CENTRAL ELECTRICITY REGULATORY COMMISSION
NEW DELHI

Petition No. 155/MP/2012

Subject: Application under Section 79 of the Electricity Act, 2003 evolving a mechanism for Regulating including changing and/or revising tariff on account of frustration and/or of occurrence of force majeure (Article 12) and/or change in law (article 13) events under the PPAs due to change in circumstances for the allotment of domestic coal by GOI-CIL and enactment of new coal pricing Regulation by Indonesian Government.

Coram Dr. Pramod Deo, Chairperson
Shri S.Jayaraman, Member
Shri V.S.Verma, Member
Shri M.Deena Dayalan, Member
Shri A. S. Bakshi, Member (EO)

Date of Hearing 6.2.2013

Petitioner Adani Power Limited

Respondents Uttar Haryana Bijli Vitran Nigam Limited, Panchkula
Dakshin Haryana Bijili Vitran Nigam Limited, Panchkula
Gujarat Urja Vikas Nigam Limited, Vadodara

Present:
Shri Amit Kapoor, Advocate, APL
Shri Nankani, Advocate, APL
Shri Arun Kumar, Advocate, APL
Shri Jatin Jalundhwala, APL
Shri Vipul H. Jadav, APL
Shri Harish Priyani, APL
Shri M G Ramachandaran, Advocate, Haryana Utilities and GUVNL
Shri Anis De, Mercados, on behalf of APL
Shri KP Jangid, GUVNL
Shri PJ Jani, GUVNL

RECORD OF PROCEEDINGS

The submissions on behalf of the petitioner were made in three parts. In the first part, Shri Nankani, learned counsel, traced the historical perspective of the fuel supply arrangements. In the second part, Shri Anis Dey of Mercados, consultant appointed by the petitioner made a presentation on behalf of the petitioner, highlighting the financial impact of upward revision of price of coal imported from Indonesia consequent to promulgation of Indonesian Regulation and the way forward. Lastly, Shri Amit Kapur, learned counsel, covered the legal aspects of the issues arising in the present proceedings.

2. Shri Nankani made his submissions in the context of the compilation of the fuels supply agreements earlier filed by the petitioner. He submitted that the promoters of the petitioner company, Adani Enterprises Ltd were into coal trading business for more than a decade and had a fairly good idea of nature of coal required for operation of Mundra plant and prices prevalent in international markets. He submitted that Adani Enterprises was already involved in import of coal from Indonesia when the bids for supply of electricity were submitted. Accordingly, the bids were submitted on the assumption that the coal imported from Indonesia would be used for generation of electricity.

3. The detailed submissions made by learned counsel were as under:

(a) Adani Enterprises Ltd had entered into two MOUs for supply of coal for Mundra plant, one on 9.9.2006 and other on 21.12.2006.

(b) The ultimate source of supply of coal under the MoUs was the Indonesian mines as seen from the recitals.

(c) Based on the MoUs, the formal coal supply agreements were to be signed on completion of the feasibility studies of Mundra plant, on the mutually acceptable terms and conditions (including price) and supply was to start from December 2011.

(d) The MoU dated 9.9.2006 was terminated by Adani Enterprises in February 2008 since the parties could not mutually agree on the terms and conditions for supply of coal and the MoU dated 21.12.2006 was terminated in March 2008.

(e) The MoUs establish that the bid was submitted on the assumption that imported coal from Indonesia was to be used for power generation at Mundra plant.

(f) Adani Enterprises executed the Fuel Supply Agreement (FSA) dated 8.12.2006 with the petitioner for supply of coal for Phase 1 for a period of five years, the FSA was later amended to cover Phase 2 though this FSA is not relevant to the present petition.

(g) The agreed price of Indonesian coal was $45 per tonne for coal with GCV of 6000 Kcal and when worked out on *pro rata* basis in accordance with Article 11 of the FSA the price for coal with GCV of 5200 Kcal came to $35 to $36 per tonne.

(h) Under the FSA, the price of coal supplied was to be matched to international index after five years.

