Appellate Tribunal for Electricity
(Appellate Jurisdiction)

Appeal No.191 of 2009

Dated 27th April, 2011

Present: Hon'ble Mr. Justice M. Karpaga Vinayagam, Chairperson
Hon'ble Mr. Rakesh Nath, Technical Member
Hon'ble Mr. Justice P.S. Datta, Judicial Member

In the matter of:

Maharashtra State Power Generation Co. Ltd.,
A company incorporated under the
Companies Act, 1956 and having
its registered Office at Plot No. G-9,
Prakashgad, Bandra (East),
Mumbai-400 051. ... Appellant(s)

Versus

1. **Maharashtra Electricity Regulatory Commission,**
a Commission constituted under the provisions
of Electricity (Supply) Act, 1998 and having its office at
13th Floor, Center No. 1,
World Trade Centre, Cuffe Parade,
Colaba, Mumbai-400 005.

2. **Dr. Ashok Pendse,**
Mumbai Grahak Panchayat,
Grahak Bhavan, Sant Dyaneshwar Marg,
Behind Cooper Hospital,
Vile Parle (W),
Mumbai- 400 056.

3. **Thane Belapur Industrial Association,**
Plot – P14, MIDC, Rabale Village,
P.O. Ghasoli,
Navi Mumbai-400 701.

4. The President,
Vidarbha Industrial Association,
1st Floor, Udyog Bhavan,
Civil Lines, Nagpur-440 001.

5. Prayas (Energy Group),
Amrita Clinic, Athwale Corner,
Deccan Gymkhana, Karve Road,
Pune-411 001.

6. Shri Shrikant Dudhane,
Chairman,
Kolhapur Engineer Association,
1243/46, 47, E-Ward,
Shivajiudyam Nagar,
Kolhapur-416 008.

7. Shri B.T. Tendulkar,
Vice-Chairman,
Kolhapur Engineer Association,
1243/46, 47, E-Ward,
Shivajiudyam Nagar,
Kolhapur-416 008.

8. Shri Balachandran
General Manager (Power & Energy),
ISPAT Industries Ltd.,
"Nirmal" 7th Floor, Nariman Point,
Mumbai-400 021

9. Shri N. Poorathnam,
Vel Induction Hardenings,
25, Majithia Industrial Estate,
WTP Marg, Deonar,
Mumbai-400 088.

10. Shri Bhasker U. Mete,
Working President,
Graduate Engineers Association,
Quarter No. IV/08/04,
Koradi TPS Colony, Koradi,
Nagpur-441 111.

**11. Maharashtra State Electricity Distribution Co. Ltd.,
Plot No. G-9, Prakashgad,
Bandra (East), Mumbai-400 051 ...Respondent(s)**

Counsel for the Appellant(s): Mr. Shyam Divan Sr. Advocate with
Ms. Deepa Chavan, Mr. Rakesh Sinha,
Mr. Kiran Gandhi, Ms. Amita Rajora &
Ms. Taruna A. Prasad

Counsel for the Respondent(s): Mr. Buddy A. Ranganadhan for R-1
Mr. Abhishek Mitra, Mr. Raunak Jain &
Ms. Puja Priyadarshini,
Mr. A.R.Chowdhury for MSEDCL
Mr. Varun Pathak & Mr. Aashish Bernard
Mr. Rakesh Pal (Rep.) for R.9

JUDGMENT

HON'BLE MR. RAKESH NATH, TECHNICAL MEMBER

This Appeal has been filed by Maharashtra State Power Generation Company Limited, a State owned power Generating Company. Maharashtra State Electricity Regulatory Commission is the Respondent no. 1. The Respondent nos. 2 to 10 are the consumers or consumer Associations or Consumer Representatives. Maharasthtra State Electricity Distribution Company is the Respondent no.11.

2. Initially, the Appeal was filed challenging the order passed by the State Commission on 17.8.2009 in Case No. 115 of 2008 for True up for FY 2008-09 and tariff for FY 2009-10 of the Appellant. The Appeal was subsequently amended to challenge the State Commission's orders dated 19.1.2010 and 5.3.2010 regarding true up for FY 2005-06 to FY 2007-08 and provisional true up for FY 2008-09 of the financials of the Appellant.

3. The brief facts of the case are as under:

3.1. On 7.9.2006 the State Commission passed the order on the Aggregate Revenue Requirement (ARR) of the Appellant for the FY 2005-06 and FY 2006-07 in case no. 48 of 2005.

3.2. The State Commission on 25.4.2007 issued Multi Year Tariff (MYT) order in case No. 68 of 2006 in respect of the Appellant for the first Control Period from FY 2007-08 to FY 2009-10 and tariff for the year 2007-08.

3.3. The Appellant filed appeals against State Commission's order dated 7.9.2006 and 25.4.2007 bearing Appeal nos. 86 and 87 of 2007 respectively. The Tribunal by its order dated 10.4.2008 allowed the appeals partly and remitted the matter back to the State Commission for re-determination of the tariff of the Appellant. The Tribunal also directed the Appellant to engage an independent agency to conduct a study to assess the achievable Station Heat Rate of the Appellant's power plants.

3.4. On 4.11.2008 the State Commission appointed Central Power Research Institute to carry out detailed study of the Appellant's plants.

