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PRESS RELEASE

CERC Announces Draft Regulation for Terms and Conditions for Electricity Tariff

The Electricity Act, 2003 came into force with effect from 10th June 2003. The Act has been hailed as a revolutionary piece of legislation which promises to usher a new era in India's power sector. The Central Electricity Regulatory Commission (CERC) being the principle regulator in the Electricity Sector took the lead in moving forward to implement the various provisions of the new Law in letter and spirit. The first action in the series was taken on 12th June, 2003 by floating a Consultation Paper prepared by the staff of the Commission, on Terms and Conditions of Tariff. The Consultation Paper evoked enthusiastic response from stakeholders, experts, investors, State Commissions, financial institutions etc. Carrying forward the debate further, open consultations were held with all the stakeholders and experts on 10th, 11th & 12th November, 2003.

2. As a result of this exercise, CERC has today issued a new set of draft regulations containing Terms and Conditions of tariff for generation and transmission. Keeping the spirit of the Electricity Act, 2003, the Commission has emphasised the need to move away from the cost plus regulatory regime to a new regime of lighter regulation. The Commission would like all projects to come through competitive bidding route in future to harness the benefits of increased economic efficiency and ensuring that electricity prices are in line with costs. However, it will take sometime before the sector can move to a fully competitive regime. The Commission has urged the Central Government to issue the guidelines for competitive bidding as required under Section 63 of the new Electricity Act. This would remove the need for detailed regulation.

3. Besides, the Commission is aware of the fact that these regulations will also act as guidelines for all the State Commissions in respect of generation and transmission tariff. The Commission has given due consideration to the prevailing conditions of the sector at the state level while framing these regulations.

4. The Electricity Act envisages multi year tariff principles and accordingly Commission's new norms would be applicable for a period of five years i.e. during the period 1.4.2004 to 31.3.2009. This provides enough regulatory certainty to all concerned parties. The Act also envisages that the tariff

parameters should encourage competition, efficiency, economical use of the resources, good performance and optimal investment and at the same time safeguard consumers' interest. All these parameters have been kept in view by the Commission while formulating the norms for different parameters of the generation and transmission sectors.

5. The new terms and conditions will apply to all inter-State Generating and Transmission utilities including NTPC, NHPC, POWERGRID, NEEPCO, Neyveli Lignite Corporation and Satluj Jal Vidyut Nigam. **The changeover from intrusive regulation involving detailed scrutiny of various actual costs to light handed regulation based on normative parameters of performance is the hallmark of the proposed new regulation.** Regulation based on normative parameters leads to higher efficiencies by creating incentive for the utilities to achieve savings by performing better than the normative benchmarks of performance.

6. The new terms and conditions of tariff will be applicable only to projects taken up on cost plus basis. As regards projects which came up through a transparent tariff based bidding process as per the guidelines of the Central Government, the tariff shall be adopted by the Commission.

7. The salient features of the new regulations are as follows:

- **For new projects the capital cost shall be as admitted by the Commission and the normative debt equity ratio would be 70:30.** The capital cost and debt equity ratio of all the stations and transmission lines for which tariff has been approved by the Commission prior to 1.4.2004, shall be continued during the next tariff period as well.

- **The return on equity for the CPSUs is pegged at 14% post tax as against the existing 16% post tax. In case of Independent Power Producers (IPPs), the return on equity shall be 16% post tax.** However, in case the Government provides the same payment security mechanism as extended to CPSUs, the return on equity for IPPs shall also be pegged at 14% post tax.

- **Depreciation shall be allowed over the fair life of the assets at the rate notified by the Commission. In addition advance against depreciation shall also be allowed to meet debt service obligations and the repayment period for the loan shall be considered as 10 years instead of the existing 12 years.**

- **Working capital shall be allowed on normative basis and the rate of interest applicable shall be the Short Terms 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.

- **The existing provision regarding Development surcharge for taking up new capacity additions shall continue for the next 5 years.**

- **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 existing 21.5 paise per unit.**

- **Performance benchmarks of normative auxiliary power consumption and fuel oil consumption have been revised for coal fired power stations.**

- **Normative benchmark has been set at 0.3% and 0.8% for transit and handling losses of coal in respect of pit head and rail fed coal based power stations, respectively.**

- **Normative benchmarks have been set for operation and maintenance expenses to be payable to generating and transmission utilities**.

- **Higher normative efficiency benchmarks in terms of station heat rate have been fixed for existing and new thermal power stations.**

- **Rates to be charged for unscheduled deviations from the generation or drawal schedules have been revised upwards with a view to further improving grid discipline.**

8. All interested persons have been requested to send their comments on the Draft Regulations by 23.1.2004.

9. The regulations will be finalised and notified well before 1.4.2004 after taking into account the comments of the stakeholders, and they will be valid for a period of five years.