(i) The FSA dated 8.12.2006 was not the basis for the price quoted in Gujarat bid dated 2.1.2007, the subject matter of the present petition, and the bid was based on the domestic price as per the letter from GMDC who agreed

in principle to allot Morga coal block for 100% generation, though imported coal could be used for techno-economic reasons.

(j) The Haryana bid dated 24.11.2007 was on the assumption that 70% coal would be available from domestic source and the balance requirement of coal was to be met through the imported coal.

(k) The rate quoted for Gujarat bid dated 2.1.2007 was ₹ 2.3495/kWh, ₹1/kWh was the capacity charge and ₹1.3495/kWh was the energy charge.

(l) Since the supply of coal from GMDC did not materialise, an alternative arrangement had to be made and accordingly the petitioner entered into the FSA dated 24.3.2008 with Adani Enterprises, with validity period of 15 years for supply of coal at $36 per tonne for coal with GCV of 5200 Kcal for Mundra power plant Phase III (2 X 660 MW). Under the FSA, the supply of coal was to be effected from Buneo mines in Indonesia. The FSA dated 24.3.2008 was amended by Modification Agreement dated 12.5.2009

(m)The petitioner entered into another FSA dated 15.4.2008 with Adani Enterprises , with validity period of 25 years for supply of coal at $24 per tonne for coal with GCV of 5200 Kcal for Mundra power plant Phase IV (3 X 660 MW). The FSA dated 15.4.2008 was amended vide two Amendment Agreements both dated 15.4.2008. The FSA dated 15.4.2008 was further amended vide Modification Agreement dated 25.6.2009.

(n) Meanwhile, Adani Enterprises floated a Singapore based subsidiary, Adani Global Pte Ltd which had acquired mining rights in Buneo mines in Indonesia. The FSAs dated 24.3.2008 and 15.4.2008 was for supply out of designated mines through Adani Global Pte Ltd, which, meant that without changing the source of supply, partially changed the supplier.

(o) Subsequently it was realized that the quality of coal to be procured through Adani Global Pte Ltd was not upto the mark and was below the agreed specifications, the total output was in the range of 2 million and the mine started incurring loss. Therefore on 14.12. 2009 an FSA was entered into between Adani Global Pte Ltd and PT Dua Samudra Perkasa for supply of 10 MTPA to meet the petitioner's requirements of coal at price of $28/ Tonne.

(p) The FSAs dated 24.3.2008 and 15.4.2008 between the petitioner and Adani enterprises provided for supply of coal to commensurate with or corresponding to the scheduled COD under the PPAs, February 2012 in case of the Gujarat PPA and August 2012 under the Haryana PPA.

(q) The FSAs dated 8.12.2006, 24.3.2008 and 15.4.2008 entered into by the petitioner with Adani Enterprises were consolidated into one FSA executed on 26.7.2010, which is the final FSA determining the relationship inter-parties for supply of total quantity of fuel for Mundra power plant.

(r) On 23.9.2010 Government of Indonesia enacted Regulation of Ministry of Energy and Mineral Resources No 17 of 2010 (Indonesian Regulation) under which the coal producers were required to supply coal at prices notified by the Government and all the contracts for sale of coal were declared void.

(s) Before the actual supplies could commence under the FSA dated 26.7.2010, came the intervening event of 23.9.2011 when the Indonesian Regulation was brought into force. As a result the supplies for Phase 3 for Gujarat, and Phase 4 for Haryana could not be started on the contracted price since the price was payable as per the price decided by the Indonesian Government. So the performance under the FSA dated 26.7.2010 was intervened or frustrated by an external event.

(t) From the Buneo mines the petitioner is getting the coal at index price for 15% to 20% of the total requirement. For 80% of the requirement, the petitioner is getting supply from other sources in Indonesia.

(u) The bid price dated 2.1.2007 for supply of power to Gujarat (Phase III) was based on supply from GMDC which arrangement failed, thus the very stratum of the arrangement made had fallen and disappeared because of change in law.

