APPELLATE TRIBUNAL FOR ELECTRICITY
(APPELLATE JURISDICTION)

Appeal No. 153 of 2009

Dated 30th July, 2010

Present: **Hon'ble Mr. Justice M. Karpaga Vinayagam, Chairperson**
Hon'ble Mr. Rakesh Nath, Technical Member

Appeal No. 153 of 2009

In the matter of:

1. North Delhi Power Ltd.
Grid Sub-Station Building
Hudson Lanes, Kingsway Camp
Delhi-110 009 … Appellant
Versus

1. Delhi Electricity Regulatory Commission
Viniyamak Bhawan
C-BLCk, Shivalik, Malviya Nagar
New Delhi-110 001 … Respondent

Counsel for the Appellant **Mr. Amit Kapoor and**
Ms. Poonam Verma

Counsel for the Respondent **Mr. A.N. Haksar, Senior Counsel**
Ms. Purnima Sapra
Mr. Pradyuman

JUDGMENT

PER HON'BLE MR. JUSTICE M. KARPAGA VINAYAGAM, CHAIRPERSON

1. North Delhi Power Limited, is the Appellant herein. Delhi Electricity Regulatory Commission (State Commission) is the Respondent herein.

2. The Appellant filed a Petition before the State Commission for approving the truing up for the FY 2007-08. The State Commission by the Order dated 28.05.2009 allowed some claims and rejected the other claims made by the Appellant. Hence, the present Appeal by the Appellant as against the disallowance of the said claims.

3. The short facts of the case are as follows.

4. The Appellant is a company engaged in the business of distribution and retail supply of electricity in the North and North-west circle of National Capital Territory of Delhi. It is a

successor in interest of the erstwhile Delhi Vidyut Board. The Appellant functions under the regulatory control and supervision of the Delhi Electricity Regulatory Commission.

5. The State Commission notified the DERC (Terms and Conditions for Determination of Wheeling Tariff and Retail Supply Tariff) Regulations 2007 on 30.05.2007.

6. On 02.12.2008, the Appellant filed its petition before the State Commission for truing up of the tariff order in respect of. FY 2007-08 as well as for the determination of the ARR for the FY 2009-10. In the said petition, the State Commission conducted a hearing on the admission of the petition on 19.12.2008. Thereupon on 23.12.2008, public notice was published inviting objections and suggestions from the general public, in the various newspapers. After collecting all the objections and suggestions from the public, the State Commission conducted public hearings to discuss the issues from 25th to 27th February 2009. Ultimately, on 28.5.2009 the State

Commission passed the impugned order, allowing some claims and rejecting other claims made by the Appellant. Hence this Appeal.

7. The Learned Counsel appearing for the Appellant would raise the following grounds in this Appeal while assailing the impugned order in respect of the claims rejected in the truing up order for the FY 2007-08.

(i) The State Commission has concluded that any delay in payment by the consumers beyond the normal credit period entails additional cost which need to be allowed, since the late payment surcharge levied for such a delayed payment is treated as a non-tariff income. The above-said principle adopted by the State Commission is erroneous, and it has resulted in denial and miscalculation of the financial cost of late payment to the tune of Rs. 9.5 crores. The financial cost should have been allowed on Rs. 84.89 crores of the principal amount which was outstanding beyond the due date rather than on Rs. 15.28 crores as erroneously held by the State Commission.

(ii) The State Commission has acted contrary to the regulations 5.7 and 5.2.3 of the MYT Regulations to adjust the rebate claimed by the Appellant on earlier payment of power purchase adjusted against power purchase cost. The approach of the State Commission in deducting the rebate from power purchase cost in the impugned order is a clear departure from its own stand on payment of rebate in the MYT order as well as against the earlier tariff order in which it was held that it would treat the rebate earned on power purchase cost as a part of non-tariff income. The rebate offered by the generating company is an incentive given to the Appellant, being a distribution company for their pre-payment from their own revenues for which no additional cost is allowed to them. If the Appellant is not allowed to retain the same as a part of non-tariff income for tariff determination as against the power purchase cost, this incentive would become meaningless. Allowing any rebate income beyond 1% to be retained by the distribution company will not adversely impact the consumers as the rebate allowed by the generation company to the distribution company for pre-payment of power purchase bills on the date of raising of bill is out of and not in addition to the normative working capital allowed to the generation company as part of tariff.

(iii) In the impugned order, the State Commission has considered the interest income for the FY 2007-08 as part of the non-tariff income for tariff determination purposes on the ground that such income is incidental to electricity business. This is a wrong approach. The State Commission ought not to have treated this interest income as incidental to the electrical business in view of the fact that these earnings are primarily related to the investment of surplus funds arising due to the efficiency in working capital management and share-holder funds retained in the business till the same are paid as dividends.

(iv) The Appellant is aggrieved by the order of the State Commission rejecting to allow a realistic cost of fund for the carrying cost by blindly arriving at a figure of 9% per annum. This order was passed based upon the Tribunal order reported in 2007 ELR (PTEL) 1370. This is wrong because the interest rate in FY 2004-05 was 9% and the same was used by the Tribunal as the base for allowing 9% carrying cost. But now the rate has substantially increased in the FY 2008-09. The working capital interest rate during FY 2008-09 was in the range of 11-12% per annum. Therefore, the rate fixed by the State Commission has to be reconsidered, as the rate of carrying cost can be allowed at weighted average cost of prevailing rate of debt for 70% of the amount and cost of the equity for the balance 30% of the amount.

(v) The State Commission disallowed additional charges incurred by the Appellant for submitting the Letters of Credit and payment security in respect of various Power Purchase Agreements entered for procurement of power for its area supply to the tune of Rs. 13 lakhs. The State Commission has ignored the settled industry practice and the fact that the charges for obtaining the LC as payment security for power purchase are incurred directly in relation to total cost of power purchase over which the Appellant has no control as has been recognized by the State Commission by considering the power purchase cost as an uncontrollable expenditure in terms of Regulation 4.2(f) and 4.16 (a) of the MYT Regulations. Therefore, the State Commission may be directed to allow the additional expenditure incurred to the tune of

Rs. 13 lakhs as this pertains to the new Power Purchase Agreement entered in FY 2007-08.

8. On behalf of the Appellant the following authorities have been cited:.

(1) Judgment dated 21.07.2006 as reported in 2007 ELR (APTEL) 1370 in BSES Rajdhani Power Ltd. V. DERC, New Delhi & Ors.

