CENTRAL ELECTRICITY REGULATORY COMMISSION

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PRESS RELEASE

CERC Announces Final Regulations for Terms and Conditions for Electricity Tariff for the Five - Year period beginning April 1, 2004.

The Electricity Act, 2003 requires the Central Electricity Regulatory Commission (CERC) as the principal regulator in the Electricity Sector, to specify the Terms and Conditions for determination of tariff for generation and inter-state transmission. The existing Regulations covering the period 1.4.2001 to 31.3.2004 are due to expire on March 31, 2004. Accordingly, it is essential that new Regulations should be put in place, effective from April 1, 2004.

2. The Commission on 12th June, 2003 floated a Consultation Paper prepared on Terms and Conditions of Tariff, for comments from stakeholders, experts, investors, State Commissions, financial institutions etc. This was followed by open hearings on 10th, 11th & 12th November, 2003 in which all the stakeholders and other experts participated. Based on the outcome of these hearings, the Commission issued its Draft Regulations and a detailed Order, in January, 2004. The Commission held another consultation with the stakeholders through a public hearing on 9th & 10th March, 2004.

3. Based on this elaborate exercise, CERC has today issued the Final Regulations containing Terms and Conditions of Tariff for generation and inter-state transmission. Keeping the spirit of the Electricity Act, 2003 which lays the foundation for new unbundled power sector functioning in a competitive environment, the Commission has emphasised the following:

i) **All future projects and new investment in generation, transmission and distribution both by public sector utilities as well as IPPs should be structured through a tariff-based transparent competitive bidding process**, so that the benefits of increased economic efficiency are passed on to the customers. This would also obviate the need for detailed regulation based on the existing “cost plus approach” which leads to inefficiencies and lack of initiative for better performance. Guidelines for competitive bidding should be announced by the Government as early as possible.

ii) During the period of transition to a competitive bidding regime, **tariff regulation as far as practicable, should move away from the “cost plus actuals” approach, to a new regime of light-handed regulation based on normative parameters**. This would incentivise efficiency and streamline tariffs. **This is the direction in which the Commission has moved. The change-over from intrusive regulation involving detailed scrutiny of actual costs to a lighter regime of normative parameters is the distinctive feature of the new regulation.**

iii) Keeping in view the need for setting multi-year tariff norms **for regulatory certainty, the Commission has prescribed the Terms and Conditions for a five-year period from April 1, 2004 to March 31, 2009,** as against the existing regulations, which cover a three-year period.

iv) The Act envisages that the tariff parameters should **encourage competition, efficiency, economical use of resources**, good performance and optimal investment, **while safeguarding consumer interest.** All these parameters have been kept in view while framing the Regulations.

4. The terms and conditions finalised by the Commission now will apply to all inter-State Generating and Transmission utilities including NTPC, NHPC, POWERGRID, NEEPCO, Neyveli Lignite Corporation, Satluj Jal Vidyut Nigam and the relevant IPPs.

5. Projects which are taken up through a transparent tariff based bidding process as per the guidelines of the Central Government shall be examined in accordance with the guidelines, and tariff arrived at through the bidding process shall be adopted by the Commission. These Regulations shall not apply to such projects.

6. The **salient features** of the new Regulations are as follows:

- The **Capital Cost** of all projects shall be as admitted by the Commission.
- The **normative Debt : Equity ratio** would be 70:30.
- The **Return on Equity** shall be 14% post tax across the board, and this shall be uniformly applicable to the CPSUs and the IPPs.
- **Depreciation** shall be allowed over the fair life of the assets at the rate notified by the Commission. In addition, advance against deprecation shall also be allowed to meet debt service obligations by considering the repayment period of loan as 10 years. While determining the advance against depreciation, cumulative depreciation recovered shall also be compared with the cumulative repayment made.
- **Working capital** shall be allowed on normative basis, and rate of interest applicable shall be the Short Term Prime Lending Rate of State Bank of India.
- **Income tax on the core activity** of the utility shall be reimbursable by the beneficiaries and shall be adjusted subsequently based on the income tax assessment by the IT Authority under the Income Tax Act, 1961.
- **Development surcharge** has been discontinued.

- **Performance benchmark** of availability in terms of capacity index has been raised from 85% to 90% for **purely run of the river hydro power stations** (existing as well as new).
- **Incentive benchmark for thermal generating stations** has been raised from a plant load factor of 77% to 80%. Rate of incentive has been increased to 25 paise per unit from the existing 21.5 paise per unit.
- Target Availability and incentive benchmarks for existing **Lignite based power stations of NLC** increased from 72% to 75%.
- **Efficiency benchmark for coal based thermal generating units** of 500 MW has been revised to 2450 kcal/kWh from 2500 kcal/kWh.
- **A separate higher efficiency benchmark** of 1850 kcal/kWh has been specified **for advance class gas turbine stations,** whereas for other new gas turbine based generating stations the efficiency benchmark has been revised to 1950 kcal/kWh from 2000 kcal/kWh. However, the norms for small gas turbine stations have not been changed.
- **Specific oil consumption norm** has been revised to 2 ml/kWh from 3.5 ml/kWh for coal based stations, and for lignite based stations, the norm has been revised to 3 ml/kWh from 3.5 ml/kWh.
- For generating stations using coal or lignite as fuel, the **norms for auxiliary energy consumption** within the power station have been reduced by 0.5 percentage point across the board.
- Normative benchmark has been set at 0.3% and 0.8% for **transit and handling losses of coal** in respect of pit head and non pit-head coal based power stations, respectively.
- Normative benchmarks have been set for **Operation and Maintenance expenses** to be payable to thermal generating stations and transmission licensees.
- **Target availability for A.C transmission system and HVDC transmission system** have been separately specified as 98% and 95% respectively instead of 98% on overall basis.
- The maximum **rate to be charged for Unscheduled Deviations (UI charges)** from the generation or energy drawal schedules has been revised upwards from Rs.4.20 to Rs.6.00 at 49 hertz with a view to further improving grid discipline.

7. CERC's new Regulations announced today are expected to benefit the power sector in several ways, including the following:

a) The Act prescribes that **the State Electricity Regulators shall be guided by the principles and methodologies prescribed by CERC. This would lead to greater harmonisation, uniformity and certainty in electricity regulation across the States.**

b) The new Terms and Conditions of tariff finalised by CERC are **likely to result in some reduction in bulk electricity tariffs,** since the norms for servicing capital investment have been fine tuned with the current financial scenario and the benchmarks of efficiency have been raised. It would enable the State regulators, who determine the retail electricity tariffs, **to pass on the benefit to the ultimate consumer.**

c) Simultaneously, CERC **has created an investor friendly environment** by moving to light handed regulation based on normative parameters as far as possible, and carefully crafted the norms in a manner which allows an efficient enterprise to earn additional returns through savings and incentive.

8. The Availability Based Tariff (ABT) mechanism was adopted by the CERC during the last tariff period and has been successfully implemented across the whole country at the regional/inter-state level. ABT incentivises grid discipline and reliability of supply through frequency linked pricing mechanism and has brought about remarkable improvement in grid discipline at the regional level**. CERC has decided that ABT would be continued during the new tariff period**. **The Commission expects that** the ABT mechanism would be taken to its logical conclusion and **the State regulators would extend it to intra-state level in the near future.**

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(A.K.Sachan)
Secretary