(v) Opinion was taken from Indonesian law firm in Jakarta, SSCK who advised that the Indonesian Regulation could not be challenged. In another opinion it was advised that even if the Indonesian Regulation was challenged it would take 8 years to materialise.

(w) The change in the Indonesian Regulation would not benefit Adani enterprises as only Indonesian supplier would be benefited, though the Indonesian supplier is its subsidiary.

At this stage the Commission intervened to observe that even after promulgation of Indonesian Regulation, the cost of extraction remains unchanged, but the sale price has increased. So the profit of the mining company has increased. So it is a zero sum game for the Adani group as a whole because the gainer is another company of Adani group. However, if the petition is allowed the consumers of Gujarat and Haryana will pay higher tariff while Indonesian company of Adani group would make additional profits. The Commission further observed that the risk on account of price escalation was taken by the petitioner as the bid did not have any escalable element.

(x) When Haryana bid was made the national coal distribution policy had already been announced on 18.10.2007 under which the petitioner was to be allotted coal block commensurate with supply of power to Haryana. So the petitioner factored 70% of coal requirement based on indigenous supply considering the national coal distribution policy and 30% from imported supply. On this basis the petitioner bid at ₹2.94/kWh, including

capacity charge of ₹1/kWh. In the bid it was made clear that two MOUs were executed for using imported coal. Subsequently the petitioner was issued LOA and the Coal Supply Agreement was signed with Mahanadi Coalfields on 9.6.2012 for supply of 70% of the coal requirement for supply of power to Haryana.

(y) There was no document in existence prior the date of bid that bid was based on domestic and imported coal supply in the ratio of 70:30. However, there are documents on record pertaining to post-bid period which show that the petitioner had conceived that 70% of the coal requirement was to be met indigenously. It was explained that after the application for coal linkage was made and the issue was being discussed with the authorities including CEA, there was an indication that the petitioner would not get 100 % linkage. Therefore the petitioner took it as 70%.

(z) The petitioner did not inform the Haryana Utilities about the source of supply of coal, though as per the PPA, it was one of the conditions to inform the source within 12 months.

4. Shri Anis Dey, the representative of Mercados, the consultant engaged by the petitioner, made a presentation highlighting the financial implications of the increase in price of coal and the steps needed to remedy the situation. The salient features of the presentation are summed up as under:

(a) The capacity charge considered by the petitioner in the bid made for supply of power to Gujarat was lower than that worked out based on prevalent norms of the Commission for cost-plus pricing, primarily because of favourable debt-equity structure considered by the petitioner.

(b) The energy charge was quoted on non-escalable basis to reflect back-to-back arrangements based on GMDC's in principle commitment for supply of coal from Morga coal block, because of which lower energy charges were quoted. Imported coal was factored as a potential fallback option to domestic shortfall after the techno-economic feasibility study.

(c) In case of Haryana there was a difference in tariff because there was a HVDC line, of which transmission charges, transmission losses were factored. The energy charge was based on the assumption of domestic coal and imported coal in the ratio of 70:30. This led to an overall tariff of ₹2.94/kWh.

(d) Non-escalable energy charge was quoted considering the following factors:

(i) Based on the Commission's fuel price escalation index published in October 2006, quoting non-escalable charges led to more competitive bid.

(ii) The Commission's reports indicated that discounts available under long-term contracts were better reflected as non-escalable component rather than escalable one.

(iii) Under the bid conditions, there was restriction to quote energy charge only on one type of fuel even if bid envisaged use of fuel from more than one source.

(iv) There was availability of back-up supply option from Indonesia at predicable price on long-term basis.

(v) The bidders prefer to go for non-escalable rates because apart from having advantages in bid computation it also reflects the control and hedging abilities.

(e) The petitioner's assumptions were consistent with the competitive scenario in the country as reflected in the bids submitted by other project developers such as Essar-Salaya, Reliance Power and Shapoorji Pallonji for other competitively bid projects.