(2) Judgment dated 23.05.2007 as reported in 2007 APTEL 193 in North Delhi Power Limited v. Delhi Electricity Regulatory Commission.

(3) Judgment dated 15.02.2007 as reported in (2007) 3 SCC 33 in Delhi Electricity Regulatory Commission v. BSES Yamuna Power Limited & Others.

(4) Judgment dated 23.03.2010 in Appeal No. 68 of 2009 in Torrent Power Limited v. Gujarat Electricity Regulatory Commission

(5) Judgment dated 06.10.2009 in Appeal No. 36 of 2009 as reported in 2009 ELR (APTEL) 0880 in BSES Rajdhani Power Limited v. Delhi Electricity Regulatory Commission

(6) Judgment dated 29.09.2006 as reported in 2007 ELR (APTEL) 1310 in BSES Yamuna Power Limited v. D.E.R.C. and NDPL v. DERC

(7) (1978) 1 SCC 405 in Mohinder Singh Gill and Anr. Vs. The Chief Election Commissioner, New Delhi and Ors.

(8) Judgment dated 26.04.2010 passed by; the Tribunal in Appeal No. 72 of 2009 in Haryana Power Generation Corporation Ltd. Vs. Haryana Electricity Regulatory Commission and Ors.

(9) Judgment dated 31.07.2009 passed by the Tribunal in Appeal No. 42 of 2008 in Haryana Power Generation Corporation Limited vs. Haryana Electricity Regulatory Commission and Anr.

(10) Judgment dated 03.0010.2002 as reported in (2002) 8 SCC 715 in West Bengal Electricity Regulatory Commission vs. CESC Limited.

(11) Judgment dated 09.03.2010 as reported in (2010) 3 SCC 732 in Secretary and Curator, Victoria Memorial Hall vs. Howrah Ganatantrik Nagrik Samity & Others.

(12) Judgment dated 19.09.2007 passed by Tribunal in Appeal No. in the case of Maharashtra State Electricity Distribution Co. Ltd. Vs. Maharashtra Electricity Regulatory Commission.

(13) (2008) 3 SCC 128 in LML Limited vs. State of Uttar Pradesh & Others.

(14) Judgment dated 17.10.2003 as reported in (2004) 1 SCC 195 in the case of BSES Limited vs. Tata Power Co. Ltd. And Others.

(15). Judgment dated 11.12.2003 as reported in (2004) 2 SCC 579 in the case of N.C. Dhoundial vs. Union of India and Others.

(16) Judgment dated 17.12.2002 as reported in (2003) 3 SCC 186 in the case of Cellular Operator Association of India & Others vs. Union of India and Others.

(17) Judgment dated 15.03.2010 passed by the Hon'ble Supreme Court of India in Civil Appeal No. 3902 of 2006 in PTC India Ltd. Vs. Central Electricity Regulatory Commission.

(18) Judgment dated 06.03.2002 reported as (2002) 3 SCC 711 in Association of Industrial Electricity Users vs. State of A.P. and Others.

9. The Learned Senior Counsel for the State Commission would make elaborate and effective submissions to the effect that the State Commission order rejecting these claims would correctly project the reasonings for the same and, therefore, the order impugned does not warrant any interference.

10. The Learned Senior Counsel for the State Commission has cited following authorities for defending the order of the State Commission:

(1) Judgment dated 12.01.1993 as reported in Manu/SC/0462/1993 in the case of Ashok Soap Factory and Anr. Vs. Municipal Corporation of Delhi and Ors.

(2) Judgment dated 09.11.2005 as reported in Manu/EE/2745/2005 in the case of Madhu Garg Vs. NDPL & Ors.

(3) Judgment dated 23.05.2007 passed in Appeal Nos. 265, 266 and 267 as reported in 2007 APTEL 193 in North Delhi Power Limited v. Delhi Electricity Regulatory Commission.

(4) Judgment dated 01.08.1980 as reported in MANU/SC/00406/1980 in the case of State of Tamil Nadu Vs. Binny Ltd., Madras.

(5) Judgment dated 19.12.1985 reported as1986 (1) SCC 264 in LIC of India versus Escorts Limited

(6) Judgment dated 03.03.2005 reported as MANU/SC/0172/2005 in the case of Rekha Mukherjee Vs. Ashis Kumar Das and Ors.

(7) Judgment dated 21.07.2006 passed by the Tribunal in Appeal Nos. 155, 156 and 157 of 2006 in the case of BSES Rajdhani Power Ltd. Vs. DERC & Ors.

(8) Judgment dated 05.05.1978 as reported in MANU/SC/0291/1978 in the case of Workmen of Cochin Port Trust Vs. Board of Trustees of the Cochin Pot Trust and Anr.

(9) Judgment dated 20.04.1960 as reported in MANU/SC/0295/1960 in the case of Satyadhyan Ghosal and Ors. Vs. Smt. Deorajin Debi and Anr.

(10) Judgment dated 11.05.1999 reported as MANU/SC/0352/1999 in the case of Hyderabad Industries Limited & Anr. Vs. Union of India and Ors.

(11) Judgment dated 16.02.2009/17.02.2009 reported as MANU/GJ/0106/2009 in the case of ACIT Vs. Patel Specific Family Trust.

(12) Judgment dated 03.08.1983 reported as MANU/MP/0145//1983 in the case of Electrofab Industries Vs. Sales Tax Officer and Anr.

(13) Judgment dated 08.04.2009 reported as MANU/GJ/0223/2009 in the case of Assistant Commissioner of Gift Tax Vs. Syabiotics Ltd.

11. Both the learned Counsel for the parties thus have cited above authorities in support of their respective submissions. We have considered the same carefully and perused the impugned order and other records.

12. This Appeal gives rise to the following questions of law for adjudication by this Tribunal:

(i) Whether the State Commission was justified in wrongly limiting the finance cost for delayed payment surcharge by consumers to the late payment surcharge receipt of around Rs. 15 crores instead of the principal amount of outstanding dues of around Rs. 85 crores?

(ii) Whether the State Commission was justified in acting contrary to the MYT Regulations in wrongly reducing the rebate due to early payment of power purchase from the ARR?

(iii) Whether the State Commission was justified in acting contrary to its past tariff orders and in wrongly deducting the interest of surplus funds, even share-holders money, efficiency in working capital from the ARR and treated as non-tariff income?

