Appellate Tribunal for Electricity
(Appellate Jurisdiction)

Appeal No.152 of 2010

Dated: 20th Oct, 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,

M/s. Dodson-Lindblom Hydro Power Private Limited,
6, Shiv Wastu, Tejpal Scheme Road No.5,
Vile Parle (E),
Mumbai

… Appellant(s)

Versus

1. Maharashtra Electricity Regulatory Commission,
World Trade Centre No.1, 13th Floor,
Cuffe parade, Colaba,
Mumbai-400 001

2. Maharashtra State Electricity Distribution Company Ltd.,
Prakashgad, Bandra (E),
Mumbai-400 051

.....Respondents

Counsel for Appellant(s): Mr.M G Ramachandran,
Ms. Ranjitha Ramachandran,
Mr. Anand K. Ganeshan,
Ms. Swapna Seshadri,
Ms. Sneha Venkataramani,

Counsel for Respondent(s): Mr. Buddy A Ranganadhan for R-1,
Mr. Hasan Murtuja for R-1
Mr. Raunak Jain for MSEDCL,
Mr. Varun Agarwal for MSEDCL,
Mr. Abhishek Mitra for MSEDCL,
Mr Lakshayveo R Odhekar for MSEDCL,
Mr. Samir Malik for MSEDCL

JUDGMENT

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

M/s. Dodson Lindsblom Hydro Power Private Limited, the Appellant, being a generator filed the Petition before the State Commission for re-determination of tariff. The State Commission after following the procedure passed the impugned order dated 24.5.2010 re-determining the tariff for the generation and sale of electricity by the Appellant. In the said order, the State Commission has not allowed certain claims of the Appellant. Hence, the Appellant has filed the present Appeal before this Tribunal challenging the said order dated 24.5.2010.

2. The short facts are as follows:

(a) M/s. Dodson Lindblom Hydro power Private Limited, the Appellant has been incorporated with the object of engaging in the business of generation and sale of electricity.

(b) Maharashtra State Electricity Distribution Company Limited (the Respondent 2) is one of the Distribution

Licensee for the State of Maharashtra engaged in the business of procurement of electricity and distribution and retail supply of electricity.

(c) In the year 1999, the Government of Maharashtra had established and commissioned the Bhandardara Hydro Electric Project Power House – II project in the State of Maharashtra.

(d) Since the Government of Maharashtra was not in a position to utilise the water resources effectively and operate the power plant at its full capacity, it decided to transfer the Bhandardara II station to private Sector. In pursuance of the said decision in December, 2003, the Government of Maharashtra invited bids from private entrepreneurs for operation of Bhandardara II station for a period of 30 years.

(e) Pursuant to the above, on 21.5.2004, the Appellant submitted its bid giving the price bid with the option of paying Rs.60 crore payable upon execution of the Agreement and further an aggregate amount of Rs.262.70 Crores to be paid over the lease period of 30 years.

(f) The Government of Maharashtra selected the Appellant as the successful bidder and issued the Letter of Award dated 31.12.2004.

(g) In pursuance of the award of the lease, the Appellant submitted its proposal to the erstwhile Maharashtra State Electricity board to supply electricity from the Bhandardara II at a mutually agreed rate and to enter into a Power Purchase Agreement.

(h) Thereafter, on 24.3.2005, the erstwhile Maharashtra State Electricity Board submitted a proposal to the State Commission for approval of the tariff from Bhandardara II. Accordingly, the State Commission vide the order dated 10.4.2006, determined the tariff for generation and supply of electricity from Bhandardara II. Thereupon, the Appellant and the second Respondent (Maharashtra State Electricity Distribution Company) entered into a Power Purchase Agreement dated 28.6.2006 for a period of 20 years.

(i) On 19.12.2006, the Appellant took over the Bhandardara II project from the Government of Maharashtra.

From then onwards, the Appellant undertook the operation of Bhandardara II project and supply of electricity to the Distribution Company in terms of the Power Purchase Agreement.

(j) On 28.5.2008, the Appellant filed a Petition in PetitionNo.27 of 2008 before the State Commission seeking determination of tariff for the Bhandardara II project.

(k) Then the State Commission directed the Appellant to submit a new tariff proposal based on the completed capital cost of the project. Accordingly, the Appellant filed an Amended Petition before the State Commission for approval of the completed capital cost and determination of tariff for the Bhandardara II project.

(l) During the course of proceedings, the State Commission directed the Appellant to furnish the entire data and file a petition in terms of the Regulations. Accordingly, the Appellant on 30.1.2009 filed a fresh petition before the State Commission in accordance with the Regulations.

(m) The State Commission ultimately, after holding public hearing and consulting expert consultants to provide a report on the tariff order dated 8.7.2009 decided the applicable tariff from Bhandardara II of the Appellant.

(n) Since some of the claims were disallowed, the Appellant filed an Appeal before this Tribunal in Appeal No.151 of 2009. This Tribunal by the judgement dated 23.12.2009, disposed of the said Appeal and remanded the matter to the State Commission for determination of tariff of the Bhandardara II generating station.

