# Before the Appellate Tribunal for Electricity
## Appellate Jurisdiction
## New Delhi

Appeal No. 33 of 2005 and Appeal No. 74of 2005

Dated: this 7th day of July, 2006

Present: **Hon'ble Mr. Justice E Padmanabhan, Judicial Member**
**Hon'ble Mr. H.L. Bajaj, Technical Member**

**Appeal No. 33 of 2005**

Haryana Vidyut Prasaran Nigam Ltd. …..Appellant

Versus

Haryana Electricity Regulatory Commission …..Respondent

For the Appellant : Mr. Pradeep Dahiya, Mr. Ajay Siwach
Mr. Rajiv Gupta, Advocates
Mr. M.K.Mittal,CS,NVPNL

For the Respondent : Mr. Sanjay Varma, Joint Director (HERC)
Mr.Rajesh Kumar Monga, Law Officer
Mr. Deepak Chopra, UHBVN

**Appeal No. 74 of 2005**

Haryana Vidyut Prasaran Nigam Ltd.(HVPNL) ……Appellant

Versus

Haryana Electricity Regulatory Commission ……Respondent

For the appellant : Mr. Pradeep Dhiya,Advocate
Mr. Rajiv Gupta, Advocate
Mr. Ajay Siwach
Mr. M. K. Mittal, CS,HVPNL

For the respondent : Mr. Sanjay Varma, Jt.Director,HERC
Mr. Rajesh Kumar Monga, Law Officer
Mr. Anil Kumar,AE/RA,UHBVNL,Pnchkula
Mr. Deepak Chopra,UHBVN
Mr.Vikas Gupta, Sr.AO

## Judgment

**Appeal No. 33 of 2005**

1. The present appeal is filed against the order dated March 7,2005 passed by Haryana Electricity Regulatory Commission (hereinafter referred to as HERC or the Commission) in Case No. HERC/PRO-15 of 2004 with respect to the Revised Annual Revenue Requirement (hereinafter referred to as 'Revised ARR) and Bulk Supply Tariff filed by Haryana Vidyut Prasaran Nigam Ltd. (hereinafter referred to as HVPNL) for its Transmission and Bulk Supply Business for financial year 2004-05.

2. The present appeal is also filed against the order dated June 6,2005 passed by the Commission in case No. HERC RA-2 of 2005 vide which the Commission has dismissed the Review Petition filed by the appellant seeking review of the order dated March 7,2005.

3. The appellant in this appeal has sought the following relief:

(i) allow the appeal;

(ii) quash and set-aside the order dated June 6,2005 passed by the Commission dismissing the Review Petition filed by the appellant seeking review of the order dated March 7,2005;

(iii) modify the order dated March 7,2005 by allowing the following:

(a) the appellant be allowed Rs. 37.94 millions actually incurred by the appellant during the year 2004-05 towards reactive energy charges

as against Rs. 66 millions claimed in the revised ARR and BST filing for FY 2004-05

(b) the appellant be allowed Rs. 1132.10 millions towards interest on account of over capitalization of interest made by the Commission on the capital works in progress. The interest capitalization should have been Rs. 204.58 millions as against Rs. 336.68 millions considered by the Commission;

(c) the appellant be allowed depreciation of Rs. 15.49 millions in addition to that has been allowed by the Commission;

(d) the appellant be allowed the depreciation/diminution in BBMB and IP Station assets/investments amounting to Rs. 107.04 millions as claimed in the revised ARR and BST filing for financial year 2004-05

(e) the appellant be allowed return on capital base @ 0.5% on the loans as claimed in the revised ARR and BST filing for Fy 2004-05;

(f) the appellant be allowed the Income Tax amounting to Rs. 13.17 million as claimed in the revised ARR and BST filing for FY 2004-05;

(g) the appellant be allowed 5.25% transmission losses (on actual basis) as against 4.62% approved by the Commission;

(h) the appellant be allowed the transmission and bulk supply tariff on the basis of the net aggregate revenue requirement worked out in the Review Petition

(iv) pass any other order(s) as this Hon'ble Tribunal may deem fit and proper in the facts and circumstances of the case and in the interest of justice.