(iv) Whether the State Commission was correct in considering the inappropriate lower rate for allowance of carrying cost at a rate of 9%?

(v) Whether the State Commission was justified in not allowing LC charges incurred on procurement of power under new Power Purchase Agreement?

13. Let us now deal with each of the issues one by one.

14. The first issue relates to the denial of financing cost on outstanding dues by limiting it to interest on late payment surcharge. According to the Appellant, the State Commission having found that there is financial cost associated with the delayed payment surcharge, has erred in computing the said cost on two counts: (a) Applying the carrying cost on the wrong base, i.e. instead of total amount of shortfalls, the State Commission applied it to the late payment surcharge alone; and (b) Allowing carrying cost at a lower rate as compared to the then prevailing market lending rate. The prayer on this issue made by the Appellant is that the financing cost of outstanding dues, i.e.

principal amount, should be allowed at a rate which equals the prevailing interest rate for working capital loans. In short, the Appellant prays that the financing cost should have been allowed in respect of the entire principal amount which was outstanding, i.e. Rs. 84.89 crores, instead of Rs. 15.28 crores at the interest rate of 12%, that is the prevalent cash credit interest rate, instead of 9% allowed by the State Commission.

15. In reply to the above submission, it was submitted by the Learned Senior Counsel for the State Commission that the claim of interest/carrying cost in respect of the entire principal amount is not in consonance with the MYT Regulations and since the late payment surcharge itself is in the nature of financing cost, it compensates it for the cost of financing the shortfall in cash flow due to the late payment by the consumers. It is also contended that the carrying cost at the rate of 9% per annum was fixed by the State Commission only on the basis of the Tribunal judgment reported in 2007 ELR (APTEL) 1370 and therefore, finding by the Commission is correct.

16. While dealing with this issue in the light of the rival contentions urged by the Counsel for the parties, it would be worthwhile to refer to the findings given by the State Commission in the impugned order, as under:

> "*3.93. As regards the delayed payment surcharge collected by the Petitioner during the year, the Commission is of the opinion that there is a financing cost associated with the delayed payment surcharge. Therefore, while computing the delayed payment surcharge, the Commission has deducted the carrying cost of financing the same @ 9% per annum.*"

17. The above observation would make it clear that the State Commission has given a finding that the Appellant is entitled to the financing cost interest/financing cost associated with the delayed payment surcharge. It is not the case of the State Commission in the impugned order that the MYT Regulations do not provide the financing cost associated with the delayed payment surcharge. The question whether the financing cost to be

calculated in respect of the entire outstanding dues, namely the principal amount, has not been considered. On the other hand, the State Commission has limited the financing cost to the late payment surcharge amount alone.

18. In the light of the above situation, this issue has got to be considered. Late payment surcharge is levied on consumers who do not make timely payment of their electricity bills. Due to the delay in making the payment, there is a shortfall in cash flow available with the distribution company to incur its expenses. In such a situation, to meet such shortfall in cash flow, the Appellant being a distribution company is constrained to meet the expenses either through internal accruals or borrowings. The State Commission having felt that the delay in payment by the consumers beyond the normal period entails the additional cost which needs to be allowed since the late payment surcharge levied which compensates for such a delayed payment is treated as non-tariff income.

19. According to the MYT Regulations, the non-tariff income is deducted from Aggregate Revenue Requirements to work out the Net Revenue Requirement. Working capital cost for financing the Receivables of revenue within the due date is allowed in tariff determination. As such, no late payment surcharge is leviable or earned for Receivable Liquidated up to due date. The late payment surcharge is levied on consumers who do not make payment within the stipulated period allowed for payment. This compensates the licensee for the interest cost that would be incurred on the additional working capital requirements due to consumers not paying their dues in time. Therefore, the entire late payment surcharges should accrue to the licensee to off-set additional financing costs of incremental working capital requirement beyond the normative two months receivables allowed in working capital. However, as per the Tariff Regulations, the amount received by the Licensee on account of Non-Tariff Income is deducted from the Aggregate Revenue Requirement in calculating the Net Revenue Requirement of the Licensee.

20. The State Commission having treated the late payment surcharge as a part of the non-tariff income for tariff determination, it would be proper on its part to allow the entire associated financing cost of the outstanding principal amount on which late payment surcharge was charged for the delay beyond the due dates. The Commission, instead of allowing interest/financing cost on the entire outstanding principal amount, has treated the late payment surcharge amount alone, which is nothing but interest cost for the delayed payment, as outstanding principal amount itself and allowed interest/financing cost on the said amount. This is a wrong approach. Having considered the entire late payment surcharge as principal outstanding amount beyond due date as a non-tariff income, the State Commission should have allowed the entire cost computed by applying an appropriate financing rate to the said principal amount on which late payment surcharge has been levied. According to the Appellant, the financing cost should have been allowed on Rs. 84.89 crores of principal amount which was outstanding beyond

the due date rather than on Rs. 15.28 crores which is late payment surcharge, as erroneously calculated by the State Commission.

21. It has been strenuously contended by the Learned Senior Counsel for the State Commission that the Appellant has failed to point out any MYT Regulations conferring right to the distribution companies to claim financing cost relating to delayed payments. The Appellant by way of rebuttal has pointed out the Regulation 5.7, 5.23, 5.37 of the MYT Regulations to justify the claim made by the Appellant. Let us quote those Regulations as under:

> "***Regulation 5.7*** *The RRB shall be determined for each year of the Control Period at the beginning of the Control Period based on the approved capital investment plan with corresponding capitalisation schedule and normative working capital.*"

> "***Regulation 5.23*** *All incomes being incidental to electricity business and derived by the Licensee from sources, including but not limited to profit derived from disposal of assets, rents, delayed payment*

surcharge, meter rent (if any), income from investments other than contingency reserves, miscellaneous receipts from the consumers and income to Licensed business from the Other Business of the Distribution Licensee shall constitute Non-Tariff Income of the Licensee."

***"* <u>*Regulation 5.37*</u>** *Working capital for retail supply of electricity shall consist of:*

(1) Receivables for two months of revenue from sale of electricity; and

(2) Operation and maintenance expenses for one month; and

(3) Less power purchase cost for one month.