(o) Pursuant to this order, the Appellant field a Petition in Petition No.105 of 2009 seeking re-determination of the tariff. The State Commission, thereupon, held a public hearing inviting objections from the stake-holders and the consumer representatives.

(p) During the course of the proceedings, the State Commission directed the Appellant to provide details of certain documents and details of the pre-operative expenses incurred by the Appellant. Accordingly, the details were

furnished. Ultimately, on 24.5.2010, the State Commission has disposed of the Petition 105 of 2009 and re-determined the tariff of the Appellant's Bhandardara II Project, through its impugned order.

3. Even though the State Commission has allowed the claims in favour of the Appellant in pursuance of the remand order, the Appellant still felt aggrieved over the rejection of certain claims. Therefore, this Appeal has been filed.

4. The Appellant has challenged the impugned order dated 24.5.2010 passed by the State Commission on the following issues:

(a) Pre Operative expenses of Rs.4.11 crores incurred by the Appellant in its office in the United State of America and expenses of Rs.1.10 crores incurred by the Appellant in Indian office have been disallowed by the State Commission.

(b) Spare Runner of Rs.4.50 crores and SCADA system of Rs.2 crores proposed to be procured by the Appellant have

not been allowed to be included in the capital cost of the Appellant.

(c) Secondary energy charge has not been allowed by the State Commission over and above the design energy by the generating station.

5. The **First Issue** relates to the **pre-operative expenses**. The total pre operative expenses claimed by the Appellant were Rs.9.75 crores. The State Commission while passing the earlier order dated 8.7.2009, in the Petition No.27 of 2008 did not allow any part of the above pre operative expenses. As against the said order dated 8.7.2009, the Appeal was filed in Appeal No.151 of 2009 before this Tribunal which in turn partly allowed the Appeal filed by the Appellant and remanded the matter to the State Commission for re-determination of the tariff by the judgement dated 23.12.2009. Now in the present impugned order dated 24.5.2010, the State Commission has allowed the pre-operative expenses of Rs. 4.54 Crores only as against the claim of Rs.9.75 Crores.

6. According to the Appellant, the disallowance of Rs.5.21 crores of pre-operative expenses would cost serous prejudice to the Appellant as the same would not be serviced from the said tariff. The gist of the submissions made by the Appellant on this issue is as follows:

> *"The rejection of the claim to the tune of Rs.5.21 crores towards the pre-operative expenses was on the ground that the Appellant has not submitted the copies of the reports of the consultants and other agencies and other details sought by the Commission as such, the Commission was unable to carry out the complete prudence check . This finding is wrong. The State Commission has totally ignored the documents filed by the Appellant on 20.5.2010 in pursuance to the directions given by the State Commission. As a matter of fact, there is no reference to the letter dated 11.5.2010 and 20.5.2010 by the Appellant in the impugned order. In fact, no reference has been made by the State Commission to the documents filed on 20.5.2010 while the impugned order refers to other documents filed. The documents were filed on 20.5.2010 and the impugned order was passed on 24.5.2010. The State Commission in the impugned order dealt with the issue of not giving copies of the reports of the consultants and other agencies. It failed to deal with the documents by a letter dated 10.5.2010 and the documents furnished on 20.5.2010. The Appellant had given full details of such pre-operative expenses from the*

beginning. The Appellant filed the statement of the brake-up of the pre-operative expenses. This included the expenses incurred by the parent company of the Appellant in the United States of America. Similarly, Indian expenses also included the fees paid to various consultants. These expenses of the nature such as fees paid to the technical consultants including legal and financial consultants for various due diligence and documentation, expenses incurred in arranging loans from the foreign lenders, etc. All these are necessary expenses to be incurred for the project and for financial closure. In the case of determination of tariff on a cost plus basis such disallowance of substantial capital expenditure of Rs.5.21 cores is totally unwarranted and unjustified.

7. The Learned Counsel for the Respondent on this issue, has pointed out that the State Commission has given proper reasoning for allowing only one part of the expenses out of the total claim of Rs.9.75 Crores and therefore, there is no merit in this contention urged by the Counsel for the Appellant. The relevant question on this issue would arise for consideration is given below:

"Whether the State Commission is justified in not considering the pre-operative expenses of Rs.4.11 incurred by the Appellant in its foreign office and Rs.1.10 Crores in its Indian Office on the ground that the Appellant has not given the required details?

