exchanges would be dealing only in the forward contracts which are NTSD. It would be relevant to mention that section 18(1) of FCRA exempts NTSD contracts from regulation of Forward Market Commission under section 15 of the Act.

ii) The power exchanges are being regulated by CERC which is a statutory body constituted under the Act of Parliament. The provisions for regulation of the power exchanges have been exhaustively covered in the Power Market Regulations, 2010.

In view of the above two conclusions, regulation of power exchanges till the time they are dealing in NTSD contracts by any other regulatory agency is not required. The power exchanges are newly formed entities in the nascent electricity markets. The regulation of such entities by multiple regulatory agencies needs to be avoided so that power sector stakeholders have clarity and avoidable complexities do not arise. In view of the above, the Commission hereby advises the Central Government to invoke its powers under section 27 of FCRA to exempt power exchanges dealing in non-transferable specific delivery electricity contracts from all provisions of FCRA.

(B) Prohibition on electricity forward contracts which can be financially settled.

As has been mentioned above, in the Power Market Regulations, 2010 notified by the Commission, it has been provided that the forward trading in electricity with option of financial settlement would be permitted by CERC in future after taking into account the supply demand scenario and the level of liquidity and volatility in the electricity markets. The Commission has taken this view to ensure reasonable price of electricity. In view of this position which has also been stipulated in the regulations under Electricity Act, 2003, the Commission would advise the Central Government to ensure that such electricity contracts where there is an option of financial settlement are not traded in the commodity exchanges being regulated by Forward Market Commission.

Best regards.

Yours sincerely,

Pramod Deo

(Dr. Pramod Deo)

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