22. On the basis of the above Regulations, it is submitted on behalf of the Appellant that:

(i) the Working Capital cost for financing Receivable Liquidated within due date is allowed in tariff regulations. As such, no late payment surcharge is leviable or earned for receivable liquated up to due date;

(ii) the late payment surcharge is levied in Delhi at 1.5% per month. In the earlier tariff order, the State Commission allowed on entire outstanding amount beyond the due date which goes towards compensating the cost of financing such outstanding amount beyond the due date.

On the other hand, it was submitted on behalf of the State Commission that normative working capital takes into account the fact that the distribution companies will not be paid immediately.

23. In the light of the aspects pointed out on behalf of the Appellant, the reply made on behalf of the State Commission may not be correct for the reasons given below:

(i) The normative working capital compensates the distribution company in delay for the 2 months credit period which is given to the consumers.

(ii) Admittedly, the late payment surcharge is charged only if the delay is more than normative credit period.

(iii) Thus, for the period of delay beyond the normative period, the Distribution company has to be compensated with the cost of such additional financing.

24. It is not the case of the Appellant that the late payment surcharge should be treated as non-tariff income and should be retained by the Appellant. The Appellant is only praying that the financing cost is involved in earning late payment surcharge and as such the Appellant is entitled for compensation to incur such additional financing cost. Therefore, the financing cost of outstanding dues, i.e. the entire principal amount, should be allowed and it should not be limited to late payment surcharge amount alone.

25. According to the Appellant, the interest rate which was fixed as 9% is not under the prevalent prime lending rate. On behalf of the State Commission, it was pointed out that the 9% has been fixed by the State Commission only on the strength of the judgment of the Tribunal dated 21.07.2006 reported in 2007 ELR (APTEL) 1370. It is true that the Tribunal in that case fixed the interest rate as 9%. In that case, the tariff order was passed by the Commission on 09.06.2004. At that time, the prevailing lending rate was around 9%, which was much lower as compared to that prevailing rate during the year 2007-08. Therefore, the said decision would not apply to the present case. While fixing the interest rate, the State Commission should have considered the prevalent SBI prime lending rate. Even in the said judgment, the Tribunal has laid down the principle that the rate of carrying cost must be derived from prevalent prime lending rates. As such, this principle has not been followed in this case. According to the Tariff Regulations, the cost of debt has to be determined considering Licensee's proposals, present cost of debt already contracted by the Licensee and other relevant factors viz. risk free

returns, risk premium, prime lending rate, etc. Therefore, we deem it appropriate to direct the State Commission to rectify its computation of financing cost relating to the late payment surcharge and consequently reduce the amount of non-tariff income considered by the State Commission as available for the tariff determination for the FY 2007-08 at the prevalent market lending rates. Accordingly ordered.

26. Let us now come to the second issue. The second issue relates to deduction of the rebate due to the early payment for the power purchase cost from the ARR. According to the Appellant, the State Commission wrongly adjusted the rebate earned by the Appellant by making early payment of power purchase as against the power purchase cost. It is contrary to the Regulation 5.7 and 5.23 of the MYT Regulations which allow rebate income to be retained by the distribution company and this does not adversely impact the consumers as the rebate allowed by the generation companies to the distribution companies for pre-payment of the power purchase bills is out of the normative working capital cost and not in addition to the normative working capital cost allowed.

It is further contended on behalf of the Appellant that if the payment is made within 30 days of the due date, the distribution company is entitled to 1% rebate and the said rebate can be treated as the non-tariff income but if the rebate earned is above 1% it cannot be treated as a non-tariff income, as the same is purely due to the efficiency of the distribution company/the Appellant.

27. In reply to the above submissions, it is strenuously contended on behalf of the State Commission that the rebate is a part of the non-tariff income as per MYT Regulations; the amount for rebate reduces the burden of power purchase cost, and therefore, the State Commission has reduced the rebate earned on account of power purchase from the gross power purchase cost as it is in consonance with the MYT Regulations.

28. It is not disputed that the rebate is a commercial arrangement between the generation companies and the distribution companies. The purpose of granting rebate to the distribution companies is in order to incentivize the distribution companies to make their payment of the bills for the power

purchase to the generation company promptly before due date of the bill. The rebate of 2% is allowed to the distribution companies if the bill is paid through letter of credit on presentation. The rebate of 1% is allowed if the distribution company pays to the generating company by a mode other than the letter of credit within one month of presentation of bill. This rebate of 1% correlates to the working capital as provided for in Regulation 5.37 of the MYT Regulations.

29. It has been claimed by the Appellant that through its efficient management, the Appellant has paid all the bills immediately on raising of the bills by the generating company and therefore, it has been allowed a rebate of 2%. The distribution company is entitled to have 1% rebate if the payment is made within 30 days of presentation of bill and such rebate up to 1% can be treated as a non-tariff income. Admittedly, the State Commission has considered the rebate of 2% which has been earned by the Appellant as a part of the non-tariff income and deducted from Power Purchase Cost. The 2% rebate earned by the Appellant is only due to the efficiency of the Appellant which

is not provided in the working capital as per the MYT Regulations. Therefore, there is no justifiable reason for the State Commission to hold that the rate earned above 1% is a part of the non-tariff income. The rebate of 2% being not a part of the non-tariff income cannot be deducted from the power purchase cost. The rebate allowed is a cash discount available on early payment of power purchase bills. The rate of rebate is linked to the number of days for which the payment is made in advance. Therefore, the rebate earned by the Appellant over and above 1% should not be treated as non-tariff income and as such there cannot be any reduction from the power purchase cost.

30. It is pointed out on behalf of the Appellant that the State Commission has wrongly deducted the rebate earned by the Appellant, i.e. Rs.35.94 crores from the power purchase cost of Rs. 1882.10 crores. As per Regulation 5.7, allowance of interest on working capital on the basis of normative working capital utilization is provided. Any loss or gain arising on account of insufficient utilization of working capital or efficient utilization of working capital respectively shall be on account of distribution

company/the Appellant. Regulation 5.23 describes the non-tariff income. The Regulation does not provide for rebate being treated as a non-tariff income for the purpose of tariff determination.

31. Similarly, Regulation 5.37 provides for a cost of working capital on normative basis. The underlying principle is that any additional cost arising due to the inefficient management of working capital requirement is to the account of the distribution company and is not to be passed on in the ARR. Similarly any gain achieved by the distribution company due to its efficiency above the normative levels must go to the benefit of the distribution company. However, contrary to these regulations, the State Commission has ruled that such efficiency gained by the distribution company be passed on in the ARR in the form of reduction in power purchase cost.