**Appeal No. 74 of 2005.**

4. The present appeal is filed against the order dated May 10,2005 passed by Haryana Electricity Regulatory Commission in case No. HERC/PRO-19 of 2004 with

respect to the Annual Revenue Requirement and Bulk Supply Tariff filed by Haryana Vidyut Prasaran Nigam Ltd. for its Transmission and Bulk Supply Business for Financial Year 2005-06.

5. The appeal is also filed against the order dated July 6,2005 passed by the Commission in case No. 970/HERC/SV-rev 2005 vide which the Commission dismissed the Review Petition filed by the appellant seeking review of the order dated May 10,2005.

6. The appellant in its appeal No. 74 of 2005 has sought the following reliefs:-

(i) allow the appeal;

(ii) quash and set-aside the order dated July 6,2005 passed by the Commission dismissing the Review Petition filed by the appellant against the order dated May 10,2005;

(iii.) modify the order dated May 10,2005 by allowing the following:

(a) the appellant be allowed Rs. 792.73 millions (including guarantee fee of Rs. 23.91 millions) towards interest on the capital expenditure loans as against Rs. 725.64 million (including guarantee fee of Rs. 2.44 millions) allowed by the Commission

(b) the appellant be allowed Rs. 106.16 millions towards interest on account of over capitalization of interest made by the Commission on the capital works in progress. The interest capitalization should have been Rs. 164.60 millions as against Rs. 270.76 millions considered by the Commission

(c) the appellant be allowed depreciation of Rs. 20.59 millions in addition to that has been allowed by the Commission;

(d) the appellant be allowed depreciation/diminution in BBMB and IP Station assets/investments amounting to Rs. 107.04 millions as claimed in the ARR and BST filing for Financial Year 2005-06;

(e) the appellant be allowed return amounting to Rs. 178.99 millions @ 0.5% on the loans as claimed in the ARR and BST filing for FY 2005-06;

(f) the appellant be allowed the income tax amounting to Rs. 14.03 millions as claimed in the ARR and BST filing for FY 2005-06;

(g) the appellant be allowed 5.25% transmission losses as actual recorded during Financial Year 2004-05 as against 4.50% approved by the Commission;

(h) the appellant be allowed to exclude the amount of Rs. 474.90 millions towards cash discount as the same was excluded by the Commission in the ARR & BST for FY 2004-05;

(i) the appellant be allowed the transmission and Bulk Supply Tariff on the basis of the net aggregate revenue requirement on the basis of the above.

(iv.) pass any other order(s) as this Hon'ble Tribunal may deem fit and proper in the facts and circumstances in the case in the interest of justice.

7. We observe that the appellant, in both appeals No. 33 of 2005 and No. 74 of 2005, has raised identical issues against the tariff and review orders of the respondent Commission. In view of this we are of the opinion that it will be sufficient to delve deeper into details of one appeal only and decide on various issues which could be applied to in both appeals. We are taking up the Appeal No. 74 of 2005 for details.

8. **<u>Appeal No. 74 of 2005</u>**

The facts of the case leading to this appeal are given below :

(1) On December 31,2004, the appellant submitted ARR for Transmission and Bulk Supply Business for FY 2005-06. The ARR was accompanied with Bulk Supply and Transmission Tariff (hereinafter referred to as 'BST') application for its Transmission and Bulk Supply Business (hereinafter referred to as T&BS). The appellant projected an Annual Revenue Requirement of

Rs. 52,239.66 millions. This comprised of expenditure of Rs. 53,392.03 millions and a reasonable return of Rs. 178.99 millions from which non-tariff income amounting to Rs. 1331.37 millions was deducted to arrive at net ARR for the year 2005-06.

(2) That on March 22,2005 the Commission directed the appellant to file the required supplementary information within 15 days from the date of issue of the letter.

(3) That on April 7,2005 the appellant filed its reply along with supporting and additional data to the ARR (T&BS) and BST for the FY 2005-06.

(4) UHBVNL the distribution and retail supply licensee filed its comments and objections on the application filed by the appellant. DHBVNL a distribution and retail supply licensee and also one Shri Deepak Walia, President Forum for Common Cause, Panchkula desired to make oral submission during the public hearing. No objections were received from other public institutions, organizations and individuals.

