COMMENTS ON DRAFT CERC REGULATIONS 2019-2024

Quarterly plant availability factor and plant load factor

Consideration of Normative Plant Availability Factor and Normative Plant Load Factor on a quarterly basis is a welcome step. It will ensure that the plants are available as and when required and non-availability of plants during the period it is required is not covered up in other quarters.

As the maintenance related shutdowns which reduce 7-8% of PAF are not included for calculating PAF, there is no reason to lower normative availability factor to 83%. It should atleast be increased to 85% in light of new technologies and ability for plants to predict failures.

Computation and payment of capacity charges for thermal generating stations

Segregation of charges into peak and off peak period will be a cumbersome process. Further, it is proposed to consider the regional peak and off peak for the same.

Most of the States have become power surplus now a days and further, regional peak rarely coincides with state peaks, therefore linking tariff with ToD blocks of Region would not serve any purpose. Rajasthan, for instance, gets its peak at a very different time than the other states in northern region and will be loaded with peak charges despite of not having peak demand. As such, the same is strongly opposed.

Further, if capacity charges are linked with peak and off-peak periods, providing for different incentives for peak and off-peak period is also not required.

Computation and payment of energy charges

Incentive proposed of 65 paise/kWh during peak hours and 50 paise/kWh during off peak hours is too high. The incentive during peak should be limited to 50 paise/kWh while during off-peak should be limited to 30 paise/kWh. The incentive is linked to PLF of stations. The beneficiaries may not be aware of the PLF for the period when they are scheduling their energy and as such will not be in a position to correctly anticipate the merit order. Not accounting for such incentive while scheduling will lead to deviation from merit order principles.

At this juncture of time, when most states are in power surplus, it is very much possible to schedule power from other stations to avoid this incentive in case all information regarding PLF and if incentive will applicable will be applicable on the scheduled energy is readily available.

As such, incentive should ideally be removed from per unit cost and other means may be explored.

Return on Equity

Return on Equity should have some linkage with the risk involved in the sector as well as the prevailing market conditions.

CERC in its consultation paper issued on draft tariff regulations had rightly pointed out the need to reduce RoE in line with market dynamics, lending rates and other prevailing factors discussed in the consultation paper itself. The RoE should be market driven and therefore linked with lending rates. In line with directives of RBI on fixed lending rates, RoE may be linked with MCLR (Marginal Cost of Funds based lending rate) or with the G-Sec rates (risk free return).

The proposed rate @ 15.5%/16.5% is too high and has no justification. The time at which these rates were fixed, there was a dire need of investment in the sector along with high interest rates.

Even in the case of wind and solar projects, where risk involved is considerably higher, a return of 14% is considered. Similarly return in case of generation should also be brought down to 14% while it could be further lowered to 13% in case of transmission projects considering the lower risk involved.

Depreciation

The Commission has proposed to reduce the salvage value from 10% to 5% in line with the companies act. Consideration of salvage value of 5% may be appropriate in other industries, however, in case of power sector where majority of project cost is towards the use of metal such as steel, iron, copper, aluminum, etc. this reduction is not logical.

The cost of such metals only escalates over time. For example, a coal based power plant constructed in 1988 costed 0.50 Crore per MW and cost of the same plant after 25 years is around Rs. 6.0 Crore/MW i.e. an increase of around 12 times. Similar is the case for transmission system. Any conductor can be melted and recast into a new conductor. The salvage value of such much metallic items is easily in the range of 30%-40%. As such, a study may be conducted to check the market value of equipment after their useful life considering the initial price as well as market escalation in the price of metals. Till such time, the existing norm of 10% salvage value may be continued.

Debt Equity Ratio

The Commission has proposed to reduce the equity component by the accumulated depreciation less the cumulative repayment of loan. This is a welcome step.

However, it is pertinent to mention that with the existing norms of 70:30 debt equity ratio and the depreciation rates, the entire debt is paid off in 13 years by the provision of depreciation. From 13th year onwards, depreciation is still provided as part of the tariff component and no benefit is passed on to the beneficiaries. Further, in case any additional capital is required during the period of 14th year till the end of useful life, that is also allowed by the commission to be passed through as tariff. The depreciation should be utilized to fund that additional capitalization.

Interest on working capital

The Commission has proposed to reduce the working capital requirement by reducing the allowed cost of coal from 30 days to 20 days in case of non-pit head generating stations. It is pertinent to highlight that coal shortage is being experienced throughout the nation and despite best efforts put in by the coal companies, coal shortage is envisaged in the coming years as well. In such a scenario, when the coal availability is not certain the proposed provision will only fictitiously increase tariff without actual purchase of coal and will increase tariff. As such, the provision may be suitably amended to account for such scenarios and allow cost of coal on normative basis or actually utilized.

Transit Losses

The transit loss norm has been proposed to be revised by introducing distance slabs for non-pit head generating stations. The slabs may be further modified to ensure efficiency is not compromised.

	Existing	Proposed in draft regulations	New Proposal
Pit Head	0.20%	0.20%	0.20%
Non-Pit Head	0.80%	Upto 1000 km: 0.80% Above 1000 km: 1.20%	Upto 500 km: 0.50% 500 to 1000 km: 0.80% > 1000 km: 1.20%

In case of imported coal, the existing provision may be continued instead of replacing with the norms for non-pit head generating station.

Operation and Maintenance Expense

Normative O&M expenses have been proposed for various type of generating stations. However, the age of the station has not been accounted for. In absence of analysis of impact of age on O&M norms, the proposed norms should only act as a ceiling limit. In case actual expenditure is less than the proposed norm, the same should be passed on or shared with the beneficiaries.