32. It has also been pointed out, on behalf of the Appellant, that the State Commission has earlier passed an order dated 23.02.2008 (MYT order) upholding the rebate earned due to the payment of power purchase bills in less than one month should be treated as a non-tariff income but in the impugned order, the

State Commission has deducted the rebate earned by the Appellant from the power purchase cost and this finding is contrary to the earlier stand taken by the State Commission in the earlier order passed by the State Commission on 23.02.2008. This aspect has not been disputed by the State Commission. It is pointed out by the Learned Counsel for the Appellant that before the MYT regime, i.e. up to FY 2006-07 all expenses were allowed at actuals and the rebate was considered as non-tariff income and the entire interest on working capital was allowed as pass through in the ARR. But now rebate over 1% cannot be considered as non-tariff income and the interest on working capital is allowed on normative basis and is not a pass through on the basis of the actual cost incurred.

33. It is further pointed out on behalf of the Appellant that in the tariff order passed by the State Commission in respect of Delhi Transco dated 20.12.2007, it is held that rebate cannot be passed through in tariff as it is a commercial decision. So the same item of rebate cannot be treated as a non-tariff income in the hands of distribution company when it is not considered as

expenditure in the hands of generating company. If permitted, this would create a mismatch in energy accounting, negating the very foundation of double-entry system of accounting.

34. According to the State Commission, the rebate is a part of non-tariff income as per the MYT Regulations which is an essential part of the power purchase cost and the effect of MYT order as well as the impugned order is the same, in so far as treatment of rebate on power purchase cost is concerned and the distribution company would earn a rebate of 1% even if it pays the power purchase bills within 30 days of the due date and that by making the payment on time it cannot be construed that the distribution company are being efficient and on the contrary it has the duty to pay the bills in time. The State Commission relied upon the judgment of the Hon’ble Supreme Court reported in 1986 (1) SCC 264 – *LIC of India versus Escorts Limited.* We have gone through the said judgment. The perusal of the said judgment would make it evident that this is not applicable to the present facts of the case. In the present case the State Commission itself provided a format for ARR petition to be

submitted by the distribution companies. The format referred to in the ARR petition do not cover rebate income and do not provide for the subtraction of the rebate earned from the power purchase cost. By referring to the said formats, Form-1 and Form-11 and Form-1a, the Appellant is only providing additional documents to substantiate their claim that under MYT Regulations the rebate from the power purchase cost is not to be deducted from Power Purchase Cost and not to be included as a non-tariff income for determination of tariff. The Working Capital includes Power Purchase Cost for only one month. The generation company offers rebate of 2% on payment of presentation which takes place immediately after completion of the month. On the other hand the billing cycle of domestic consumers is bi-monthly and for Industrial and Commercial consumers taking supply at 11 KV and above it is monthly. The consumer also gets 15 days time for payment of bill after issue of bill. Thus there is mismatch between the receipt of payment from consumers and the payment to be made by distribution licensee for power purchase for getting 2% rebate. Applying the principle that all gains and losses on account of overachievement or underachievement in performance with respect to norms, have to be retained/borne by the distribution licensee, we hold that rebate over and above 1% can not be considered non-tariff income for reducing the ARR. In view of the same, it has to be concluded that the rebate earned on early payment of power purchase cost cannot be deducted from the power purchase cost and rebate earned only up to 1% alone can be treated as part of non-tariff income. Therefore, the finding on this issue by the State Commission is contrary to the law and spirit of the MYT Regulations as it defeats the very purpose of allowing cost on normative basis. It is also contrary to the principle of allowing cost on normative basis of working capital. On the one hand, the State Commission has reduced one month power purchase payment from the working capital requirement and on the other hand it has been observed that if the Appellant is making the payment earlier, the benefit of entire rebate is used for reducing the power purchase cost.

35. Therefore, it is clear from the above that treating rebate income for reduction from power purchase cost as per the impugned tariff order is contrary to the MYT Regulations. Rebate only to the extent of 1% is to be considered as non-tariff income. As such, the issue is answered accordingly.

36. The third issue relates to the wrongful deduction of interest on surplus funds out of the share-holders' money, efficiency in the working capital management, etc. from the ARR of the Appellant.

37. According to the Appellant, the State Commission has considered the interest income for the FY 2007-08 as part of non tariff income on the premise that such income is incidental to the electricity business. This finding is clearly wrong because these earnings are primarily related to investment of interim surplus funds arising due to the efficiency of the working capital management and the retention of the share-holders' funds in the business till the same are paid out as dividends. It is further stated by the Appellant, that as per Regulation 5.7 of the MYT Regulations, the working capital expenditure is allowed on

normative basis implying that any efficiency or inefficiency due to the working capital management is to the account of the distribution company/the Appellant. It is also pointed out that the State Commission invariably agreed on this point urged by the Appellant in all the earlier orders it did not treat such interest income as non-tariff income and having accepted the same in the earlier orders and also through clarification letter dated 21.01.2009 sent by the Appellant to the State Commission, the State Commission has wrongly passed the impugned order on this issue holding that the interest income of Rs. 3.06 crores is a part of the non-tariff income as the said income is incidental to the electricity business and as such it has to be deducted from the ARR of the Appellant.

38. On the other hand, the said submission has been rebutted by the State Commission by stating that the true up order of FY 2007-08 has been considered by the State Commission as per MYT Regulations prevalent as on date and it has no bearing on the previous tariff orders. It is further submitted on behalf of the State Commission that as per Regulation 5.23 of the MYT

Regulations which has been framed now, this item had to be included in the non-tariff income, especially when this interest income is incidental to the electricity business.

39. On a careful reading of the impugned order, relevant Regulations and also on consideration of the submissions made by the Senior Learned Counsel appearing for the State Commission, it becomes clear that the State Commission has treated the interest income as part of the non-tariff income for tariff determination mainly for the reason that such income is incidental to electricity business. Admittedly these earnings, as pointed out on behalf of the Appellant, are primarily related to (1) investment of interim surplus funds arising due to the efficiency in working capital management and (2) share-holders' funds retained in the business till the same are paid out as dividends. Hence the said interest income cannot be considered as incidental to electricity business.