8. In this context it would be worthwhile to refer to the observations made by this Tribunal by earlier judgement dated 23.12.2009 in Appeal No.151 of 2009 on the issue of pre-operative expenses. The relevant portion of the judgement is as follows:

> *"It appears to us that the Commission did not sufficiently scrutinize the petition of the Appellant so far as it relates to claim for Rs.9.75 Crores and rejected the entire claim on the assumption that these expenses were pre-bidding expenses and, therefore, not permissible to be recovered through tariff. The Commission, therefore, further needs to revisit its decision in this regard.*
>
> *The Commission is fully entitled to carry out prudence check and disallow as much of the expenditure claimed as may be found to be imprudent. No part of the expenditure can be disallowed simply on the ground that it is more than the usual pre-operative expenditure. The Commission has to keep in view* ***the project specific requirements*** *and the peculiar situation in which the project was transferred including the fact that the project was running far below the design capacity and was a part of the irrigation project. This all that we have to say in respect of Appellant's claim for pre-operative expenses".*

9. By this judgement, this Tribunal directed the State Commission to conduct prudence check to allow only as much as the expenditure claimed as may be found to be prudent. In this context it is appropriate to refer to the relevant Regulations. Regulations of the MERC (Terms and Conditions of Tariff) Regulations 2005 read as under:

> ***"30.3****. The capital expenditure of the following nature actually incurred after the cut-off date may be allowed by the Commission for inclusion in the original cost of project,* ***subject to prudence check.***
>
> *(i) -------*
> *(ii) -------*
> *(iii) -------*
> *(iv) Any additional works/services which have become necessary for efficient and successful operation of the generating station, but not included in the original project cost".*

10. Both the Regulations and the judgement of the Tribunal would indicate that the State Commission was bound to conduct a detailed "prudence check' and prudence check is not limited to the verification of whether an expenditure has actually been incurred or not. The prudence check involves the following factors:

(a) Whether such expenditure has been incurred exclusively towards the project or not;

(b) Whether such expenditure is justifiable having regard to the industry norms for such expenses;

(c) Whether such expenditure is such that a prudent businessman would have incurred on his business at the stage at which it was incurred;

(d) Whether such expenditure was necessitated having regard to all the surrounding circumstances of the project;

(e) Whether such expenditure is aligned to the "project specific requirements";

(f) What is the efficacy of such expenditure and whether such expenditure has actually resulted in some benefit or likely benefit to the project;

(g) Whether such expenditure is such that it ought to be passed through to the consumers in a cost plus oligopoly situation".

11. The State Commission took into consideration the above factors while carrying out the prudence check of the pre-operative

expenses. According to the Appellant, the other documents furnished on 20.5.2010 in pursuance to the E mail dated 10.5.2010 have not been taken into consideration. E mail was sent on 10.5.2010 by the Commission intimating the Appellant to provide all the back-up information regarding pre-operative expenditure. The text of the E-mail is as follows:

> *"This has reference to the discussions at the hearing held at site on 9th April 10 and subsequent meeting at the Commission's office held on 19th April 10 when you were instructed to submit back-up information regarding pre-operative expenditure to the Commission for prudence check.*
>
> *It is observed that although the concerned bills and vouchers were submitted by you, the back-up information as required for the prudence check (**including** that regarding payment made to the foreign consultants) is still pending.*
>
> *Kindly ensure that the said information is submitted at the Commission's office latest by 14th May 2010".*

12. In response to the said E-mail dated 10.05.2010, the Appellant on 20.5.2010 submitted the copies of various documents. The State Commission in the impugned order has

actually referred to this E-mail and replies filed by the Appellant. The said reference by the State Commission is as follows:

> **"45**. *The expenses claimed by DHPPL under this head are mainly towards payment of Technical and Management fees, Financing and Legal fees, Administration expenses, Machinery, tools, equipment, and Furniture and fixtures. During the hearing held at site on April 9, 2010, the Commission directed the Petitioner to submit all the documents pertaining to these expenses, in order to enable the Commission to undertake the prudence check on the same. In compliance with the above direction, on April 19, 2010, the Petitioner submitted that available documents such as vouchers, bills and payment receipts for the expenses directly incurred by DLHPPL Indian office. The Petitioner was further directed on May 10, 2010 that to support the above details, it has to also submit the documents such as vouchers, bills and payment receipts for the expenses directly incurred by DLHPPL parent office in the USA,* ***copies of Orders placed on the technical and financial consultants, the Terms of Reference given to the consultants, copies of reports submitted by the Consultants,*** *relevant Government or RBI approvals for remittances or payments made in foreign currency, etc., to enable the Commission to conduct prudence check on these expenses. Merely because an expense is stated to have been incurred and is duly audited and the necessary back-up invoices are submitted, it does not mean that the expenses*

are prudent, and need to be passed on to the consumers. The prudence check involves the assessment of the efficacy of the expenditure incurred, and whether the desired objectives were achieved.

46. *As regards the details sought from the Petitioner such as copies of Orders placed on the technical and financial consultants, the Terms of Reference given to the consultants, copies of reports submitted by the consultants, etc.* ***DLHPPL has only provided some of the documents pertaining to the scope of Work/Terms of Reference,*** *however, the Petitioner* ***has not submitted the required copies of the Reports*** *of the Consultants and other Agencies. As the Petitioner has not submitted all the details sought by the Commission, the Commission has been unable to carry out the complete and meaningful prudence check of this expenditure, and, hence the Commission has not considered the expenses incurred towards fees for consultants and technical studies, as part of the Capital Cost.*

47. *Similarly, as regards the expenses incurred by USA Sponsor (Parent Company), the Petitioner has not submitted the complete details of the various expenses incurred by USA Sponsor (Parent Company). As the Petitioner has not submitted all the details sought by the Commission, the Commission has been unable to carry out the complete prudence check and hence, the Commission has not considered the reimbursement of the cost incurred by Parent Company in USA, as part of the Capital Cost.*

48. The Commission is of the view that the inability of the Petitioner to furnish the desired documents from his own records reflects on the managerial practices of the Petitioner, and not having sufficient controls and systems in place for making payments. The Petitioner also has a duty to ensure that only those expenses that are just and reasonable as well as essential are passed on to the consumers.

