



Comments
by
Powerlinks Transmission Limited
(A JV of Tata Power & POWERGRID)
on
Draft CERC
(TERMS & CONDITIONS OF TARIFF)
Regulation 2008

November 3-4, 2008



Depreciation including AAD- Clause 17.4 a



	Depreciation Rate	No of Years	Total Depreciation
Existing	2.57%	35	90%
Proposed	4.67%	15	70%
	1.00%	20	20%

Depreciation including AAD- Claus

17.4 a



Concerns

- AAD discontinued
- 70% depreciation allowed in 15 years
- Difficult to get debt from Lenders with matching repayment schedule (15+3 yrs moratorium)
- Higher tenure makes loan costlier

Comments

- Increase depreciation rate to 5.84% for initial 12 years to facilitate recovery of debt portion

Incentive – Clause 23



Concerns

- Calculation of Incentive - change of base from % of equity to % of annual transmission charges.
- Discontinuation of reimbursement of tax on the incentive amount

Comments

- Changing base reduces incentive amount
- Insignificant incentive will defeat purpose of increasing availability
- Tax to be reimbursed on the incentive amount also
- Older system needs more expenses to keep system healthy enabling increased availability

Rebate – Clause 34



Concerns

- Rebate allowed on all the bills of transmission licensee

Comments

- To exclude bills of income tax, FERV etc. as these are reimbursable expenditures

Interest on Loan Capital- Clause 16(7)



Concerns

- Benefit due to refinancing – Sharing Ratio: 2:1

Comments

- To encourage such efforts – Sharing Ratio should be: 1:1



Long Term Transmission Customer- (LTTC) Clause 25

Concerns

- Proposed definition of LTTC envisages long term lien on the transmission system

Comments

- Existing definition of LTTC to be retained as Lenders raise objections for long term lien by the customers

Benchmark Norm-Clause (8)



Concerns

- Benchmark norms to be published for Capital Cost

Comments

- Benchmarking of capital cost per Km. of the transmission line would be difficult as it is dependent upon terrain, number of river crossings, forest clearance etc.
- Existing methodology subject to prudence check should be continued

Initial Spares Clause 9(iv)



Concerns

- Reduction of Initial Spares Capitalisation from 1.5% to 0.75% of the Project Cost

Comments

- Initial spares are required for repair and maintenance after commercial operation due to unforeseen reasons. Existing norm of 1.5% to be continued

Additional Capital Expenditure Clause 10(ii)



Concerns

- Deletion of the clause regarding capitalization on account of additional work / services which have become necessary for efficient and successful operation of the project but not included in the original project cost

Comments

- Certain expenditure not envisaged earlier may be necessary
- Existing Clause to be retained
- Additional capitalization is subject to prudence check by CERC

Interest on Working Capital- Clause 18



Concerns

- Receivable reduced from 60 days to 45 days
- Computation of spares changed from 1% of the project cost to 15% of the O&M expenses
- Norm for one month O&M expenses discontinued

Comments

- Leads to abnormally low working capital, which would jeopardize the normal business operation
- Existing provision to be continued

Return on Equity- Clause 15



Concerns

- ROE has been retained as 14% p.a. though the interest rates have increased from 10% in 2004 to 14% in 2008
- Proposed ROE has been linked with Capital Market conditions

Comments

- To maintain the consistency, ROE need to be linked to prevailing interest rate & pegged at 18%

Return on Equity - Clause 15 (Contd.)



Concerns

- ROE from COD
- Interest on debt during the construction phase allowed as IDC, however, there is no return on equity during the construction phase

Comments

- Normally equity is invested prior to loan disbursement
- Non receipt of ROE during construction further erodes effective ROE

Operations & Maintenance Expenses



Clause 19

Concerns

- Fixation of O&M exp on the basis of per Km instead of per Ckt KM
- Annual Increase based on the Inflation of 5% p.a.
- O & M exp benchmarked on the basis of data provided by CPSU only
- Proposed change would further reduce the O&M amount drastically

Comments

- Annual increase to be based on average inflation prevailing during the concerned year

Operations & Maintenance Expenses



Clause 19

Comments

- JVs would be maintaining limited network of transmission lines and as such its expenses cannot be compared with Powergrid, which enjoys economies of scale
- Powergrid maintains both transmission lines and substations
- Non-recovery of actual bonafide O&M expenses to further reduce returns
- Proposed change would discourage private investors to participate in development of Transmission Sector

Operations & Maintenance Expenses



Clause 19

Comments

- We strongly recommend O & M expenses as under:
 - Transmission Lines – up to a maximum of 1.5% of the Gross Block
 - Substations – up to a maximum of 3% of the Gross Block
- above subject to actual expenses incurred by the transmission licensee

CDM - Clause 36 (b)



Concerns

- CDM benefits to be shared with the Beneficiaries
- Registration with UNFCCC is essential to avail CDM benefit which involves expenses on account of registration, appointment of consultant, appointment of validator etc.