40. Regulation 5.7 of the MYT Regulation provides that working capital expenditure is allowed on normative basis implying that any efficiency or inefficiency due to the working

capital management is to the account of the distribution company, namely the Appellant. The efficiency in working capital management or the better performance on parameters set for working capital would either result in (1) actual working capital cost being lower than the normative capital cost allowed by the State Commission or (2) the release of funds blocked in working capital which are invested by way of short-term investments, thereby earning investment income. Similarly there are other transient surplus funds which are invested to earn investment income which cannot be considered as a part of the non-tariff income for the purpose of tariff determination, such as return on equity which is retained in the business till it is paid out as dividend. As pointed out by the Learned Counsel for the Appellant, the Appellant has clarified the issue of interest income through its letter dated 21.01.2009 by submitting that the interest income should not be considered for tariff determination. As a matter of fact, earlier the State Commission accepted the Appellant's contention on the same issue and concluded that the interest income cannot be treated as a part of non-tariff income till FY 2006-07.

41. As per MYT Regulations 2007, i.e. Regulation 8.3 (h) and Regulation 5.7, any change in controllable parameters is to the account of the distribution company and, therefore, the benefit on account of achieving any AT&C loss and efficiency in either controllable parameters ought to have been allowed in favour of the distribution company. In other words, the interest on investment arising due to efficiency in working capital is required to be allowed to the Appellant. The Tariff Regulations define Non-Tariff income as income relating to Licenced business other than from tariff (Wheeling and Retail Supply). Therefore, interest on income from Retail Supply tariff cannot be considered as Non-Tariff income.

42. It is contended on behalf of the State Commission that the consumer's share of revenue from the over achievement of Aggregate Technical and Commercial Loss (AT&C loss) reduction target is with the distribution company and thus any interest income earned from such surplus funds needs to be

considered to reduce the ARR. There is a merit in this contention. According to Regulation 5.23 income from investment other than contingency reserve are included in the non-tariff income. Regulation 5.24 provides that interest on security deposit in excess of rates specified by the Commission in 'Delhi Electricity Supply Code and Performance Standard Regulations 2007' is to be considered as non-tariff income. Similarly interest on Delayed Payment Surcharge will earn some interest till the true up of financials. We have already decided above in favour of the Appellant the financing cost on outstanding dues. Thus the interest on Delayed Payment Surcharge has to be considered as non-tariff income to be deduced from the ARR. Thus the interest income on Delayed Payment Surcharge and on account of difference in interest rate on consumer security with respect to that specified by the Commission should be considered as non-tariff income for deduction in ARR. Also the credit of interest income on consumer's share in incentive on over achievement of AT&C losses should be given to the consumer by reducing the ARR to that extent. However, the Appellant has admittedly factored the same while computing the carrying cost on the revenue gap. Consequently the carrying cost is lower to that extent. Therefore, when the benefit of the same had already been passed on to the consumers, the same cannot be again passed on to them by way of interest cost. However, in order to correctly determine the ARR as per the Regulations, the interest on investment out of surplus funds generated by delayed payment surcharge and the difference in interest rate on consumer security with respect to rate specified in the Regulations may be taken as non-tariff income to be deducted from ARR. Similarly, credit for interest income on consumer's share of incentive on over-achievement of AT&C losses has to be deducted from ARR. Accordingly, if credit has given by the Appellant in carrying cost for interest income, adjustment may be made in the carrying cost on the revenue gap to ensure that double deduction on this account does not take place. The receivable money, i.e. return on equity/incentive/carrying cost, etc. retained in the business either by periodical utilisation for meeting working capital requirements or by investing for short-term, thereby earning interest income. In both the circumstances, the benefit is to be retained by the Appellant for the benefit of its share-holders since the original amount deployed for meeting working capital requirements are invested in mutual funds/banks belonging to the share-holders. While deployment of such funds for meeting working capital requirements results in the benefit being retained by the distribution company for its share-holders by way of reduction in working capital cost, vis-a-viz the normative interest cost allowed in tariff in a latter case where such funds are invested. The State Commission cannot erode the benefit to be derived by the distribution company by considering such interest income as part of non-tariff income to be deducted from ARR. Therefore, the finding on this issue by the State Commission is wrong. Consequently the interest income only on delayed payment surcharge and difference of interest rate on consumer security till the true up of financials should be treated in the non-tariff income. Interest income on surplus on account of retail supply tariff except the consumer's share in incentive on over-achievement of AT&C losses cannot be deducted from the ARR.

The Commission will compute the interest income for which credit has to be given to consumer from the total interest income. This point is answered accordingly.

43. The next issue is relating to the inadequate lower rate of 9% for the allowance of the carrying cost, ignoring the prevalent MYT Regulations and prime lending rate.

44. According to the Appellant, the State Commission allowed the carrying cost @ 9% per annum by merely adopting the rate allowed by the Tribunal in its judgment reported in 2007 ELR (APTEL) 1370. This finding is wrong because the rate of 9% was fixed by the Tribunal in the said judgment as the same was based on the then prevailing rate. Now the rate has been increased significantly. Therefore, the fixation of the lower rate is wrong. On the other hand, the learned Senior Counsel appearing for the State Commission has submitted that MYT Regulations do not provide for any carrying cost nor rate thereof and the impugned order relating to the true up order of FY 2007-08 has been correctly considered as per MYT Regulations and it has no bearing on the previous tariff orders where the State Commission

approved any such interest income and that the State Commission has provided the carrying cost @ 9% in line with the Tribunal's judgment dated 21.07.2006 and therefore, the finding cannot be said to be wrong.

45. The carrying cost is allowed based on the financial principle that whenever the recovery of cost is to be deferred, the financing of the gap in cash flow arranged by the distribution company from lenders and/or promoters and/or accruals, has to be paid for by way of carrying cost. This principle has been well recognised in the regulatory practices as laid down by this Tribunal as well as the Hon'ble Supreme Court. In 2007 APTEL 193, this Tribunal has held that "along with the expenses, carrying cost is also to be given as legitimate expense". Hon'ble Supreme Court in 2007 (3) SCC 33 has also held "the reduction in the rate of depreciation is violative of the legitimate expectation of the distribution company to get lawful and reasonable recovery of expenditure".