3.5. The Appellant filed case No. 115 of 2008 with the State Commission for truing up for FY 2007-08, Annual Performance Review (APR) for FY 2008-09 and tariff determination for FY 2009-10. The State Commission after public hearing passed an order in Case No. 115 of 2008 on 17.8.2009. Aggrieved by this order the Appellant filed this appeal.

3.6. However, during the proceedings of the Appeal, the Tribunal permitted the truing up exercise by the State Commission. Subsequently, by its order dated 19.1.2010 the State Commission decided to hold the public hearing on some of the items of true-up. The

State Commission after the public hearing passed the true-up order dated 5.3.2010 in case No. 16 of 2008.

3.7. Thereafter, the Appellant moved IA No. 82 of 2010 before this Tribunal for amendment of the Appeal which was allowed. In the amended appeal the Appellant has also challenged the State Commission's order dated 19.1.2010 directing public hearing in true up of some of the items and order dated 5.3.2010 allowing some of the claims of the Appellant in the true-up of the financials and disallowing others. Thus in this Appeal, the orders of the State Commission dated 17.8.2009, 19.1.2010 and 5.3.2010 are being challenged.

4. The Appellant had raised a number of issues some of which did not survive after the State Commission's order dated 5.3.2010. Learned counsel

for the Appellant argued extensively on the following remaining issues assailing the impugned orders of the Respondent-1/State Commission:

i) Truing up not taken up expeditiously.

ii) Truing up of Operation & Maintenance expenses with erroneous computation of base year figures for arriving at the O&M expenses for subsequent years.

iii) Truing up for fuel costs for the years 2005-06 to 2007-08.

iv) Carrying cost for deferred true up.

v) Non-consideration of Deferred Tax Liability for computation of Return on Equity.

vi) Non consideration of station-wise Advance Against Depreciation.

vii) Reactive Energy Charges.

viii) Erroneous period of spread for bad and doubtful debts.

ix) Erroneous Disapproval of Interest on Working Capital.

On the issue of employees incentive scheme raised in original Appeal the Appellant has submitted that they would approach the State Commission with a scheme for consideration. The State Commission in its impugned order has already welcomed any incentive scheme which facilitates improvement in operational efficiency.

5. Learned counsel for the Respondent-1/State Commission argued strenuously on the various issues raised by the Appellant in support of the impugned orders of the State Commission. We have also received written submission from Respondent no. 9 opposing any additional burden on the consumers.

6. We have perused the various documents submitted by the parties and considered the contentions of the learned counsel for the parties. After considering the rival contentions of the parties we frame the following questions for consideration:

(i) Whether there was any delay on part of the State Commission to implement the directions of the Tribunal passed in its Judgment dated 10.4.2008 and was a second public hearing necessary before the true-up?

(ii) Whether the base figure of Operation & Maintenance expenses adopted by the State Commission for projecting normative O&M expenses for the period 2007-08 to 2009-10 was correct?

(iii) Whether the State Commission was correct in truing up the fuel costs for the FY 2005-06 to FY 2007-08 as per the actual expenses in contravention to recommendations of CPRI?

(iv) Whether the State Commission was correct in limiting the carrying cost on deferred trued up amount till 31.3.2010 whereas the same is to be recovered in 12 monthly instalments during the FY 2010-11?

(v) Whether the State Commission has erred in not including the deferred tax liability in equity base and denying the return on equity on the same contrary to its own Regulations?

(vi) Whether the State Commission erred in denying Advance Against Depreciation

station-wise due to the reason that the actual depreciation for Appellant's company is higher than actual loan repayment by the Appellant's company as a whole?

(vii) Whether the Central Commission was right in not allowing reactive energy charges for reactive energy injected by Appellant's power plant without regard to the directions of the Tribunal?

(viii) Whether the State Commission was correct in not allowing bad and doubtful debts to be recovered from FY 2005-06 without regard to the directions given by the Tribunal?

(ix) Whether the State Commission has wrongly disallowed interest on Working

Capital on the ground that the working capital requirement was met from internal accruals?

7. The first issue is regarding expeditious true up of the financials of the Appellant by the State Commission/Respondent no.1.

7.1. Learned counsel for the Appellant has raised the issue of delay in implementing the directions of the Tribunal in its Judgment dated 10.4.2008 and need for a second public hearing at the stage of true up. The time schedule given by the Tribunal for appointment of agency for carrying out the study of performance parameters was not followed by the State Commission. According to her, a public hearing at the stage of true up is not required as the main Tariff Order had been passed earlier after a public hearing.

Section 64(3) of the 2003 Act also does not provide for the same.

7.2. Shri Buddy A. Ranganadhan, the learned counsel for the State Commission has given a detailed explanation for each of the activities involved in the study by the independent agency post the Judgment of this Tribunal dated 10.4.2008. The State Commission had to develop detailed terms of reference including all the technical aspects after which enquiry inviting bids was issued on 20.6.2008. However, only two bidders viz; NTPC and Central Power Research Institute (CPRI), showed interest. The State Commission had also to extend the date of opening of bids on two occasions on the request of one of the bidders. Ultimately Letter of Intent/order could be issued on the CPRI only on 14.11.2008. At every stage, starting from kick-off meeting in which the detailed schedule for the study

for each station was discussed and during the study, the Appellant was fully involved.