Further, the definition of O&M expenses already include water charges and security expenses while at page 78, the same have been allowed separately. The discrepancy should be removed.

Auxiliary energy consumption

Old provision may be retained as increasing AEC will indirectly reward, support and promote inefficiency. Moreover, with improved and more efficient machine designs and availability of better motors, AEC is expected to further reduce.

Sharing of non-tariff income

While clause on sharing of non-tariff income has been newly introduced in the CERC regulations, it is already in existence in almost all of the state regulations. The non-tariff income derived from all the sources specified in the regulation is used to reduce the ARR of the generating company or the licensee. As such, instead of sharing of such income in the ratio of 50:50, full benefit of the same should be passed on to the beneficiaries.

Non-Tariff Income can also be divided in two heads– one which is incidental to the business – such as Income from Sale of scrap, Income from statutory investments etc, and second where income is dependent upon the effort put in by the generator/transmission licensee for generating non-tariff income, such as Income from rent of land or building, rental from contractors, Income from advertisement etc.

It is suggested that the income coming under the first head should be reduced 100% from the ARR of the generating plants/transmission licensee, while income from the second head should be shared in 75:25 ratio in favor of long term customers.

Sharing of clean development mechanism benefits

While determining the tariff, cost of all the items to ensure meeting emission standards is always included and passed on for payment by the beneficiaries. To meet the end of justice, the income derived from these benefits may also be passed on in full to beneficiaries. As such, the proceeds of carbon credit from approved emission reduction projects under Clean Development Mechanism shall be passed on in full to beneficiaries

Rebate

The Commission has proposed to continue with the existing methodology of Rebate. The stakeholder submits that the Commission should allow 2% rebate for payment within 5 days after presentation of the bill. Further, the rebate should be reduced per day on graded basis instead of reducing from 2% to 1% and 1% to zero in line with the methodology followed for Late Payment Surcharge.

Late Payment Surcharge

The Commission has proposed to reduce the late payment surcharge @1.25% per month instead of 1.5% prevalent in current regulations but has proposed to levy the same after 45 days from the date of billing instead of 60 days.

It is submitted that the late payment surcharge may be linked to the bank rate as in the case of interest on working capital. Delay in payments result in increased requirement of working capital and as such it is only justifiable to link it with the interest on working capital. LPS should not be treated as a financing mechanism.

Bank Rate

The Discoms are of the view spread on rate of interest on working capital should be reduced as Interest cost has been falling in the country. The Spread should be 2.50% above SBI MCLR instead of the proposed 3.5%.

Alternative source of fuel

The Commission has proposed to continue with the existing methodology for allowing usage of alternative source of fuel by the generating plants. As the fuel availability is the responsibility of the generating stations, such provision is important. However, the Commission may consider reducing the cap from existing 30% to 15% and prior consultation with beneficiaries may be mandated beyond that. This will ensure that Discoms are not getting any surprise in the power purchase cost.

Determination of Tariff

*"Where the capital cost considered in tariff by the Commission on the basis of projected additional capital expenditure exceeds the actual additional capital expenditure incurred on year to year basis by more than **10%**, the generating company or the transmission licensee shall refund to the beneficiaries or the long term transmission customers as the case may be, the tariff recovered corresponding to the additional capital expenditure not incurred, as approved by the Commission, along with interest at 1.20 times of the bank rate as prevalent on 1st April of the respective year."*

The Commission has proposed to increase the limit from 5% to 10%. The projected capital expenditure should be as close to the actual expenditure as far as possible. However, to take into account any deviations in projection, 5% limit is prescribed in the existing regulations is more than adequate. Proposed increase of this limit to 10% will encourage Generating Company/ Transmission Licensee to project inflated capital expenditure in order to retain increased tariff at the cost of the end consumers. Ideally, the regulations should be made stringent and encourage the developers to estimate expenses correctly. As such, <u>any reduction in the actual expenditure as compared to the proposed expenditure should be passed on to the beneficiaries irrespective of the quantum of difference.</u> <u>Any variation above 5% should be passed on along with interest at 1.20 times of the bank rate as prevalent on 1st April of the respective year.</u>

On similar lines, the proposed regulation given below also needs to be amended.

"(9) Where the capital cost considered in tariff by the Commission on the basis of projected additional capital expenditure falls short of the actual additional capital expenditure incurred by more than 10% on year to year basis, the generating company or the transmission licensee shall recover from the beneficiaries or the long term customers as the case may be, the shortfall in tariff corresponding to difference in additional capital expenditure, as approved by the Commission, along with interest at the bank rate as prevalent on 1st April of the respective year."

The beneficiaries have no direct role in projecting the capital expenditure for the project. As such, the developers should be encouraged to estimate capital cost correctly. <u>However, any variation to the extent of 5% may be recovered from the beneficiaries along with interest at 0.80 times the prevailing bank rate but any expenditure above this variation should not be allowed as a pass through.</u>

Special provisions relating to BBMB and SSP

Under clause 83 of the draft regulations, special provision for tariff of generating station and the transmission system of Bhakra Beas Management Board (BBMB) and Sardar Sarovar Project(SSP) has been mentioned.

In this regard it is submitted that the projects under BBMB complex were set up jointly by the partner states on cost sharing basis and power is being shared as per agreement between partner states. There is no sale of power from these projects to any partner states, and hence the requirement of determination of tariff does not arise. The provisions have already been incorporated in Punjab Reorganization Act, 1966 to meet out and share the expenses of cost of generation by the partner states.