46. In view of the above ratio, it is evident that the carrying cost is a legitimate expense and, therefore, recovery of such carrying

cost is legitimate expectation of the distribution company. According to the Learned Senior Counsel appearing for the State Commission, the rate of carrying cost was fixed in line with the judgment of this Tribunal where 9% rate was fixed. We are of the opinion that the said judgment would not apply to the present facts of the case in the light of the following:

> "*That rate of 9% was fixed by the Tribunal in that Appeal as the same was on the basis of the then prevailing lending rate.*"

47. The State Commission, instead of applying the principle of allowing the prevailing market rate for debt for the carrying cost, has allowed the rate of 9% on the strength of the Tribunal judgment even though the present interest rate has increased significantly. As pointed out by the Counsel for the Appellant, the State Commission in the earlier case had decided tariff on 09.06.2004 and that on commercial borrowings an interest rate of 9% had been applied considering the then prevalent prime lending rates. Therefore, the State Commission before fixing the

rate of carrying cost, has to find out the actual interest rate as per the prevailing lending rates. Admittedly, this has not been done.

48. According to the Senior Learned Counsel for the State Commission, MYT Regulations do not provide for any carrying cost or rate thereof. In this context, relevant extracts of Regulation 5.42 are to be quoted below:

> "***Regulation 5.42:*** *Variations on account of uncontrollable items like energy sales and power purchase cost shall be trued up. Truing-up shall be carried out for each year based on the actual/audited information and prudence check by the Commission:*
>
> *Provided that if such variations are large and it is not feasible to recover in one year alone, the Commission may take a view to create a regulatory asset, as per the guidelines provided in clause 8.2.2 of the National Tariff Policy".*

49. As per these regulations, the State Commission has to be guided by clause 8.2.2 of the National Tariff Policy. As per this clause of National Tariff Policy, the carrying cost of regulatory asset should be allowed to the utility. The working capital interest rate during the tariff period in question namely FY 2007-08 were

in the range of 11-12% per annum. As referred to in several letters issued by various banks to the Appellant, the commercial lenders are not willing to finance these requirements solely through the debt, with part financing through internal accruals/equity being a pre-requisite for commercial lending. Admittedly, the prevailing lending rate was higher than the rate fixed by the State Commission in their tariff order.

50. The working capital is being allowed by the State Commission on normative basis in line with the MYT Regulations. These Regulations would imply that it is controllable parameters which is not to be trued up. Any loss/saving in interest on working capital is to the account of the distribution company. When there is some savings on this account, the State Commission cannot deny the benefit of the same to the distribution company to enable it to utilise the same to meet the other requirements. As a matter of fact, the Appellant claim is in line with the State Commission view that the carrying cost is to be allowed in the ratio of 70:30. It is also pointed out by the Appellant that there is no increase in consumer tariff in Delhi

since 2005-06 except for a meagre increase of 5 paise from March 2008, whereas there has been significant increase in the cost of electricity procurement by the Appellant and implementation of the wage revision pursuant to the Sixth Pay Commission Recommendations. As mentioned earlier, MYT Regulations provide for a carrying cost and, therefore, the contention of the State Commission that MYT Regulations do not provide for carrying cost is not tenable.

51. It cannot be disputed that the State Commission shall be guided by the principles that reward efficiency in performance as provided under section 61(e) of the Electricity Act, 2003. Similarly, the said section provide that State Commission shall be guided by the National Electricity Policy and Tariff Policy. Therefore, the State Commission should have allowed the carrying cost at the prevailing market lending rate for the carrying cost so that the efficiency of the distribution company is not affected. The State Commission is required to take the truing up exercise to fill up the gap between the actual expenses at the end of the year and anticipated expenses in the beginning of the

year. This Tribunal in various judgments rendered by it held in Appeal No. 36 of 2008 in the judgment dated 06.10.2009 reported in 2009 ELR (APTEL) 880 has held that "*the true up exercise is to be done to mitigate the difference between the projection and actuals and true up mechanism should not be used as a shelter to deter the recovery of legitimate expenses/revenue gap by over-projecting revenue for the next tariff.*" Therefore, the fixation of 9% carrying cost, in our view, is not appropriate. Therefore, the State Commission is hereby directed to reconsider the rate of carrying cost at the prevailing market rate and the carrying cost also to be allowed in the debt/ equity of 70:30.

52. The next issue is relating to non-allowance of LC charges incurred on procurement of power under new PPAs. According to the Appellant, the actual LC charges incurred by the Appellant should be allowed by the State Commission as the same is not within the control of the distribution company/the Appellant, and also contrary to the MYT Regulations. On the other hand, it is submitted by the Learned Senior Counsel for the State Commission that the State Commission had reviewed the LC

charges, particularly when the State Commission approved the Operation & Maintenance cost for each year of the control period and assumed the growth on the A&G expenses based on the WPI and CPI and as such the additional cost claimed by the Appellant has already been factored at the time of approval of A&G expenses.

53. Let us now discuss this issue. The LC is a document issued by the bank on behalf of the buyer to guarantee the seller that the seller will be in receipt of full amount of payment on presenting the said LC. The LC charges are dependent on the rate of charges fixed by the bank which is not admittedly in the control of the Appellant. Similarly, the amount of power purchase cost incurred by the Appellant also is uncontrollable as recognized in the MYT Regulation 4.16(a).

54. The LC charges incurred by the Appellant are directly linked to the power purchase cost and varies in proportion to the increase/decrease in power purchase cost on which the Appellant has no control. The power purchase cost has no linkage with the

CPI/WPI. The LC charges incurred by the Appellant are directly linked to the power purchase cost.

55. For the FY 2002-03 to FY 2006-07, all costs namely power purchase cost, employees expenses, repair and maintenance expenses and A&G expenses were allowed by the State Commission based on actual expenditure incurred by the Appellant subject to prudent check. In these years all costs were treated as uncontrollable parameters. Further under various MYT regulations, more particularly Regulation 4.2 (f) which are applicable for the period between FY 2007-08 and FY 2010-11 the cost has been classified into controllable and uncontrollable parameters. The power purchase cost is classified as uncontrollable cost. Hence the entire cost incurred by the Appellant on power cost was allowed in the ARR subject to prudent check. On the other hand, the Operation & Maintenance expenses are classified as controllable costs and are allowed based on norms. These costs are not trueable and are not allowed based on the actual cost incurred. Thus, LC charges cannot be a part of A&G expenses.