7.3. On the issue of public hearing, Shri Buddy A Ranganadhan has argued that the Tribunal in its order dated 10.4.2008 had remitted the matter back to the State Commission for re-determination. The State Commission in its order dated 19.1.2010 had identified the issues/elements of truing up on which suggestion and objections from public were to be invited for re-determination of tariff and issues on which only the information was to be made available to the public. Even a truing up process is not merely a mathematical exercise of comparing the actuals with projections and the State Commission has to examine the prudence of expenditure. The public has a right to contend that a particular expense was prudently incurred or not.

7.4. We have examined the matter. On the issue of delay in appointment of agency in compliance of the Tribunal's Judgment dated 10.4.2008, the Respondent-1 has submitted detailed explanation giving the chronological events and milestones from invitation of bids to the submission of report by CPRI. Considering that such a study was being carried out for the first time, limited response from bidders and extensions sought by the bidders for submission of bids, we do not find that any blame can be put on the State Commission for delay in instituting the study.

7.5. We now examine whether the State Commission was correct in inviting public suggestions and objections on the re-determination of tariff/true up on the direction of the Tribunal. Firstly, we will examine Section 64 of 2003 Act relating to procedure to be

followed for tariff order. The relevant clauses of Section 64 are reproduced below:

"64. Procedure for tariff order. - (1) An application for determination of tariff under section 62 shall be made by a generating company or licensee in such manner and accompanied by such fee, as may be determined by regulations.

…….

(3) The Appropriate Commission shall, within one hundred and twenty days from receipt of an application under sub-section (1) and after considering all suggestions and objections received from the public,-

(a) issue a tariff order accepting the application with such modifications or such conditions as may be specified in that order;

(b) reject the application for reasons to be recorded in writing if such application is not in accordance with the provisions of this Act and the rules and regulations made thereunder or the provisions of any other law for the time being in force:

Provided that an applicant shall be given a reasonable opportunity of being heard before rejecting his application".

Thus the State Commission has to consider the suggestions and objections before determination of tariff.

7.6. It is noticed that the State Commission while determining the tariff for the ensuing financial year the (nth year) also carries out the Annual Performance Review for the current year(year n-1) and the True Up for the previous year (year n-2). Accordingly, the Public Notice given for the determination of tariff for the forthcoming Financial Year also covers the APR for the current year and True Up for the previous year. In the petition No. 115/08 which culminated in the impugned order dated 17.8.2009, the State Commission had decided the

True Up for 2007-08, APR for 2008-09 and Tariff for 2009-10 after a public hearing. Now the question arises that when the State Commission trued up the financials from FY 2005-06 to FY 2007-08 based on the Tribunal's judgment dated 10.4.08 and CPRI report and provisional true up for FY 2008-09, was it necessary to give public notice under Section 64(3)?

7.7. The State Commission in its order dated 19.1.2010 examined in details each element of true up so as to decide whether public notice was necessary and came to conclusion that in the matter of resetting of performance parameters, employees incentive, reactive energy changes, hydel tariff mechanism and O&M norms for hydel plants, public notice was necessary. However, other issues where the Tribunal's order had no scope for consideration of suggestion/objection from the public it was directed to

make available for the information of the public only and not for inviting any suggestions/objections.

7.8. In our view the State Commission had correctly decided to issue public notice under Section 64(3) for issues where the State Commission had to devise new norms on the basis of the CPRI report or devise new schemes or mechanism for hydel tariff, reactive energy charges and employee incentive scheme. The Tribunal has not given a clear finding on these issues which could be directly applied by the State Commission. On the other hand, the State Commission had to reconsider these issues afresh and then decide. Thus we do not find any fault with the decision of the State Commission for obtaining suggestions and objections from the public in the interest of principles of natural justice.

7.9. Ms. Deepa Chavan, the learned counsel for the Appellant has referred to Tribunal's judgments in North Delhi Power Ltd. versus CERC & Ors. ELR 2007 APTEL 193 and North Eastern Electricity Supply Company versus OERC & Ors. 2007 APTEL 278. These judgments are of no relevance to the Appellant as they deal with reasonable estimation of the revenue requirement and on true-up to be undertaken by the State Commission on a regular basis. In the present case the State Commission carried out the true up by its order dated 17.8.09 but the Appellant was aggrieved on some issues which were challenged by the Appellant in this Appeal. We agree with the learned counsel for the Appellant that true up of the uncontrollable expenses should be done as expeditiously as possible. However, in this case, the delay was due to the following of the process of law

and in the interest of honouring the principles of natural justice. In view of this we hold that the State Commission's order dated 19.1.2010 is correct.

8. The next issue is regarding true up of operation and maintenance expenses. The limited grievance of the Appellant is computation of the base year figures for arriving at O&M expenses for the subsequent years.

8.1. According to the Appellant, during the base year 2006-07, some capital works were in progress at some of the power plants of the Appellant and a part of the employees' cost was booked to the Capital Works. The net O&M expenditure considered as base figures excluded the employees cost booked to the Capital Works. Thus the actual net O&M expenditure for the base year would not correctly reflect the O&M

expenses as some employees expenses were booked to the capital works. If in subsequent years no capital works such as Renovation & Modernization is carried out at the existing stations, the actual O&M expenditure incurred would be more than the normative O&M expenses worked out on the basis of base O&M figures for FY 2006-07. According to the Appellant, gross O&M expenses for existing stations for FY 2006-07 should have been taken as base figure instead of net figure for projecting the normative O&M expenditure for subsequent years.