10. These regulations have been published and posted at CERC's web site **http://cercind.org**.

(A.K. Sachan)
Secretary

Power regulator for new price model

Anil Sasi in New Delhi | July 21, 2003 09:59 IST

With a view to ensuring that promoters source funds at optimum cost, the Central Electricity Regulatory Commission has asked the Industrial Development Bank of India to work out the broad guidelines for using the return-on-capital-employed approach to determine power tariffs.

Tariffs are now set by factoring in both the return on equity and the interest on loans.

The move to ask the IDBI to submit a proposal on the merits of having a single rate of return for the calculation of tariffs and suggestions on the rate itself followed a meeting of the CERC's Central Advisory Committee on July 18.

The meeting was attended by P P Vora, chairman of the IDBI, C P Jain, chairman and managing director of the National Thermal Power Corporation, Anil Ambani, vice-chairman and managing director of Reliance, Phiroz Vandrevala of Tata Power and representatives from industry chambers and consumer groups.

In the build-up to setting new tariff norms for central power utilities and inter-state private projects, the CERC had asked the various stakeholders to comment on improvements to be brought about in the existing tariff norms.

Some of the suggestions received have already been incorporated in the discussion paper floated by the CERC and will be formulated under the "terms and conditions of tariff order" for central utilities from April 1, 2004.

The advantage of determining tariffs based on a single rate for return-on-capital-employed over having two separate rates for interest on loan and return on equity is one of the suggestions received from stakeholders.

The benefit of having just one rate of total investment, say a 12 per cent on return-on-capital-employed, rather than having a 16 per cent return on equity and a separate rate of interest on loans to be passed on to the tariffs, is expected to force promoters of projects to rethink the financing structure, including the debt-equity ratio and the rate at which they source the debt portion.

At present, the 16 per cent return on equity and the interest on loans are passed on to the tariffs, giving promoters the luxury to source loans at relatively high rates of interest.

"The committee stressed the need for simplicity of regulation, uniformity in orders of the central and state regulatory commissions and speedy disposal of orders," CERC Chairman A K Basu said.

On other parameters of tariff fixation, the committee advised the CERC on retaining the present three-year tariff period and allowing operational and maintenance expenses to utilities to recover only 'prudent costs,' he said.

In the responses submitted to the CERC by stakeholders earlier, the option of changing over from the present system of a three-year tariff regime to a four-, five- or 10-year one was suggested.

There was also a suggestion on the need to have a one-time tariff and indexing of financial parameters like return on investments to the annual inflationary trend.

The rate factor

- Tariffs are now set by factoring in both the return on equity and the interest on loans.
- CERC had asked stakeholders to comment on improvements to be brought about in the existing tariff norms.
- The benefit of having one rate of total investment rather than a return on equity and a separate rate of interest on loans can force promoters to rethink the financing structure.

CERC proposes new investor-friendly tariff

Sanjay Jog
Posted online: Thursday , December 13, 2007 at 2345 hrs IST

Mumbai, Dec 13 Power sector investors, both domestic and foreign, may be in for a good time, as the Central Electricity Regulatory Commission (CERC) has proposed a slew of changes in terms & conditions of tariff for the period commencing from April 1, 2009.

The CERC had specified the terms & conditions of tariff for April 1, 2004, to March 31, 2009, under the provisions of Section 61 of the Electricity Act, 2003. However, it has decided to give a fresh look into the bases and assumptions to be considered while framing the fresh terms & conditions of tariff in view of many changes and developments in power and financial sectors.

The power regulator has proposed to replace the return on capital employed (ROCE) approach by return on equity (RoE) approach.

" With the listing of major power utilities on stock exchanges, permission of 100% FDI in power sector, development of debt market in India, stabilising trends of interest rate and accessibility of Indian Companies to foreign market for debt and equity, the ground situation has changed to a great extent. As such, a fresh look is required to be given towards the approach for rate of return, that is, whether RoE approach vis-à-vis ROCE approach,”   CERC said in its approach paper which has been circulated for suggestions.

CERC had specified a post tax RoE rate of 16% for the tariff period 2000-04 and 14% for the tariff period 2004-09. CERC wants to know whether it needs to be revised considering the present equity market expectation, risk perception of power sector. Whether CERC should adopt a fixed rate of return (as has been followed in the past), or to link the rate of return to market rate considering the risk perception. If rate of return is to be linked to market rate, the power regulator has asked suggestions on criteria to be adopted for arriving at the rate of return.

According to the CERC, profit of the utilities be equal to RoE specified as all other elements of tariff are based on the general premise of pass through. However, profit is influenced by a slew of other factors such as non-core business carried out by the utility, unscheduled interchange earnings, efficiency gains, incentive earned.