(5) On April 18,2005 a public hearing was held by the Commission for considering the objection/comments to the ARR and related documents which were made available through public notices issued by HVPNL in the daily news papers informing the general public about the salient features of their filing/availability of the necessary documents and procedure for filing objections/comments. The public was informed about the availability of the ARR and related documents.

(6) The Commission while passing the orders dated May 10,2005 made certain modifications, which, according to the appellant, were not justified and were contrary to the guidelines issued by the Commission. The Commission made following modifications in its order dated May 10,2005 :

(A) Under Clause 3.1.1.1 regarding Volume of Power Purchase, table 3.9 Commission has allowed 21249 MUs against projections of 24413 MUs submitted by HVPNL for the year 2005-06, which is less by 3164 MUs.

(B) Under Clause 3.1.1.2, Commission vide table No. 3.11 has allowed Rs. 40109.43 millions towards power purchase cost against submission of appellant amounting to Rs. 48338.6 millions.

(C) Under Clause 3.1.2, Commission has approved transmission losses at 4.50% against 5.25% submitted by HVPNL.

(D) The net power available for sale to Distribution Companies was worked out as under:

| Description | HERC approval **(Units in MU)** | HVPNL proposal as per review petition **(Units in MU)** |
|---|---|---|
| Power Purchase Volume | 21249 | 24413 |
| Transmission Losses @ | 4.50% | 5.25% |
| Net power for sale to Distribution and Retail Supply Business | 20293 | 23131 |

(E) In the table 3.21 of said Order, the Commission has allowed interest (including guarantee fee of Rs. 2.44 millions) of Rs. 725.64 millions against HVPNL claim of Rs. 792.73 millions on loan for capital expenditure. The Commission deducted Rs. 270.76 millions towards interest capitalized from the allowed interest of Rs. 725.64 millions (including guarantee fee of Rs. 2.44 millions) and thus the net interest allowed on the capital expenditure loans was arrived at Rs. 454.88 millions.

(F) The approved depreciation rate for FY 2005-06 has been calculated on the basis of audited accounts for FY 2003-04 after adjusting it for generation assets i.e. land for the proposed Hissar Thermal Plant

and Yamunanagar Thermal plant and income earning assets at 6.1% against 6.726% worked out by the licensee.

(G) The appellant has projected Rs. 197.70 millions as A&G expenses for the purpose of the ARR under consideration. Besides expenses on Administration amounting to Rs. 90.38 millions, this includes Rs. 107.04 millions on account of diminution in the value of investments and Rs. 0.28 millions on account of prior period expenses and other debits.

(H) The Commission disallowed an amount of Rs. 178.99 millions on 0.5% on loans as part of ARR for FY 2005-06.

(I) Against projected income tax of Rs. 14.03 millions in the current ARR, the Commission disallowed this expenditure as no return on capital base is being allowed in the current ARR for FY 2005-06.

(J) The other incomes projected by HVPNL for FY 2005-06 were Rs. 1331.37 millions. This amount includes Rs. 474.90 millions towards cash discount likely to be available from power suppliers for prompt payment.

(7) The appellant filed review petition under Section 10(1) (h) of the Act read with Regulations 78,79,80,85 to 91 of the HERC (Conduct of Businesses) Regulations, 2004 on June 9,2005 seeking review and/or modification and/or clarification of the order dated May 10,2005 passed by the Commission with respect to the ARR and BST filing by HVPNL for its transmission and bulk supply business for FY 2005-06.

(8) The appellant sought review of the impugned order on the following grounds and submissions:

(a) While allowing volume from different projects it is observed that availability of power from the projects during the past

and variations in availability due to higher fuel cost, particularly volume of liquid fuel generation due to higher cost has considerably been deviated from the power projections. The inter-project volume-mix has in turn affected cost of power.

(b) The Commission approved rates for purchase of power from various sources for the year 2005-06 vide its orders dated May 10,2005 which were based on power purchase cost invoices received from various sources up-to February, 2005.