8.2. According to the learned counsel for the State Commission, the base figures have been adopted as the actual audited O&M expenses for 2006-07 as per the Tribunal's judgment. Further, the Appellant did not make any claim regarding expenditure of capital

nature under O&M expenses before the State Commission, as is being made before the Tribunal.

8.3. Let us first examine the O&M expenses for base year 2006-07 determined by the State Commission in its order dated 5.3.2010. The actual gross and net O&M expenses for FY 2006-07 as determined by the State Commission based on the data submitted by the Appellant before it are as under:

'All figures in Rs. Crores'

	Existing Stations	Upcoming Stations	Total
Gross Expenses	919.12	28.99	948.11
Less excess Gratuity	(3.26)	3.26	-
Expenses Capitalized	32.41	61.25	93.66
Net expenses	883.45	(29.00)	854.45

8.4. The State Commission has considered the total gross O&M expenses of FY 2006-07 at Rs. 948.11

crores and after deducting the capitalized O&M expenses of Rs. 93.66 crores, the net O&M expenses were worked out at Rs. 854.45 crores. Accordingly, the State Commission has considered the actual O&M expenses of Rs. 854.45 crores under truing up of O&M expenses for FY 2006-07 and also for base figures for computing the revised O&M expenses for FY 2007-08 to 2009-10 after applying indexation factor.

8.5. According to Ms. Deepa Chavan, learned counsel for the Appellant some capital works were in progress during FY 2006-07, which may not recur in the subsequent years. Non-consideration of employees' expenses booked to capital expenses will eventually increase the gap between actual and normative expenses, in case no renovation and modernization is taken up by the power stations in the subsequent

years. She also argued that the determination of O&M expenses is contrary to the Regulations.

8.6. According to Mr. Buddy Ranganadhan, learned counsel for Respondent-1, the Appellant had not made any such claim before the State Commission. The submission of the Appellant before the State Commission was that for the purpose of true up for subsequent years, the State Commission should also consider the prudency of actual expenditure incurred due to vintage of units, actual employees expenses and A&G expenses and escalation rate, etc.

8.7. We have perused the petition filed by the Appellant before the State Commission and found that the issue now being raised regarding capitalization of O&M expenses before the Tribunal was not raised before the State Commission. The contention of the

Appellant is also based on the presumption that in case no Renovation & Modernization work is carried out in subsequent years, then the Appellant will be prejudiced due to consideration of net O&M expenses for the base year. The Appellant has also not given any facts and figures in respect of true up for FY 2007-08 and provisional true up for FY 2008-09 to establish its contention. We have also examined the Regulations and we do not find any clause specifically dealing with gross and net O&M expenses and employees expenses booked to Capital Works.

8.8. In view of the above, we do not find any reason to interfere with the order of the State Commission on O&M expenses. However, we give liberty to the Appellant to place the issue of gross/ net O&M expenses raised in this Appeal before the State Commission for consideration in subsequent True Up

or Tariff petition and in that event the State Commission may consider the same to ensure that the Appellant is not denied of the legitimate O&M expenses on account of booking of O&M expenses to Capital Works.

9. The next issue is regarding truing up for fuel costs for the years 2005-06 to 2007-08.

9.1. Learned counsel for the Appellant has argued that while the State Commission has adopted the Station Heat Rate for future years as per CPRI, the benefit of CPRI recommendations for FY 2005-06 to 2007-08 has been denied to the Appellant as it would result in allowing fuel expenses in excess of actual fuel expenses.

9.2. We find that CPRI had carried out the study and arrived at achievable Station Heat Rate by conducting studies at various power plants of the Appellant during the years 2008 and 2009. The State Commission also asked CPRI to give its views on achievable heat rate for FY 2005-06, 2006-07 and 2007-08. CPRI derived the Station Heat Rate for past period by applying the degradation factor on the achievable heat rate arrived on the basis of the study for the year 2008/2009 when the study was carried out at the various power stations. Thus, the heat rates assessed by CPRI for the year 2005-06 to 2007-08 were computed by applying some theoretical degradation factor on the achievable heat rate assessed on the basis of study conducted in years 2008 and 2009.

9.3. The State Commission has observed that there has been significant change in measurement of the Station Heat Rate and calorific value during FY 2008-09. CPRI in its report has also highlighted the reason for sudden increase in the Station Heat Rate in FY 2008-09 as reproduced below:

> *"It is seen that heat rate achieved by almost all the MSPGCL stations for the FY 2008-09 are more than those achieved for previous years. This is attributable to procedural changes in the methodologies for arriving at the heat rate and heating values of coal. To assess the prevailing practices & ensure correctness of heat rate & Auxiliary consumption data, MSPGCL has formed a study group for arriving the uniform method of calculations of Heat Rate & Auxiliary consumption in MSPGCL Stations. After deliberations at various*

MSPGCL power station this group has formulated 'a procedure for correctness of data of heat rate and auxiliary consumption' which was accepted by Director (Operations) MSPGCL and circulated for immediate implementation vide letter MZ/PST/MOR/Nil dtd. 13/10/2008 which was implemented at MSPGCL Stations vide instructions ref. no CHN/CGM/Instruction/02098 dt. 27/Oct./2008.