Comments

- Expenditure also needs to be shared

License Fees - Clause 42



Concerns

- License fees during construction phase is capitalised, however, during O&M phase it is not reimbursed

Comments

- License fee be recovered by the transmission licensee directly from the long-term customer during O&M phase
- Should be part of Tariff Regulation & not discretionary

Cut Off Date - Clause 3(13)



Concerns

- Extended cut off date shall be applicable provided project achieves COD in last quarter of the financial year

Comments

- The relaxation of enhanced cut off date be extended to projects declaring COD in the second half of the financial year

Definition of Core Business- Clause (12)



Concerns

- Core business means business of generation or transmission of electricity. (No specific exclusion now)

Comments

- Existing regulation specifically excludes other business or activity like consultancy, telecommunication of the transmission licensee
- Existing definition to be continued



Thank You!

COMMENTS ON DRAFT CERC(TERMS & CONDITIONS OF TARIFF) Regulation 2008

S.No.	Pg. No.	Clause No.	Comments
1.	3	3(13)	<p>Cut-off Date: In the Regulation 2008, cut-off date has been extended to 31st march of the year closing after two years of the year of commercial operation in case the project is declared under the commercial operation in the last quarter of a year.</p> <p>As the intention is to give the extended time for completion of the balance works, we suggest that extended time shall be applicable to projects declared under commercial operation in the 2nd half of the year instead of just last quarter of the year.</p>
2.	3	12	<p>Core Business: In the Regulations 2004, Core business specifically excludes consultancy, telecommunication of the generating companies and transmission licensees. However, in the present regulations, core business means business of generation or transmission of electricity. It is not clear whether consultancy business or any other activity related to transmission of electricity come under the purview of core business.</p>
3.	8	25	<p>Long Term Transmission Customer: In the Regulation 2004, Long Term Transmission Customer means a person availing or intending to avail access to the inter state transmission system for a period of 25 years or more. In the Regulation 2008, it defines as a person having a long-term lien over an inter-state transmission system by virtue of paying transmission charges. As a transmission utility or generating company, is required to obtain loan for the project, the Lenders may raise objection in case Long Term Transmission Customer is having a lien over the asset created by the generating company or the transmission utility. It is suggested that old definition of long-term transmission customer may be retained.</p>
4.	15	6 (vii)	<p>Six Months Monthly Installment: In the Regulation 2008, the amount of under recovery or over recovery be recovered or paid by the generating company or transmission licensee in 6 equal monthly installments starting within 3 months from the date of tariff order. From the point of view of generating company or transmission licensee, in case of under recovery, they have to wait for effectively 9 months to get the full tariff amount. Though CERC has proposed that long term transmission customer shall have to pay interest at the rate of short term prime lending rate of SBI, it would be difficult for the transmission licensee to discharge the obligation of the lenders & its promoters. Moreover the interest on long-term debt is more than the rate of short-term prime lending rate of SBI.</p>

5.	17	8	<p>Benchmark Norm: CERC in the Regulation 2008 mentioned that prudence check of the capital cost is to be based on the benchmark norm to be published separately by the Commission from time to time. The capital cost per Km. of the transmission line is dependent upon the terrain, pile foundation, right of way, forest clearance and so many other divergent issues. It would be very difficult to compare this cost on the benchmark norm unless the benchmark norm is clear, exhaustive. It is suggested that the existing methodology of cost plus projects subject to prudence check shall be continued.</p>
6.	19	9 (iv)	<p>Initial Spares: The initial spares to be capitalized have been reduced from 1.5% of the original project cost to 0.75% of the original project cost. The initial spares have to be used for repairing and maintenance of the transmission line which may be immediately required after commercial operation due to any unforeseen reasons. Therefore, we strongly feel that limit of initial spares to be capitalized be kept at existing norm of 1.5% of the original project cost in case of transmission line.</p>
7.	20	10 (ii)	<p>Additional Capital Expenditure: An important provision which takes care of the unforeseen but justified expenditure stating that “any additional work/services, which have become necessary for efficient and successful operation of the project but not included in the original project cost” have been removed in the Regulation 2008. There may be certain situation where in the interest of the project, the transmission or generating companies have to incur certain expenditure, which were not envisaged at the time of approval of the original project cost. CERC should retain this provision as CERC has the power to examine the prudence for incurring expenditure under this head. Otherwise, we suggest that CERC may allow certain percentage of project cost on normative basis as has been done in the case of generating companies to meet the unforeseen expenditure which become critical for the successful operation of the project.</p> <p>The recent unforeseen damage happening to the transmission towers due to change of course by the Kosi river may result in certain extra-ordinary expenditure, which needs to be incurred beyond the normal O&M expenses. It is submitted that as such expenses are neither covered by the Insurance nor can be incurred out of the normal O&M expenses allowed, the same shall be allowed as expenses under force majeure situations.</p>