49. Apart from the expenses discussed above, the Commission has considered after verifying the documents and allowed all other expenses incurred by the Petitioner under this head, which includes administration expenses, bank commission for arranging Bank Guarantees, financing charges including upfront fees and commitment charges, stamp duty charges, notary charges and other miscellaneous expenses.

50. Thus, the Commission has considered the total pre-operative expenses of Rs.4.54 Crore as part of Capital Cost while re-determining the tariff as against the amount of Rs.9.75 Crore claimed by the Petitioner".

13. In the light of the above observations made by the State Commission, it can not be contended that the State Commission had not taken into account all the information and documents provided by the Appellant under cover of their letter dated

20.5.2010. According to the Appellant, the date of the letter dated 20.5.2010 has not been specifically mentioned in the impugned order. Prima facie the information and documents considered by the State Commission is specifically mentioned with regard to the information and documents provided by the Appellant under cover of their letter dated 20.5.2010. The State Commission has clearly held that the Appellant had provided some of the documents pertaining to scope of work/terms of reference. However, the Commission has further held that the Appellant has not submitted copies of the report of the Consultants and other agencies and as such the Commission has been unable to carryout the complete and meaningful prudence check of these expenditure. In the absence of the report of the Consultants, it can not be said that the Commission was bound to carryout the complete prudence check on the expenditure. In other words, in the absence of the reports actually submitted by the Consultants, no prudence check can be carried out either in terms of the Regulations or in terms of the earlier judgement by this Tribunal.

14. During the course of hearing before this Tribunal, the Appellant filed an additional affidavit dated 24.2.2011 to the effect that the copies of the reports of the Consultants were never asked.

The only ground urged by the Learned Counsel for the Appellant as raised in the Appeal is that the State Commission has totally ignored the documents filed by the Appellant on 20.5.2010 pursuant to the directions given by the State Commission on 10.5.2010.

15. Through the Additional Affidavit dated 24.2.2011, the Appellant has now tried to make out a completely new case which had never been pleaded before the Commission or raised in the Appeal or raised in the written submissions. Therefore, the plea raised in the Additional affidavit filed by the Appellant cannot be accepted. The Appellant being engaged in the business of generation of electricity cannot be allowed to contend that they are not aware of the documents which are required as a back-up document to undertake a prudence check. The specific observations have been made in the impugned order of the State Commission that in the absence of Consultant's reports, no meaningful prudence check can be carried out. This cannot be said to be wrong observation.

16. Therefore, we do not find any reason to hold that the conclusion arrived at on this issue by the State Commission would

suffer from any infirmity. Accordingly, we hold this issue as against the Appellant.

17. The **Second Issue** is relating to **non-inclusion of the cost of spare runner and SCADA in the capital cost of the project**. Submissions made by the Appellant on this issue are as follows:

> *"In the impugned order, the State Commission has not allowed the cost of SCADA (Rs.2.00 Crores) and Spare Runner (Rs.4.50 Crores) proposed to be procured and installed by the Appellant during the year 2010-11. The State Commission has not actually considered the relevant circumstances concerning the project. Unlike other hydro power plants, the runner presently used in the Appellants power plant had not been maintained properly. It had already undergone welding prior to the take over of the Project by the Appellant. The likelihood of the runner failing at any time during the operation of the plant is higher and the Appellant cannot be accused for such failure. If the Appellant had been maintaining the project from the beginning, having established the project or if the Appellant had taken over the project maintained by the Government of Maharashtra in a good condition it would be legitimately said that it is to be account of the Appellant, when major items such as Runner fails. But on the contrary the Appellant has taken over the Project which was badly maintained and admittedly required renovation and modernisation. Without the spare runner or when there is a failure of the existing runner, the Appellant will be prevented from operating the plant for his no fault. The manufacture of spare runner would take close to two years. Even if the runner is repaired or welded again, the plant would not be operational for nearly 40 days. The runner would cost Rs.4.5 Crores which is not a small amount*

that the Appellant can sponsor on its own without its inclusion in the Tariff. In addition to this, the State Commission has rejected the claim on the capital expenditure for SCADA system. The SCADA system is required for efficient control of the operation of the project on real time basis. The SCADA system enhances efficiency in the operation. Therefore, there is no justification for rejecting the claim of the Appellant on the capital expenditure for SCADA".