The change in procedure recommended by the Committee has resulted in station heat rates being changed to new values which represent more realistic field conditions or portrayal of more realistic picture. Also, skipping of overhauls (planned maintenance schedules), lower PLF have been responsible for heat rate degradation, though to a lesser extent".

Thus the methodology for arriving at heat rate was changed during the year 2008-09 at the Appellant's power plants. The State Commission has, therefore, considered the actual fuel expenses as per audited accounts of the Appellant in the true-up exercise.

9.4. We find that the State Commission has given a reasoned order for not accepting the base heat rate as per the assessment of CPRI for the past period based on theoretical assumption of degradation factor and allowed the actual fuel cost. We are in agreement with the methodology used by the State Commission for true up for fuel cost for the FY 2005-06 to 2007-08 due to change in procedure made during the study in the years 2008/2009 and back computation of Station Heat Rate on theoretical basis without regard to actual site conditions. Also no loss has been caused to the

Appellant by adopting the actual fuel expenses for these years. Accordingly, we confirm the State Commission's finding on this issue.

10. The next issue is regarding the carrying cost on deferred true up.

10.1. According to the Appellant, the State Commission has erroneously restricted the period of consideration of carrying cost till 31.3.2010 whereas the actual recovery in respect of the past period commencing from 2005-06 is spread over a period of 12 months. The State Commission ought to have allowed the carrying cost on this deferred true up till actual recovery.

10.2. We have noticed that the State Commission has allowed the carrying cost upto the end of year 2009-10. For example, for trued up amount for

FY 2005-06, the carrying cost has been allowed for the years 2005-06, 2006-07, 2007-08, 2008-09 and 2009-10 i.e. 5 years. Similarly, for trued up amount for FY 2006-07, carrying cost has been allowed for 4 years till 31.3.2010. The trued up amount is to be recovered in 12 equal monthly instalments during FY 2010-11. We feel that this is a correct approach. The amount which is now trued up for the FY 2005-06 should have been ideally included in the tariff for the FY 2005-06 and the full amount should have been recovered during the 12 months period of FY 2005-06. Now, the same amount has been allowed to be recovered during the 12 months period during FY 2010-11. Thus, the recovery has been deferred by 5 years. Similarly, the trued up cost for FY 2006-07 has been deferred by 4 years. Thus the carrying cost has been correctly allowed by the State Commission. We do not find any

infirmity in the order of the State Commission. This issue is decided accordingly.

11. The next issue is regarding deferred tax liability for computation of Return on Equity.

11.1. According to the Appellant, Regulation 31.1.1(b) of the Tariff Regulations provides for addition of deferred tax liability in calculation of base of equity. Accordingly, the Appellant has taken the same into consideration for estimating the regulated equity base for 2007-08. The State Commission has wrongly limited the scope of the Regulation by holding that such inclusion is applicable for the year in which the company was formed as per the transfer scheme.

11.2. Let us first discuss the concept of deferred tax liability. The income tax is calculated according to the provisions of the Income Tax Act wherein the

various elements for determination of income may be different from the provisions of the Companies Act. For example, the depreciation allowed on the assets according to the Income Tax Act is different from that allowed according to the Companies Act. This difference will result in creation of deferred tax liability or deferred tax assets in the books of accounts of a company. The deferred tax liability created in a project, say in the initial years of operation may be neutralized in the later years of operation of the project. Thus, the deferred tax liability can not be added to the equity base unless it can be established that such liability has been created in perpetuity.

11.3. Now we will examine the Regulations. The relevant Regulation 31.1.1(b) stipulates as under:

> *"(b) The amount of equity capital shall be equal to-*

(i) equity capital as at April 1, 2004 as determined by the Commission In accordance with the Explanation below: plus

(ii) equity component of approved capital expenditure for the financial year ending March 31,2005:

Provided that in case of a Generating Company formed as a result of a transfer scheme under Section 131 of the Act, the date of the said transfer scheme shall be the effective date instead of April 1, 2004 for determination of equity capital under clause (b) above.

Exaplanation- for the purpose of this Regulation, equity capital shall be the sum total of paid-up equity capital, preference share capital, fully/compulsorily convertible debentures (or other financial instruments with equivalent characteristics), foreign currency convertible bonds, share premium account and any reserves, available for distribution as dividend or for capitalization by way of issue of bonus shares, whish have been invested in the Generation Business. The amount of any grant, revaluation reserve, development reserve, contingency reserve and contributions from customers shall not be included in the equity capital. The amount

reflected in the books of account as deferred tax liability or deferred tax asset of the Generation Business shall be added or deducted, as the case may be, from the amount of equity capital."

According to Shri Buddy A. Ranganadhan, learned counsel for the State Commission/Respondent-1, the words "in accordance with the explanation" appear only in the first sub-clause of the Regulation. The first sub-clause pertains only to the computation of opening equity capital and not on any other computation. Hence, the inclusion of deferred liability in equity capital is applicable only for the year in which the company is formed as per the transfer scheme.

11.4. We feel that deferred tax liability of the Appellant is not created in perpetuity. Thus, in view of the explanation given by us explaining the deferred tax

liability in para 11.2 above, we fully agree with the reasoning given by the State Commission in the impugned order for not including the deferred tax liability in equity capital. This point is accordingly decided against the Appellant.