(f) Over a period of time, the basic assumptions changed. GMDC reneged on its commitment for supply of coal from Morga, Coal India was unable to meet the requirement of coal for supply to Haryana because of shortage in the country. Presently, only 35% of coal requirement is met indigenously in case of Haryana and the remaining 65% is met through the coal imported from Indonesia. These factors led to increased dependence on coal imported from Indonesia. Meanwhile, the Indonesian Regulation was enacted which resulted in increase in price of coal.

(g) The increase in supply cost of imported coal, the cost of supply of power to Gujarat has increased ₹1.1/kWh and to Haryana by ₹0.64/kWh.

(h) The actual cost of executing the project is higher than the estimated cost by 10-25% and equity IRR has dropped to 3-5% over life of the plant. Though the petitioner has not asked for a capacity charge revision it does not have the capacity to absorb the increase in capital cost because of increase in price of fuel.

(i) The projected ROE has been substantially eroded because of impact of increase in capital cost and price of imported fuel. The net effect cannot be absorbed/mitigated by the petitioner.

(j) Since 2007 when bids were made there has been increase in capacity charge for the reasons of increase in capital cost from ₹4.4 crore/MW to

₹6.9 crore/MW, weakening of Indian currency *qua* US Dollar, increase in interest rates and removal of benefit of Mega Power Project. In the face of these developments, the capacity charge of Mundra plant is lower by 70%.

(k) Mothballing of Mundra plant even a period of time will lead to widening of power availability deficit in the concerned States; consumers will be affected because alternatives are at much higher prices; lenders will be affected with immediate debt recovery concerns and have a negative impact on investment climate in the two States.

(l) Regulatory intervention is needed to restore the economic foundation of the project to ensure viable operation of the PPAs or to rescind the PPAs because of commercial impractability and frustration.

5. Shri Amit Kapoor, learned counsel for the petitioner referred to the Statement of Objects and Reasons leading to enactment of Electricity Act, certain provisions of the Electricity Act, the competitive bidding guidelines, the national Electricity Policy and the tariff policy. He also referred to the relevant provisions of the PPA, in particular Article 12 (Force Majeure), Article 13 (Change in Law) and Articles 17.1 and Article 17.3 (Dispute Resolution). Learned counsel made the following submissions:

(a) The petition was filed invoking the jurisdiction of the Commission under Section 79 read with Sections 61 to 63 of the Electricity Act and the competitive bidding guidelines, Section 56 of the Contract Act and provisions of the PPAs.

(b) The Commission as an expert body has a statutory mandate to consider the relief claimed in the petition since the Commission as a statutory authority has mandatorily to function to achieve and attain the objectives of the statute.

(c) As laid down in para 2 of the Statement of Objects, the policy and objective of the Electricity Act is to encourage private sector participation in generation, transmission and distribution and to entrust the regulatory responsibility earlier vested in the Government to Regulatory Commissions. Section 3 (1) of the Electricity Act further emphasises the need for development of power system based on optimum utilisation of resources.

(d) Section 61 of the Electricity Act lays down the factors to be considered by the Appropriate Commission while laying down the terms and conditions for determination of tariff. These factors include encouraging competition, efficiency, economical use of the resources, good performance and optimum investments; safeguarding of consumers' interest and at the same time, ensuring recovery of the cost of electricity in a reasonable manner and the principles rewarding efficiency in performance as provided under clauses (c) to (e).

(e) Section 62 empowers the Appropriate Commission to determine tariff. Similarly, Section 63 also refers to determination of tariff by bidding process. Thus, both sections deal with one particular aspect which is determination of tariff. In the first case determination is by regulator and in the second case determination is by bidding process.

(f) Section 63 overrides Section 62 only, but does not override Section 61 or Section 79. The Parliament chose to make two alternatives for determination of tariff by enacting Sections 62 and 63 without taking away the powers of the Commission under Sections 61 and 79. The overarching power is conferred on the Commission under Sections 79 and the tariff principles under Section 61 govern all tariff determinations, whatsoever. In Essar Power case, the Appellate Tribunal also so held.