18. In reply to these submissions, it is contended by the Learned Counsel for the Respondent that the Commission has rejected this claim since the report of the Appellant's own consultant did not suggest that the runner requires immediate replacement or is likely to fail and even the Commission's Consultant Mr. Rao who was engaged to go into the Appellant's Consultant's report has also not opined about any impending failure of the Runner and therefore, the State Commission's findings regarding the cost of the spare runner and SCADA expenditure is justified.

19. In the light of the rival contentions of the parties, the following question on this 2nd issue would arise for consideration:

"Whether the State Commission is correct in not allowing the expenditure of SCADA and the cost of the spare runner proposed to be procured by the Appellant for the continuous and uninterrupted functioning of the generating station?

20. In the first order dated 8.7.2009 passed by the State Commission rejecting the claim of the Appellant for Runner and SCADA the State Commission would observe as follows:

> "*57. Shri Rao further opined that under the long-term works, DLHPPL has proposed to procure a spare runner at a cost of Rs.4.0 Crore on the basis of the inspection report. In this regard, the consultant has expressed some concern regarding the quality of repair work on the turbine runner and recommended further inspection after one year of service, which has perhaps, not been done. Further, the inspection report recommends that the runner replacement could be considered when Nilwande dam is raised to its final level. At that stage, as per the consultant "opportunity exists to alter the design to improve operation at the higher tail water levels as well as increase the output of the generating unit at future reduced heads". Shri Rao suggested that a spare runner is not warranted at this stage of the project. DLHPPL could approach the Commission at an appropriate future date with data on how much higher output could be realised with the proposed change of runner and the cost economics. The rehabilitation work of the draft tube gate hoist could also be considered at that time.*
>
> *58. Shri Rao further opined that the works proposed under "maintenance and rehabilitation and upgrades" are of routine nature and mostly form part of normal maintenance and not*

of capital nature. They also do not come under the category of "not included in the original project cost" as laid down in Regulation 30.3 of the MERC Tariff Regulations.

59. Considering the views of the technical expert, Shri VVRK Rao, the Commission has not considered any expenses towards the R&M Works. DLHPPL may, if necessary approach the Commission later for prior approval of additional capital expenditure with appropriate justification addressing the comments of technical expert and with proper cost benefit analysis. The Commission may consider the additional capital expenditure based on the prudence check of the same and approve the adjustment to the tariff approved in this order".

21. As against this order, this Tribunal in the judgement dated 23.12.2009 has held as under:

"15) We thus find that in respect of the R&M expenditures to be allowed to be passed through in tariff, the Commission needs to revisit its decision after allowing the Appellant an opportunity to explain its case vis-à-vis the report of Mr.VVRK Rao".

22. In pursuance of the directions given by this Tribunal, the State Commission examined the issue again and after due

analysis, the State Commission decided to disallow the cost of SCADA and Spare Runner proposed to be procured and installed by the Appellant during the year 2010-11. The relevant observations of the State Commission in the impugned order dated 24.5.2010 is as follows:

> *"58. After due analysis of the above information and submissions, the Commission observes that as a matter of routine maintenance management, there is no standardized protocol regarding keeping a spare runner. Spare runner are at times procured at large hydro plants having machines of similar design as a common spare to all of them and not one to one spare. However, it is also observed that such spare part, although treated as an insurance spare, remains unutilised for years together. The Commission, based on the representations made by GoMWRD and expert advice, notes that there are no apparent signs of impending failure of the runner in service at the plant of the Petitioner, and therefore, procurement of an expensive spare runner appears to be unwarranted. However, the Petitioner may provide at its own cost to protect its commercial interest.*
>
> *59. A perusal of summary of runner inspections done since taking over the project on December 19, 2006, indicates that DLHPPL has carried out 7 inspections. The summary of the inspections submitted to the Commission stipulates that the cracks developed on Blade Nos. 7, have already been*

repaired by welding by GOMWRD and since then the conditions of both the blades is as it is and there has been no further deterioration in the cracks as on January 22, 2010. As regards the hair crack developed on Blade No.14 and cavitations marks on Blade No.19, the situation from January 6, 2007 to January 22, 2010 has remained the same. However, the summary tabulation submitted by DLHPPL does not indicate the remedial action taken/repairs done by DLHPPL. DLHPPL has stated that as a result of the various actions taken by them after taking over the plant, the availability of the plant has improved to 99.98% and there had been no occasion when the water was let out without power generation. Moreover, it is to be noted that the Petitioner has also installed the online vibration monitoring system and hence, any indication of failure on account of the cracks in the blades would be identified by the vibration machines, as the impact of the cracks would be first indicated in terms of vibrations.

60. The Commission is of the view that forced outages of the plant may occur due to failure of the Runner, the Generator or any of the critical parts of the plant and these may cause extensive periods of non-availability of the plant. The Commission therefore, advises the Petitioner to put in place predictive and pre-emptive measures such as installation of diagnostic tools on the machine, following a strict regime of inspection of the runner and repairs to the same through expert technicians as required, instead of proposing to procure an expensive spare runner".