12. The next issue is non-consideration of station-wise Advance Against Depreciation.

12.1. The Appellant has submitted that it has been filing for tariff determination power station wise. The Appellant has been seeking Advance Against Depreciation (AAD) in cases where the loan repayment in respect of a particular year exceeds the depreciation according to Regulation 32.3. The State Commission has wrongly denied AAD for FY 2007-08 considering that the actual depreciation for the Appellant's

company as a whole is higher than the actual loan repayment for the company.

12.2. According to the State Commission, the objective of providing AAD in addition to depreciation is to support cashflow requirement towards loan repayment of the company as a whole. The State Commission has not allowed any AAD for FY 2007-08 as the actual depreciation for the Appellant's company during the year was higher than the actual loan repayment for the company as a whole. Further, the Appellant has admitted that there is no clear segregation of loans between the stations.

12.3. Let us now examine the relevant Regulation 32 which is reproduced below:

"32. ***Loan repayment schedule****-*

32.1. The repayment schedule for the loan capital of existing generating stations

calculated under Regulation 31.1 above shall be in accordance with the loan agreements.

32.2. The loan capital calculated using the normative debt: equity ratio under Regulation 31.2, Regulation 31.3 and Regulation 31.4 above shall be assumed to be repaid each year based on a normative repayment schedule:

Provided that the amount of such normative repayment for a year shall be equal to the amount of depreciation on the fixed asset to which such loan relates:

Provided further that where the outstanding normative loan balance is less than the amount of normative loan repayment calculated as above, the repayment shall be assumed to be equal to the outstanding normative loan balance and no further amount shall be permitted on account of such loan:

Provided also that all normative repayments are assumed to be made on September 30th of each financial year.

32.3. Where, in respect of a generating station the actual amount of loan repayment in any financial year exceeds the amount of depreciation allowable under Regulation 34.4.1, the Generating Company shall be allowed an advance against depreciation for the difference between the actual amount of such repayment and the allowable depreciation in respect of such generating station, for such financial year:

Provided also that such advance against depreciation shall be restricted to 1/10th of the principal amount of loans minus the amount of depreciation allowable under Regulation 34.4.1:

Provided also that the amount of repayment, calculated in accordance with Regulation 32.1 and Regulation 32.2 above shall be assumed to be increased

by the amount of such advance against depreciation availed by the Generating Company:

Provided also that upon repayment of the entire loan amount, the original cost of the fixed asset shall be reduced by the aggregate of accumulated depreciation and advance against depreciation availed by the Generating Company and the resulting depreciable value shall be spread over the balance useful life of the fixed asset".

The Regulation 32.3 clearly indicates that the AAD is permissible in respect of a generating station where the actual amount of loan repayment in a financial year exceeds the amount of allowable depreciation in respect of such generating station, for such financial year.

12.4. The points raised by the learned counsel for the State Commission/Respondent no. 1 in support of the State Commission's order are:

i) AAD is intended to meet shortfall in meeting loan repayment obligation of the generating company and is not intended to provide additional cashflow to the Generating Company. AAD should not result in unjust enrichment of the Generating Company.

ii) In earlier tariff order dated 31.5.2008 for FY 2008-09 the State Commission had adopted similar approach and the same was not challenged by the Appellant.

iii) "actual" loan repayment in respect of each generating station is the primary requirement for application of Regulation 32.3. What is

being compared is not the actual loan for each generating station vis-à-vis depreciation but an amalgam of actual and allocated loan even if the allocated component is a small component of total loan.

12.5. Let us now examine the above contentions of the Respondent no. 1 in seriatim.

i) In the entire tariff exercise the tariff is being determined station-wise. All the components of tariff are determined for each station. The availability at which a generating station recovers its full fixed cost is also determined station-wise. Regulation 32.3 also provides for AAD specific to a generating station. Therefore, it is logical that AAD is also allowed station-wise and not company as a whole. AAD results in front loading of the

tariff but the balance depreciation after repayment of loan is appropriately adjusted for AAD so that the total depreciation allowed to a generating station remains the same. If the Regulations provide for AAD for a generating station, it should not be denied on some other grounds which do not form part of the Regulation.

ii) The second contention of the Respondent No. 1 is that the State Commission adopted similar approach for AAD in earlier tariff order. In our opinion each tariff proceeding is a separate and distinct cause of action. Failure of the Appellant to challenge an issue in earlier tariff order does not bar the Appellant to challenge that issue in a subsequent tariff order.

iii) According to the Appellant same generic loans were taken by the erstwhile Maharashtra State Electricity Board prior to its reorganization which have been allocated station-wise. In our opinion the Appellant's contention of allocating such loans station-wise is the correct approach. The station-wise interest on loan and tariff of the generating stations of the Appellant is also being determined on the basis of such allocated loans and specific loans taken for a generating station. Thus actual repayment of such allocated loans can also be apportioned power station-wise.

In view of the above we decide this issue in favour of the Appellant and direct the State Commission to determine station-wise AAD.

13. The next issue concerns Reactive Energy Charge.

13.1. According to the learned counsel for the Appellant, the reactive energy charges were adjudicated by this Tribunal in its Judgment dated 10.4.2008. The State Commission instead of deciding the issue according to the directions of the Tribunal has disregarded the claims of the Appellant.