As the invoices of income tax, FERV and incentive etc. were received in March, 2005 bills or provisions have been made in the accounts of March, 2005, hence, the rates approved by HERC are based on rates of power purchase upto February, 2005 as also mentioned in the HERC orders.

(c) The Commission had allowed 4.62% transmission losses for FY 2004-05. The appellant had filed review petition with HERC for allowing 5.35% transmission losses for FY 2004-05. HERC in its tariff order dated May 10,2005 has allowed only 4.5% losses.

(d) In the ARR for FY 2005-06, the borrowings for capital expenditure proposed by the appellant were Rs. 2393.90 millions including loan of Rs. 1073.56 millions, which was yet to be sanctioned at the time of filing of ARR i.e. in December, 2004. Since then, 4 no. schemes against which loans amounting to Rs. 662.35 millions had been sanctioned and loan documents had been executed by the appellant. In the past also, the Commission had allowed interest on the schemes yet to be sanctioned, being

projections. Keeping in view of the above facts, the Commission should allow the interest of Rs. 45.62 millions on schemes yet to be sanctioned, as the sanction of loan is a continuous process.

As the Financial Institutions usually demand guarantee for the loan, which the appellant arranges from the State Government . The State Government (since August 1,2001) charges guarantee fee @ 2% on the amount of guarantee fee of Rs. 21.47 millions on the loans yet to be sanctioned being a bonafide business expenditure may be allowed by the Commission as has been done in the past.

(e) The Commission has applied the average rate of 6.1% depreciation on GFA as on April 1,2005 while computing the depreciation for Financial Year 2005-06. But the average rate of depreciation on the GFA as on April 1,2005 works out at 6.726%.

(f) The Commission has disallowed the diminution in the value of investments in BBMB and IP station assets amounting to Rs. 107.04 millions on the ground that the assets on which diminution in the value of investments are claimed by HVPNL are not part of its licensed business and hence this cost can not form part of the ARR of T&BS business.

As the appellant, the HVPNL has ownership interest in BBMB & IP station projects, amount of Rs. 107.04 millions represents depreciation relating to these projects. The generation assets of these projects need to be depreciated like any other generation project.

(g) The Commission has disallowed the Reasonable Return amounting to Rs. 178.99 millions claimed by the appellant on the ground that the Commission is allowing financial charges as part of interest cost. As the interest and reasonable return are two separate components of the ARR and these cannot be substituted with each other. While interest is allowed to meet the debt service obligations, the reasonable return is a part of the earnings of the owner.

(h) The other incomes projected by appellant for FY 2005-06 were Rs. 1331.37 millions which amount includes Rs. 474.90 millions towards cash discount likely to be available from power suppliers for prompt payment. HVPNL requires working capital loan over and above the normative working capital to enable it to make payments to power suppliers in time and thus avail the cash payment discount. Whereas the Commission has included cash payment discount in the other income, it has not allowed the interest payment on additional working capital requirement. The Commission in the previous order dated March 5,2005 had excluded cash discount from the other incomes on the basis of similar pleading made during the public hearing held on ARR for FY 2004-05. However, in the ARR order for FY 2005-06, the Commission has not included the above amount from the other income and at the same time has allowed interest on working capital loans on merely normative basis. This is contradictory to the own ruling of the Commission, which was given in its order dated March 7,2005, on the ARR and BST for FY 2004-05.

The Commission has allowed interest of Rs. 320.24 millions on Working Capital loans as against Rs. 1611.22 millions claimed by the appellant. The appellant has raised working capital borrowings from banks so as to make timely payments to power suppliers, which would result in availing of cash payment discounts. Either the Commission may kindly allow the interest on loans raised from the banks or exclude cash payment discount from other incomes.

(9) The Commission dismissed the review petition filed by the appellant on May 10,2005 by its order dated July 6,2005. The Commission rejected the issues raised by the appellant in its review petition relating to volume of power purchase, power purchase cost, transmission losses, interest on loans, depreciation, A&G expenses, return on capital base in view of order dated June 6,2005 in case No. HERC/RA-2 of 2005 filed by the appellant against the Commission's order dated March 7,2005, against which orders the appellant had already filed appeal No. 33 of 2005. The Commission held that no new and important matter has been raised, that was not known to the Commission while passing the order under review, that may merit reconsideration.