23. According to the Appellant, in the reports submitted by Mr. V.V.R.K Rao, on 27.5.2009, it is only stated that the spare runner is not warranted at this stage and therefore, this could not be relied upon by the State Commission to reject the said claim even though this Tribunal has directed the State Commission to give an opportunity to the Appellant to accept its case in the light of the report of Mr.V.V.R.K Rao.

24. In order to **deal with this issue** we can quote the relevant portion of the impugned order given in paragraph 52 to 57 which is as under:

> *"52. In order to comply with the direction stipulated by the Hon'ble APTEL as above, the Commission took the following steps:*
>
> *a) A copy of the report of Shri VVRK Rao was handed over to the Petitioner immediately after the Public Hearing on March 22, 2010;*
>
> *b) An opportunity was given to the Petitioner during the hearing held at site on April 9, 2010 to interact*

freely with Shri VVRK Rao regarding the issues under consideration;

c) The opinion of representatives of GOMWRD present during the hearing on April 9, 2010 at the site was also sought regarding the details of the accident in which the turbine runner was involved, the repairs carried out, and the condition of the item when the project was handed over;

d) The opinion of MSPGCL was also sought at the time of the hearing held at site regarding their practice of maintaining a spare turbine runner.

53. During the hearing at site on April 9, 2010 GoMWRD (Government of Maharashtra Water Resources Department) submitted that accidental damage had occurred on the said turbine and the damages were repaired in-situ. GoMWRD representative further submitted that the repairs work carried out in-site were satisfactory and after repairs, the machine had been performing quite well, and the turbine runner was in good condition at the time of handing over the Project to the Petitioner.

54. MSPGCL submitted the following on affidavit on May 4, 2010:

"It is submitted regarding critical spares, especially runners of turbines that, presently, there is

no practice of keeping a spare runner for small hydro power stations. Though checking of the runner is usually done during annual overhaul. So far the replacement of runner has not been done in any of small hydro power stations. However, minor repairs are carried out in-situ. Almost all small HPS are different in design aspect, and as a MSPGCL's policy no spare runner is kept for each individual small hydro power station.

Only one incident (viz at Dudhganga HPS), welding repair works for runner has been carried out. Since then, the unit is running normal. However, as per OEM's recommendations, order for one set of blades has been placed.

Regarding Koyna HPS, there are two spare runners each for Stage-I (4x70 MW) and Stage-II (4x80 MW) one spare runner for Stage IV (4x250 MW). There is no spare runner for Stage-III (4 x 80 MW) and KDPH (2 x 18 MW). Minor repairs are carried out in-situ whenever required".

55. The Petitioner submitted that expenses of capital nature, equipments/instruments that need replacement due to earlier damages and new equipments/instruments that are essential, have been covered under Renovation & Modernisation expenses. The Petitioner also submitted the list of the assets capitalised"

56. The Petitioner added that the scrutiny of each items will establish that these Renovation & Modernisation works were essentially required. At the time of operation of the plant by GOMWRD, many of the items were damaged, while some items were not provided at all, and almost all the equipments needed overhauling, as the maintenance of the plant for the last 13 years had been negligible.

57. The Petitioner further submitted that the procurement of the runner is essential at this stage, as the plant is being operated with damaged runner. The Petitioner added that the Draft Tube (DT) Gates were not commissioned by GOMWRD and the overhauling and commissioning was required to be done in FY 2008-09 as the Nilwande Dam level was increased to RL 623 M and back water pressure on turbine would have caused damage to it, in the absence of DT gates."

25. In these paragraphs, the State Commission has given the details of the steps taken in compliance with the directions given by this Tribunal. The above paragraph would indicate that sufficient opportunity was given to the Appellant by giving the copy of the report of Shr.V.V.R.K Rao to the Appellant and by giving the full hearing. During the hearing on the issue, the Appellant was allowed to freely interact with Shri V.V.R.K Rao

regarding the issue. As a matter of fact, the Government of Maharashtra, Water Resources Department (GOMWRD) submitted before the Commission that "***the repairs work carried out in-site were satisfactory and after repairs, the machine had been performing quite well, and the turbine runner was in good condition at the time of handing over the project to the Petitioner''.*** On the basis of the opinion given by the experts, the Commission observed that there are no apparent signs of impending failure of the runner in service of the plant of the Appellant and therefore, procurement of expensive spare runner is unwarranted. Under those circumstances, the Commission advised the Appellant to put in place predictive and pre-emptive measures such as installation of diagnostic tools on the machine, following a strict regime of inspection of the runner and repairs to the same through expert technicians as required. In this context, it would be proper to quote the relevant portion of the impugned order relating to this issue:

> *"64. Further, in its submission dated May 20, 2010, the Petitioner submitted that the actual expenses capitalised in FY 2009-10 amounts to Rs.12.58 Lakh. Further, the Petitioner also submitted the revised capital expenditure plan*

for FY 2010-11 and FY 2011-12 and mentioned that it will submit the proposal with justification to the Commission for prior approval of each item. As regards the proposed capitalisation for FY 2010-11 to FY 2011-12, the Commission has considered the revised estimated capitalisation as proposed by the Petitioner, except the capitalisation proposed for installation of Supervisory Control and Data Acquisition (SCADA) of Rs.2 Crore, and procurement of spare runner for Turbine (of Rs.4.5 Crores). Since, the capital expenditure approval is a separate process, the Commission directs the Petitioner to submit Detailed Project Reports with cost benefit analysis for obtaining 'in principle clearance' from the Commission for these works and upon approval of the same, the Petitioner may approach the Commission for suitable adjustment in the tariff approved in this Order. The summary of additional capital works proposed by the Petitioner and as considered by the Commission is given in the following Table……."