13.2. The directions of the Tribunal in the Judgment dated 10.4.2008 in regard to reactive energy charges are as under:

> *"88. The Appellant has submitted that it has sought for incentives in respect of recovery of reactive energy charges on the ground that when the stations of the Appellant are called upon by the SLDC at various points of time exclusively for Reactive Energy generation/absorption for grid stabilization, no active power is generated by the Appellant incurs expenditure in the form of increased auxiliary consumption, increased operation*

and maintenance expenses by way equipment, wear/tear, etc".

"91. In our opinion, if the Appellant is required to extent support for Reactive energy generation /absorption for grid stabilization, there would be additional burden on the Appellant, which requires compensation. The Commission has already worked out a mechanism for incentive/penalty for reactive energy injection/ drawal depending upon the voltage at inter – change points, which is applicable to the Transmission Licensees, Distribution Licensees and the open Access users. We feel that since the Appellant is incurring additional expenditure without being compensated, the Commission should extend the above dispensation to the Appellant or may work out a scheme specifically for state power generators within three months".

13.3. The State Commission in its impugned order dated 5.3.2010 has decided as under in respect of reactive energy charge:

"In this regard , it is clarified that there is no expenditure that is incurred by MSPGCL for injection of reactive energy that is not being compensated, since all the expenses prudently incurred by MSPGCL are recovered through

the tariffs, irrespective of whether or not MSPGCL is generating active energy at the time of injecting reactive energy. Further, such additional compensation for reactive energy injection by the generator has not been given even by the CERC in the recently notified Tariff Regulations".

13.4. In our opinion the Tribunal in its Order had given a general direction regarding the recovery of additional expenditure on reactive energy generation by the Appellant's power stations based on the submissions of the Appellant. The Appellant has also not indicated the expenses incurred in reactive power generation not compensated in the ARR/tariff. The State Commission has now clarified that no expenditure is being incurred by the Appellant for injection of reactive energy that is not being compensated. Thus, we do not find any infirmity in the orders of the State Commission and uphold the findings.

14. The next issue is erroneous period of spread for bad and doubtful debts.

14.1. According to the Appellant, the State Commission did not comply with the directions of the Tribunal given in its Judgment dated 10.4.2008 regarding recovery of bad and doubtful debts for the period 2005-06, 2006-07 and 2007-08 and only allowed the claim under this head to be recovered from the consumers only from 2008-09 and not from 2005-06.

14.2. The Tribunal in its Judgment dated 10.4.2008 regarding bad debts held as under:

> *"Hence, under the circumstances we feel it to be reasonable that both the Appellant and consumers may bear the burden on this account. The sum to be recovered from the consumer may be spread*

over a period of three years, without any interest, to lessen the burden on the consumer. However, we would like to stress that the above can not be taken as a precedent for making similar claims in future".

14.3. Accordingly, the State Commission has allowed the doubtful debts amounting to Rs. 25.1 crores in 3 years in its order dated 5.3.2010. The Tribunal had not allowed any interest on doubtful debts and had directed for sharing of burden without this being taken as a precedent. We feel that the State Commission has correctly implemented the direction of the Tribunal.

15. The next issue concerns interest on Working Capital.

15.1. According to the Appellant, the State Commission has wrongly disallowed interest on Working Capital without considering that the working capital requirement was met through the internal accruals. The State Commission has treated such interest as efficiency gain to be shared with the consumer.

15.2. This issue has been dealt with by this Tribunal in the Judgment dated 28.5.2009 in Appeal No. 111 of 2008 in the matter of Reliance Infrastructure Ltd. vs. MERC & Ors. The relevant extracts of the Judgment are reproduced below:

> *"6) It is submitted on behalf of the appellant that when working capital is funded through internal sources of the appellant, the internal funds also carry cost. It is further submitted that such funds employed elsewhere would have carried interest income.*

7) The Commission observed that in actual fact no amount has been paid towards interest. Therefore, the entire interest on working capital granted as pass through in tariff has been treated as efficiency gain. It is true that internal funds also deserve interest in as much as the internal fund when employed as working capital loses the interest it could have earned by investment elsewhere. Further the licensee can never have any funds which has no cost. The internal accruals are not like some reserve which does not carry any cost. Internal accruals could have been inter corporate deposits, as suggested on behalf of the appellant. In that case the same would also carry the cost of interest. When the Commission observed that the REL had actually not incurred any expenditure towards interest on working capital it should have also considered if the internal accruals had to bear some costs themselves. The Commission could have looked into the source of such internal accruals and the cost of generating such accruals. The cost of such accruals or funds

could be less or more than the normative interest. In arriving at whether there was a gain or loss the Commission was required to take the total picture into consideration which the Commission has not done. It cannot be said that simply because internal accruals were used and there was no outflow of funds by way of interest on working capital and hence the entire interest on working capital was gain which could be shared as per Regulation No. 19. Accordingly, the claim of the appellant that it has wrongly been made to share the interest on working capital as per Regulation 19 has merit".

Accordingly, the above issue is decided in favour of the Appellant.

16. **Summary of our findings**

16.1.The first issue is regarding the delay in implementation of directions of the Tribunal in true up of the financials and the need for second public hearing before the true up. The State

Commission has given explanation for the activities for carrying out the study by the independent agency. Considering that such a study was being carried out for the first time, limited response from bidders and extensions sought by the bidders for submission of bids, we do not find that any blame can be put on the State Commission for delay in instituting the study. Regarding the public hearing, in our view the State Commission had correctly decided to issue public notice under Section 64(3) for issues where the State Commission had to devise new norms or new schemes or charges. The Tribunal had not given a clear finding on these issues which could be directly adopted by the State Commission. Accordingly, the State Commission had to reconsider these issues afresh and then decide.