(g) If Section 63 is given overriding effect *qua* Sections 61 and 79 the result will be that Section 63 denudes the Commission of its power under Section 79 and takes away Section 61.

(h) Section 79 of the Electricity Act does not confer any discretion on the Commission but mandates it to discharge the functions laid down therein. The provision is in consonance with the 2002 judgment of the Supreme Court in WBRC case according to which only a multi disciplinary expert body should be invested with powers in matters of this nature. Accordingly, whole tariff determination process has been left in the hands of the Commission, subject to supervisory powers of the Appellate Tribunal.

(i) Although some spare capacity (556 MW minus transmission losses) is available from Units 7,8 and 9 (Phase IV) (Supply to Haryana) for sale in the open market, the petitioner is presently not in a position to sell until the line gets fully functional which may take a year or so.

(j) There was no reason to believe that the Indonesian law will be enacted in the form of Indonesian Regulation, resulting in increase in prices.

(k) Since the petitioner is procuring coal from Indonesia at $92 per tonne currently as compared to $36 per tonne assumed at the time of bids, the price then prevalent, the petitioner would suffer a loss of ₹790 crore for supply to Gujarat and ₹580 crore to Haryana every year. The present petition seeks relief under the PPA under the *Force Majeure* and Change of Law clauses after enactment of the Indonesian Regulation.

(l) The impact of Indonesian Regulation on Indian power producers was also recognised by Indian Embassy in Jakarta in its report titled “Coal Mining sector in Indonesia”, copy of which was produced.

(m) The competitive bidding guidelines issued pursuant to Section 63 contemplate that after the bid has been put in and the numbers have come out the Commission will continue to play an important role of

oversight. So it is an absolute misnomer to suggest that once Section 63 process is undertaken, for the 25-35 years the Commission has no power over tariff related matters even if the Commission finds compelling reasons for interference.

(n) The competitive bidding guidelines issued under Section 63 cannot be read so as to negate the objectives of the statute or the National Electricity Policy or tariff policy and they have to be interpreted together.

(o) Para 5.17 of the competitive bidding guidelines provides for resolution of disputes other than those falling within the jurisdiction of the Appropriate Commission, by arbitration.

(p) Section 61 further provides the tariff policy and the National Electricity Policy to be considered while formulating the terms and conditions for determination of tariff and this is another fact which has to be borne in mind by the regulator along with financial turnaround, commercial viability of the sector and, protection of consumer interests.

(q) Paras 4.0, 5.2.13, 5.2.17, 5.8 of the National Electricity Policy were relied upon to support the petitioner's contention that the tariff determined through competitive bidding was liable to be reopened if the circumstances so warranted as the tariff could not be kept unchanged for a period of 25 years.

(r) Under PPA there is definition of law according to which law means all laws including Electricity Laws in force India, and the laws interpreted by Indian authority. The interpretation of the term does not exclude Indonesian law when the entire project is predicated on imported coal or bid is predicated on imported coal.

(s) Renegotiation of long-term contracts is the worldwide accepted principle where external, uncontrollable factors have impacted the viability of the project.

(t) The principles of interpretation of the contract are that it will be interpreted in a manner that gives business efficacy and in case two interpretations are possible it will always be interpreted against the party which had drafted or controls the document. The PPAs were drafted by the respondents as the procurers and are to be interpreted against them in case the principle of commercial viability cannot be applied in the present case.

(u) The Panama Canal case relied upon by the respondents is not applicable in the present case. In Panama Canal case a particular ship carrying a particular shipload was prevented from going through a shorter route and was asked to travel by a route three times longer for a limited duration. In Panama Canal case there was a declaration of war for a few months after which it would have been lifted. The present petitioner has in two PPAs tied up 85% of the installed capacity for 25 years. What Indonesia has

enacted is not a regulation that is for next 3 months. The petitioner loses day in and day out.

6. At this stage the Commission adjourned the case for hearing on 7.2.2013 at 2.30 PM.

By Order of the Commission

Sd/-
(T Rout)
Jt. Chief (Law)