26. That apart, even prior to the Appellant having bid for the project, the Appellant had conducted a detailed inspection of the plant through its consultant Mr. Erskine L Flook, of M/s Samat

Resources. The said consultant was appointed in December, 2003. The inspection was carried out in January, 2004. The Appellant submitted its bid only thereafter in May, 2004. Hence, the Appellant was fully aware of the condition of the Runner even before submitting its bid for the plant. It is noticed even the consultant of the Appellant did not give any opinion about any impending failure of the Runner. The consultant has merely opined that the replacement of the Runner could be considered not for any impending failure but only in conjunction with modifying the design of the runner to improve the efficiency and output of the plant.

27. In this context, we would refer to the opinion given by Mr. Rao in his report who was appointed as a consultant by the Commission. The opinion of Mr. Rao is as under:

> *".....Under the long term works, it is proposed to procure a spare runner at a cost of Rs.4.0 Crore on the basis of the inspection report referred to above. The major point in the inspection report is in regard to the repair works being carried out on the turbine runner at the time of inspection. The consultant expressed some concern regarding the quality of repair work and recommended further inspection after one year of service. This has perhaps not been done.*

Further, the inspection report recommends that the runner replacement could be considered when Nilwande dam is raised to its final level. At that stage, as per the consultant "opportunity exists to alter the design to improve operation at the higher tail water levels as well as increase the output of the generating unit at future reduced heads". The turbine output reduces when the operating head on the turbine reduces and the possibility of increasing the output cannot therefore, prima-facie, be accepted. Further studies in consultation with manufacturers would be necessary.

A spare runner at this stage of the project is not warranted. DLH could approach the commission at an appropriate future date with data on how much higher output could be realised with the proposed change of runner and the cost economics. The rehabilitation work of the draft tube gate hoist could also be considered at that time".

28. In view of the above, the conclusion has been arrived at by the Commission that there was no necessity whatsoever to provide a spare runner particularly in the light of the factual finding that the condition of the runner and blades had not deteriorated ever since the Appellant had taken over the plant is on the proper reasoning. Therefore, the Commission correctly considered and held that it would not be prudent to include the cost of the spare runner in the capital costs of the project.

29. In respect of SCADA system, it is submitted that SCADA system is useful and the actual expenses capitalised in FY 2009-10 amounts to Rs.12.58 lakh. On this issue, the Commission directed the Appellant to submit project reports with cost benefit analysis for obtaining 'in principle clearance' from the Commission for these works and upon approval of the same, the Appellant was at liberty to approach the Commission for suitable adjustment in the tariff approved in this order. It is also to be noted that SCADA system which is useful for controlling all aspects of a plant from a remote location which enables the operator located at a remote locations to access and read all parameters of the plant has not yet been made mandatory in the State of Maharashtra. Therefore, it is perfectly, right on the part of the Commission to hold that it is not good to include the SCADA expenditure on the capital cost of the expenditure particularly when the Appellant has not provided any cost/benefit analysis of the same. Therefore, this point also does not hold merit.

30. The **Third Issue** relates to **Secondary Energy Charge** which was not allowed by the State Commission.

31. According to the Appellant, the State Commission, having accepted the Secondary energy charge to be provided on principle and having initiated the process for inclusion of secondary energy charges in the tariff regulations for the next period, has disallowed this claim in respect of the present year with a result, the Appellant has to supply free electricity over and over the design energy which is contrary to the observations by this Tribunal order dated 23.12.2009.

32. On the other hand, the Learned Counsel for the Commission in justification of the said disallowance contended that the State Commission has already initiated the process of framing the new Regulations for the next year as suggested but claim for the present year have been dealt by the Commission which is decided on the basis of the existing Regulations. In the rejoinder, the Appellant submitted that that State Commission has failed to invoke the power for removal of difficulties in the Regulations for allowing the secondary energy charge to the Appellant for present.

33. In view of the above, following question would arise:

"Whether the State Commission was justified in rejecting the prayer of the Appellant for removal of difficulties in the Regulations for allowing the secondary energy charge to the Appellant and differing consideration of the claim only for the future ? "

34. The Appellant has claimed the secondary charge in addition to primary charge specified under the Regulations. Under the present Regulations, the Annual fixed charges which a hydro Station is entitled to recover is based on the capital cost of the project plus the permitted return and the design energy of the project. The Annual fixed charges is so fixed that the hydro generator recovers the entire cost plus return from the sale of the design energy. Secondary energy is the energy generated by the Hydro Generator over and above the design energy. Hence, any charge for energy produced over and above the primary energy is called secondary energy charge and the rate for the same has to be specifically provided for in the Regulations. It is not disputed that the current tariff regulations of the Commission do not provide for a secondary energy charge. As such, there is no case made out for the relaxation for removal of difficulties.