56. Central Generation and Transmission Companies offer a rebate of 2% subject to opening of LC and making payment on presentation. Rebate of only 1% is payable if the payment is made within 30 days of presentation of the bill by a mode other than through LC. Thus, LC is not required for claiming 1% rebate if payment is made within one month. Delhi generation and transmission companies offer only 1% rebate for payment made within one month. We have held above that the working capital allowed by the Commission to distribution companies covers power purchase cost for one month and therefore, any rebate over 1% can be retained by the distribution company. The Appellant has also claimed that it has been able to make payment immediately due to its efficient management. Opening of LC is essential pre-requisite for claiming rebate of 2% from the Central generation and transmission companies and is not a pre-requisite for claiming rebate of 1% which is available when payment is made within a month. Thus, LC charges should logically be borne by the Appellant.

57. In view of the same, we hold that though LC charges are not part of Administrative & General (A&G) expenses but the same have to be borne by the Appellant as they are taking the benefit of rebate over and above 1%. Therefore, we uphold the Commission's view of not allowing LC charges to the Appellant.

58. **In view of the above discussion, the following is the summary of our findings:**

(i) The normative working capital compensates the distribution company in delay for the 2 months credit period which is given to the consumers. The late payment surcharge is only if the delay is more than the normative credit period. For the period of delay beyond normative period, the distribution company has to be compensated with the cost of such additional financing. It is not the case of the Appellant that the late payment surcharge should not be treated as a non-tariff income. The Appellant is only praying that the financing cost is involved due to late payment and as such the

Appellant is entitled to the compensation to incur such additional financing cost. Therefore, the financing cost of outstanding dues, i.e. the entire principal amount, should be allowed and it should not be limited to late payment surcharge amount alone. Further, the interest rate which is fixed as 9% is not the prevalent market Lending Rate due to increase in Prime Lending Rate since 2004-05. Therefore, the State Commission is directed to rectify its computation of the financing cost relating to the late payment surcharge for the FY 2007-08 at the prevalent market lending rate during that period keeping in view the prevailing Prime Lending Rate.

(ii) The second issue relates to the deduction of rebate due to the early payment of the power purchase cost from the ARR. The Appellant, through its efficient management, has paid all the bills immediately on raising of the bills by the

generating company and, therefore, it has to be allowed a rebate of 2%. Therefore, there is no justifiable reason for the State Commission to reduce the power purchase cost by rebate earned by the Appellant. The normative working capital provides for power purchase cost for one month. Therefore, rebate of 1% available for payment of power purchase bill within one month should be considered as non-tariff income and to that extent benefit of 1% rebate goes to reducing the ARR of the Appellant. The rebate earned on early payment of power purchase cost cannot be deducted from the power purchase cost and rebate earned only up to 1% alone can be treated as part of the non-tariff income. Therefore treating the rebate income for deduction from the power purchase cost is contrary to the MYT Regulations. As such this issue is answered in favour of the Appellant.

(iii) The third issue relates to the wrongful deduction of interest on surplus funds out of share-holders' money, etc. from the ARR of the Appellant and treating as a non-tariff income. Only interest income on surplus funds to the extent of delayed payment surcharge and interest on consumer security in excess of the rates specified by the Commission should be considered as non-tariff income for deduction in ARR. Also the interest income on consumer's share of incentive on over-achievement of AT&C losses need to be deducted from ARR. However, the Appellant has argued that he has factored the interest income while computing the carrying cost on the revenue gap. Consequently, the carrying cost is lower to that extent. When the benefit of the same has already been passed on to the consumer, the same cannot be passed on to them by way of interest cost. However, in order to correctly determine the

ARR as per the Tariff Regulations, the interest income on delayed payment surcharge and difference in interest rate on consumer security with respect to that specified by the Regulations may be considered as non-tariff income to be deducted from the ARR. Also interest on consumer's share of incentive on over-achievement of AT&C losses has to be deducted from ARR. The Commission will compute the interest income for which credit is to be given to consumer from total interest income. Accordingly, adjustment may be made in carrying cost on the revenue gap claimed by the Appellant to avoid double deduction of the interest income on this account in the ARR. On the remaining surplus fund on Retail Supply Tariff the benefit of interest income is to be retained by the Appellant on account of return on equity earned, overachievement in AT&C

losses and efficiency in controllable parameters, working capital, etc. invested in mutual funds/banks. The State Commission cannot erode the benefit to be derived by the distribution company by considering such interest income as a part of the non-tariff income. Accordingly, directed.

(iv) The next issue is relating to the inadequate lower rate of 9% for the allowance of the carrying cost. The carrying cost is allowed based on the financial principle that whenever the recovery of the cost is to be deferred, the financing of the gap in cash flow arranged by the distribution company from lenders and/or promoters and/or accrual and/or internal accrual has to be paid for by way of carrying cost. The carrying cost is a legitimate expense. Therefore the recovery of

such carrying cost is a legitimate expectation of the distribution company. The State Commission instead of applying the principle of PLR for the carrying cost has wrongly allowed the rate of 9% which is not the prevalent market lending rate. Admittedly, the prevalent market lending rate was higher than the rate fixed by the State Commission in the tariff order. Therefore, the State Commission is directed to reconsider the rate of carrying cost at the prevalent market rate keeping in view the prevailing Prime Lending Rate.

(v) **The next issue relates to the non-allowance of LC charges incurred on procurement of power under new PPAs. The LC is a document issued by the banks on behalf of the buyers to guarantee payment to the seller. The LC charges are dependent on the rate of charges fixed by the bank. The LC charges incurred by the Appellant**

are directly linked to the power purchase cost. These charges cannot be covered in A&G expenses which is controllable cost. However, LC is a pre-requisite for claming rebate of 2% while for 1% rebate which is available if payment is made within one month, LC is not required. As we have allowed the benefit of rebate over and above 1% to the Appellant, the LC charges should be borne by the Appellant as indicated by the State Commission.

59. In view of the above findings, we deem it fit to direct the State Commission to consider all these issues except the LC charges and give effect to those findings, as in our opinion the conclusions arrived at by the State Commission on these issues are not correct. Accordingly, the impugned order of the State Commission to the extent as indicated above is set aside. The State Commission, in the light of the findings rendered in this judgment is directed to implement the same as expeditiously as possible.

60. The Appeal is partly allowed. No cost.

(RAKESH NATH)
TECHNICAL MEMBER

(JUSTICE M. KARPAGA VINAYAGAM)
CHAIRMAN

REPORTABLE/NON-REPORTABLE

Dated: 30th July, 2010