8.	23	16(7)	<p>Interest on Loan Capital: It is proposed that the net benefit arising out of refinancing shall be shared between the beneficiary or long-term transmission customer and the generating company or the transmission licensee in the ratio of 2:1. Since the generating company or the transmission licensee has to initiate action and put in lot of efforts for refinancing of the existing debt, it is suggested that the net benefit be shared equally by the beneficiary company and the transmission licensee to encourage generating company or the transmission licensee to make an efforts for refinancing.</p>
9.	24	15	<p>Return on Equity (ROE) : ROE has been retained as 14% p.a. In Regulation 2004, where in the ROE had been reduced from 16% to 14%, CERC had given argument for reduction in the interest rates as the prima facie reasons for reducing the return on equity. In the present regulation, ROE is allowed from the date of commercial operation. Interest on debt portion of the project is allowed by way of IDC during the construction of the project; however, no return is given to investor for the equity portion invested during the construction period. One of the preconditions for the disbursement of loan is induction of equity by the investor and hence equity is invested in the project since inception. Due to this reason, the overall ROE gets further reduced.</p> <p>Interest rate has increased substantially over the period from 2002-03 to 2007-08. The interest rate has increased from 10.5% in 2004 to 14% in 2008. In the Regulation 2008, instead of linking the ROE with prevailing interest rates, CERC has linked the ROE with the performance of certain IPOs of power sector companies like NTPC, PGCIL and Reliance Power assuming that investors enthusiasm is maintained even at the post tax rate of return of 14% allowed to companies in the power sector. CERC has admitted that ROE cannot be determined on some scientific models like dividend growth model, price earning ratio, capital asset pricing model, as not many state owned generating or transmission companies have entered the capital market. It is submitted that only few companies in the power sector have ventured in the share market for raising its equity. The share premium and the market response in the IPO by the company like NTPC, Powergrid, Reliance Power are not linked with the ROE but to its goodwill, growth prospect, capability of the promoter in executing the project, global market condition at the time of IPO and short term money market situation and other macro economic factors. If we see the post issue scenario by all the companies mentioned in the explanatory memorandum, we may also find that these companies have not been able to sustain over their initial listed prices. So it is suggested that CERC should continue to compare ROE with the prevailing interest rate. Barring few Indian companies like NTPC, Powergrid, Tata Power, Reliance Power, not many domestic or</p>

			<p>no other foreign companies are showing interest in the power sector even post enactment of Electricity Act 2003. Therefore, to encourage private/foreign participation in the power sector, it is suggested to enhance the ROE to at least 18%, as the returns available to private parties in other business opportunities are more with less risk as compared to returns available in the power sector. Also as mentioned earlier, the ROE shall be given during the construction period of the project. This would contribute to overall growth of the Indian Economy, as without a corresponding development of the power sector, we may not be able to sustained GDP growth rate of 8% -9%.</p>
10.	24	19	<p>Operation & Maintenance Expenses (O&M): In the O&M expenses, Hon'ble CERC has considered the data submitted by Powergrid having more than 70,000 ckt. Km and national presence. Moreover, Powergrid is also operating substation along with the transmission lines. Hence, the Powergrid enjoys benefit of economies of scale in operation and maintenance of the transmission lines. Powerlinks have submitted initial data for 2006-07 and 2007-08, which have been completely ignored by Hon'ble CERC in framing the proposed Regulation 2008. Powerlinks have been continuously stating in all hearing/discussion that the O&M norms in the Regulation 2004 is not adequate to cover the minimum O&M expenditure incurred/ to be incurred by Powerlinks for effective operation and maintenance of the transmission lines. The following points also need specific mention and need to be considered:</p> <ol style="list-style-type: none"> 1. It would be appreciated that Powerlinks being a separate legal corporate entity, by virtue of its creation as a company under the Companies Act 1956 and requires a fixed cost to be incurred for the purpose of complying with statutory formalities, it has to discharge and comply with all Statutory Laws and regulations. It is also expected that Powerlinks should follow corporate governance, for which Corporate Office with Managing Director, Director (Finance), Company Secretary etc are minimum required. These expenses are fixed in nature and remain same irrespective of the level of Operation & Maintenance activities. Therefore, to conclude that Corporate office expenses of Powerlinks are much more than that of Powergrid is not correct and cannot be compared. Moreover, the Powergrid corporate office cost is distributed not only on the transmission lines but also on its substations and other business activities like consultancy and telecommunications. It is also pertinent to mention here that the cost per employee of Powerlinks is much lower than that of Powergrid. 2. Powergrid O&M cost cannot be compared with Powerlinks as Powergrid operates both transmission lines and the substations.