35. In the earlier judgement of this Tribunal the same issue had been raised by the Appellant and this Tribunal has given a finding

on this issue. The relevant extract of the observations of this Tribunal is as follows:

"Secondary Energy Charge:

16) The Commission has not accepted the request of the Appellant for considering the incentive for secondary energy over and above the primary energy in accordance with the provisions of CERC Tariff Regulations 2004. It is contended by the Appellant that the concept of secondary energy charge is well recognised. If in a particular year the generation of electricity from water availability is more than design energy, the secondary energy charge is recoverable in addition to the annual fixed charge. It is explained by the Appellant that design energy is defined as quantum of energy which can be generated in 90% dependable year with 95% installed capacity of the generating station. In case the total generation is less than design energy because of inadequate water flow, annual fixed charge is sufficient to recover the cost. Annual fixed charge comprises of the energy charge and capacity charge. The Appellant contends that in case the Appellant is unable to recover the secondary energy charge there is no incentive whatsoever to operate the plant after generating equivalent to design energy which amounts to wasting of opportunity to produce more than the design energy even when the water flow permits such additional generation.

17. The Commission is aware of the CERC Regulations dealing with secondary energy. Yet, the Commission has declined to grant the secondary energy charge relying upon its own Regulations".

18……..

The plain reading of the Regulations leads one to the same conclusion to which the Commission has arrived at. ***The Appellant does not dispute this position.*** *However, the Appellant contends that the CERC Regulations need to be applied because: (i) the State Commission has to be guided by the CERC Regulations while framing its own regulations and (ii) the MERC Regulations need to be read down following the principle laid down by this Tribunal in Damodar Valley Corporation Vs. Central Electricity Regulatory Commission & Others 2007 ELR (APTEL)1677 (at page 1687-1688). In the DVC case (Supra) we ignored certain Regulations which were contrary to DVC Act although those provisions were not held to be ultra vires of the DVC Act. We are of the opinion that the principle of reading down does not apply to the present case as we are not invited to ignore any part of the Regulations as being ultra vires"……..*

The prayer of the Appellant in fact is to read more than what is available in the Regulations relied upon by the Commission. This not possible within the principle of reading down. So far as CERC Regulations are

concerned, they may have some guiding value but once the State Commission frames its own Regulations, the State Commission's Regulations and not the CERC Regulations can apply. Therefore, the Appellant cannot get what it wants for secondary energy generation by application of CERC Regulations or by reading down the MERC Regulations".

19. Although we uphold the Commission's decision to disregard secondary energy charge, we cannot but express our concern for encouraging energy generation on the one hand and rewarding efficiency on the other.

……..

The Central Commission has accordingly made provision for rewarding secondary energy generation. We are not able to appreciate the Commission's approach of ignoring the need to encourage generation of secondary energy by making adequate provision in its Regulations. We hope the Commission will take remedial measures in this regard and bring appropriate amendment in the Regulations".

36. From the above, following factors would emerge:

(a) There is no provision for the Secondary Energy Charge in the current Regulations of the Commission;

(b) The Regulations of the Central Commission are not binding on the State Commission;

(c) Even assuming that the Central Commission's Regulations were to be considered, the current Tariff Regulation of the Central Commission do not specifically provides the Secondary Energy Charge;

(d) It is further submitted that under Section 61 of the Act, the State Commission are only to be guided by the "principles and methodology" specified by the Central Commission and not by "Regulations" framed by the Central Commission.

It is therefore, submitted that there is no substance in the Appellant's claim for Secondary Energy Charge. Therefore, the contention urged by the Appellant on the issue also would fail.

37. **Summary of Our Findings**

(a) The first Issue relates to the pre-operative expenses. In view of the reasonings given in the earlier paragraphs, we hold that the State Commission is justified in not considering the pre-operative expenses of Rs.4.11 crores incurred by the Appellant in its foreign

office and Rs.1.10 crore in its Indian Office particularly when the Appellant did not give the required details before the Commission.

(ii) The Second Issue is relating to non-inclusion of the cost of spare runner and SCADA in the capital cost of the project. On this issue, the State Commission has given correct reasonings for not allowing the expenditure of SCADA and the cost of the spare runner proposed to be procured by the Appellant for the continuous and un-interrupted functioning of the generating station.

(iii) The third issue relates to the Secondary Energy Charge. In view of the discussions made above, we hold that the State Commission was justified in rejecting the prayer of the Appellant for removal of difficulties in the Regulation for allowing the Secondary Energy Charge to the Appellant and deferring consideration of the claim only for the future.

38. In view of our above findings, we do not find any merit in the Appeal and so, the Appeal is dismissed. However, there is no order as to cost.

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

Dated: 20th Oct, 2011
REPORTABLE/NON-REPORTABALE