Thus, the decision of the State Commission for obtaining suggestions and objections from the public in its order dated 19.1.2010 was correct and in the interest of principles of natural justice.

16.2. The next issue is regarding Operation and Maintenance Expenses. The Appellant's limited grievance is computation of the base year figures for arriving at O&M expenses for the subsequent years. The contention of the Appellant is that the State Commission has considered net O&M expenses after deducting the O&M expenses which were booked to the Capital Works and hence capitalised. According to the learned counsel for the Appellant some capital works were in progress during FY 2006-07, which may not recur in the subsequent years. Non-consideration of employees expenses booked to capital expenses will

eventually increase the gap between actual and normative expenses, in case no renovation and modernization is taken up at the power stations in the subsequent years. On the other hand, the learned counsel for Respondent-1/State Commission had argued that the Appellant had not made any such claim before the State Commission. On examination of the petition, we find that the issue now being raised before the Tribunal was not raised before the State Commission. The contention of the Appellant is also based on some presumptions of not carrying out works of capital nature in the subsequent years. The Appellant has not given any facts and figures in respect of true-up for the FY 2007-08 to establish its contentions. The Regulations also do not deal with gross and net O&M expenses and employees expenses booked

to capital works. In view of this, we do not find any reason to interfere with the orders of the State Commission on O&M expenses. However, we give liberty to the Appellant to place the issue of gross/ net O&M expenses raised in this Appeal before the State Commission for consideration in subsequent True Up/Tariff petition and the State Commission shall consider the same so that the Appellant is not denied of the legitimate O&M expenses on account of booking of the O&M expenses on capital works.

16.3. The next issue is regarding truing up of fuel costs for the years 2005-06 to 2007-08. We find that the State Commission has passed a reasoned order for not accepting the base heat rate as per the assessment of CPRI for the past period based on theoretical assumptions of degradation factor.

The State Commission has also recorded observations of CPRI regarding changes made in measurement of the Station Heat Rate and calorific value during FY 2008-09 to ensure correctness of heat rate determination. We are in agreement with the methodology used by the State Commission for true up for the FY 2005-06 to 2007-08 and we also find that no loss has been caused to the Appellant by adopting the actual fuel expenses for the past period.

16.4. The next issue is regarding the carrying cost of deferred true up. The State Commission has allowed carrying cost for true up of past period commencing from 2005-06 till 31.3.2010 whereas the actual recovery in is spread over a period of 12 months in the FY 2010-11. We feel that this is a correct approach. The Commission has correctly

allowed carrying cost for the period the recovery of the amount was deferred. Accordingly, this issue is decided against the Appellant.

16.5. The next issue is regarding deferred tax liability for computation of Return on Equity. The deferred tax liability can not be added to the equity base unless it is established that such liability has been created in perpetuity. We feel that the deferred tax liability of the Appellant has not been created in perpetuity. Therefore, we hold that the Commission has correctly decided not to include the deferred tax liability in the equity.

16.6. The next issue is non-consideration of station-wise Advance Against Depreciation. The State Commission has determined station-wise tariff. Regulation 32.3 also provides for AAD

specific to a generating station. If the Regulations provide for AAD for a generating station, it should not be denied on some other grounds which do not form part of the Regulation. Accordingly, this issue is decided in favour of the Appellant with the directions to the State Commission to determine station-wise AAD.

16.7. The next issue is regarding Reactive Energy Charge. The State Commission in the impugned order has clarified that no expenditure is being incurred by the Appellant for injection of reactive energy that is not being compensated. We do not find any infirmity in the orders of the State Commission and uphold its findings.

16.8. The next issue is erroneous period of spread for bad and doubtful debts. The State Commission

has allowed recovery of bad and doubtful debts for the period from 2005-06 to 2007-08 and has allowed the claim under this head to be recovered from the consumers for the FY 2008-09. The Appellant has argued that the same should be allowed from 2005-06. The Tribunal in its Judgment dated 10.4.2008 had not allowed any interest and had directed for sharing of burden. We feel that the State Commission has correctly implemented the direction of the Tribunal. Accordingly, this issue is decided against the Appellant.

16.9. The next issue is regarding interest on Working Capital. According to the Appellant, the State Commission has wrongly disallowed interest on Working Capital without considering that the working capital requirements were met through

the internal accruals. This issue has already been decided by this Tribunal in its Judgment dated 28.5.2009 in Appeal No. 111 of 2008 in the matter of Reliance Infrastructure Ltd. vs. MERC & Ors. Accordingly, this issue is decided in favour of the Appellant.

17. In view of the above, the Appeal is allowed partly. The State Commission is directed to implement the directions given in this Judgment expeditiously preferably within a period of three months from the date of this order. No order as to cost.

18. Pronounced in the open court on this ***27th day of April, 2011***.

(Justice P.S. Datta) (Rakesh Nath) (Justice M. Karpaga Vinayagam)
Judicial Member Technical Member Chairperson

REPORTABLE / NON-REPORTABLE

vs