		<p>3. Powerlinks is a single project company, which is also unidirectional and spread over 1166 Km, which requires more project offices to maintain the line.</p> <p>4. The ratio of manpower deployed per 1000 Km. of Powergrid cannot be compared with that of Powerlinks, as the economy of scale for operating more than 70000 ckt. Km. in case of Powergrid is not comparable with 2332 ckt. Km. being maintained by Powerlinks.</p> <p>5. Powerlinks is the only company in the private sector who have completed the transmission line and is into O&M of transmission line. Any non-recovery of actual bonafide O&M would further reduce the already lowered ROE and would act as a deterrent to private players willing to participate in the development of power sector. We strongly recommend that O&M cost shall be fixed as percentage of project cost or Gross Block instead of ckt. Km.</p> <p>We recommend a maximum percentage of 1.5% of the Gross Block in case of transmission line and 3% in case of substations subject to actual expenses incurred by the transmission licensee. As this is subject to prudence check by the Hon'ble Commission it would ensure adequate maintenance of the transmission line.</p> <p>The present O&M cost of Powerlinks is Rs. 9.25 crs. for the year 2007-08 and Rs. 4.80 crs. in the year 2006-07 (for part of the year) excluding the insurance cost.</p> <p>We strongly feel that O&M cost of Powergrid cannot be compared with a single project company like Powerlinks, which is efficient in its working but lacks economies of scale. The present O&M norm may not only jeopardize the operation of the line but availability of the line will be seriously affected because of low O&M cost. Since, the Powerlinks transmission line from Siliguri to Mandola is an important link between Eastern and Northern regions, it is suggested that O&M norms may be considered separately in case of Powerlinks taking into account its inherent limitation due to size of operation. It is reiterated that Powerlinks is maintaining high efficiency in operation and maintenance cost in its given situation.</p> <p>It may be noted that CERC has considered an inflation rate of 5% for giving increase in O&M expenses on Year and Year (YOY) basis. This rate is far less than the prevailing inflation rate of 12% per annum (approx.). It is suggested that increase shall be given on the basis of average inflation rate prevailing during the year.</p>
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11.	26	17.4 (a)	<p>Depreciation including Advance Against Depreciation: In the proposed regulation, advance against depreciation has been abolished and the depreciation rate for the transmission line has been enhanced from 2.57% to 4.67% for the initial 15 years and for the remaining life of 20 years, it is proposed to allow depreciation at the rate of 1%. In the absence of advance against depreciation to match the cash flow requirements for repayment of loan, It appears that the Hon'ble CERC expects that the generating company or the transmission licensee shall negotiate with the lenders for loan with the repayment period tenure of 15 years. In the normal scenario, the lender is interested for 10 or 12 years repayment period. In case it is required to be extended beyond 12 years, lender ask for higher interest rates to cover the additional risk of long repayment schedule. As the interest is passed through, ultimately beneficiary will be required to bear the additional burden due to increased interest cost. The normal 10 or 12 years repayment schedule is over and above a period of 3 years moratorium allowed by the lender during the construction phase of the project. Thus a clear 15 years repayment period would require loan tenure of 18 years, which is highly expensive proposition in case of new projects coming up. Therefore, it is suggested that the depreciation rate may be enhanced to 5.84% instead of 4.67% for the initial 12 years and depreciation rate for the remaining life of the asset may be reduced from 1% to 0.8% in order to match the cash flow requirements with the loan repayment tenures.</p>
12.	28	18	<p>Interest on Working Capital: In computation of interest on working capital in the proposed regulation, the receivable have been reduced from 60 days to 45 days. Spares have been reduced from 1% of the project cost to 15% of the O&M expenses. The O&M expenses for 1 month have been discontinued. All these have resulted into abnormal low working capital, which is not reflected in the business practices/norms. The generating company or transmission licensee does not get full reimbursement of interest on working capital under the proposed regulation. In view of above, it is suggested to keep the provision same as stipulated in the 2004 regulation.</p>
13.	58	35	<p>Late Payment Surcharge: in the regulation 2004, late payment surcharge is applicable in case there is delay in payment beyond one month. In the proposed regulation, late payment surcharge is applicable in case of delay beyond a period of 60 days from the date of billing. There is no provision for rebate or late payment surcharge in case payment is made between one month to 60 days. It also encourage long term transmission customer to delay the payment up to 60 days.</p>

14.	59	36(b)	CDM : For getting registration with UNFCCC to avail CDM benefit, the generating company or the transmission licensee has to incur lot of expenditure for registration, appointment of consultant, appointment of validator etc. It is suggested to bring mechanism for sharing of expenditure also between beneficiary and generating company or transmission licensee.
15.	62	42	License Fee: Other than deemed Licensee, all transmission Licensees are required to pay license fees during the period of construction and operation period. While the license fee incurred during the period of construction is capitalized, there is no provision for getting reimbursement of license fee during operation period. It is suggested that license fee be allowed to be recovered by the transmission licensee directly from the long-term transmission customer in the similar manner as mentioned in clause 42 (application fee and publication fee). This shall be recoverable in all cases and not at the discretion of Hon'ble Commission.
16.	42	23	Incentive: In the present regulation, over-achievement of availability of transmission line against the stipulated level results in payment of incentive equivalent to a percentage of equity. In the draft regulation, it has been shifted from percentage of equity to percentage of annual transmission charges. We suggest that incentive calculation shall be taken as percentage of equity. In the earlier regulation, incentive calculation was on the basis of annual availability. However, in the present regulation, incentive calculation has been shifted from annual basis to monthly basis. We suggest that incentive shall be calculated on annual basis as certification for availability of transmission line is issued by Regional Power Committee on annual basis and secondly averaging concept minimizes the variation during the year. Also annual transmission charges are also calculated on the annual basis. Lastly, as the system gets older it requires more expenses to increase the availability and keep the system in healthy condition if no significant incentive is available, it will defeat the purpose of improving the availability.
17.	58	34	Rebate: In the earlier regulation, rebate was allowed for the payment of bills of transmission charges only. However, in the present regulation, it is stated that rebate is allowed on all the bills of the transmission licensee. It may be noted that bills should be interpreted to include only the bills of transmission charges and not any other bills like for claiming incentive, income tax, FERV etc. as this constitutes for reimbursement of already incurred expenditure by the transmission licensee and already such expenditure is incurred by the transmission licensee.

COMMENTS ON DRAFT CERC(PAYMENT OF FEES) Regulation 2008

The CERC has proposed 0.15% of the annual transmission charges as application fee for determination of Tariff. This will be applicable for entire Tariff Block. Further CERC has proposed to charge licence fee @ 0.05% p.a. of the annual transmission charges. Thus, effectively Licensee is required to pay@ 0.20% of the annual transmission service charges. The proposed fees are exorbitant higher as compared to present application and license fees together. There is no provision as of now, to get reimbursement of payment of such fees from the beneficiary.

In absence of such reimbursement provision and reduction of O & M cost in the draft Tariff Regulation, 2008, the Transmission Licensee will be under tremendous financial hardship in payment of such exorbitant fees annually to CERC. It is therefore suggested to reduce the fee even below the present rate. Alternatively allow the Transmission Licence to recover such expense from the beneficiary.

In case of Interlocutory application the fees has been proposed to increase from Rs. 10000/- to 40000/- i.e., four fold and in case of other application, fees has been proposed to enhance from Rs. 1,00,000/- to Rs 2,00,000/- i.e double the rate.

In the present scenario where every company is sincerely exploring ways and means for reduction of expenditure and tighten the belt, such exorbitant increase on the part of the Regulator is not only jeopardize the electricity growth but also economic growth of the Country

It is therefore suggested that CERC as a regularity body and not a commercial establishment should make an efforts for reduction in fees rather than proposed increased in fees