(10)The Commission further held that the lone new issue in the instant review petition seeks "exclusion of Rs. 474.90 millions towards cash discount from other incomes or allow interest on loans raised from the banks". While requesting this HVPNL's plea is that it has raised working capital borrowings from banks so as to make timely payment to power suppliers, which would result in availing cash discount. The Commission rejected the appellant's plea by merely saying that making timely payment for power purchased is a routine business activity and hence does not require any additional working capital (or borrowings) than already allowed.

9. The points that arise for our consideration in these appeals are:

(a) Whether the appellant is entitled to reactive energy charges as actually incurred by it?

(b) Whether the appellant is entitled to the interest element on account of alleged over capitalization also?

(c ) Is the appellant entitled to additional depreciation prayed for?

(d) Whether the appellant is entitled to depreciation in BBMB/IP station assets?

(e) Whether the appellant is entitled to receive reasonable return of 0.5% on the approved loan and Income Tax thereon?

(f) Whether the appellant is entitled to transmission losses on actual basis?

(g) Whether the tariff order passed by the Commission is liable to be Interfered or set aside?

(h) To what relief the appellant in each one of the appeals is entitled to?

10. **(a) Whether the appellant is entitled to reactive energy charges as actually incurred by it ?**

10.1 Appellant in its petition for Bulk Supply Tariff, had prayed for recovery of Reactive Power Charges as and when paid by it on account of bills raised by NREB/NRLDC as per provisions of para 1.8 of the Indian Electricity Grid Code (IEGC) in proportion to the individual MVARh drawl recorded by respective DISCOMS at respective interface points. Para 1.8 of IEGC is reproduced below for ready reference.

*“ 1.8 charges/payment for Reactive Energy Exchanges.”*

*The rate for charge/payment for reactive energy exchanges (according to scheme specified in sections 7.6.1 and 7.6.2), as approved by CERC*

*vide order dated October 30,1999 shall be 4 paise/kVArh upto March 31,2001 and shall be escalated at 0.05% per year thereafter, unless otherwise revised by the CERC “*

10.2. Learned counsel for the appellant pleaded that it had to incur the reactive energy charges because of non-installation/non-functioning of capacitor banks of the distribution companies namely UHBVNL and DHBVNL. Therefore the amount of reactive energy charges is legally recoverable from these companies and hence the appellant is entitled for allowing the payment of reactive energy charges demanded by and paid to NREB and SEBS.

10.3. Respondent Commission alleged that the appellants claim when submitted before the Commission was a wild guess without any rationale or documentary support specially on common pool credit received by it . Commission complained that appellant failed to submit a proper detailed proposal. Commission was of the view that the appellant should have submitted appropriate proposal along with supporting data as a part of their Bulk Supply Tariff proposal for charging or incentivising the distribution companies for their MVAr drawls or injection for consideration of the Commission. This should have included reactive drawls attributable to distribution companies and on appellant’s account. In view of the appellant’s failure to submit a proper detailed proposal as called for in Commission’s order dated January 13,2006, the Commission disallowed the expenditure. Commission further asserted that the fact that the appellant is a payer on a net basis rather than a receiver, proves that the appellant has not taken sufficient measures for reactive compensation. Commission took the stand that why the consumers should pay more tariff because of the inaction of the appellant firstly in not filing details and secondly for not taking adequate actions to control reactive drawls during low grid frequency.

Per contra the appellant fairly stated that the reactive energy drawls cannot be estimated as the power system behaves as per loading conditions and load generation balance in real time. Projections at best are made based on past experience and anticipated system conditions while submitting ARRs.

10.4 Appellant clarified that the reactive energy charge funds created by NREB by penalty paid on account of reactive energy drawls by certain constituents of NREB is intended to be used for payment of reward to other constituents who inject MVAr into the system at the same time. The appellant denied having ever mentioned that it receives certain sum back from NREB common pool.

10.5 Appellant informed that in addition to 150 MVAr capacitors installed, they are providing substantial quantity of capacitor banks in HVPNL system. As per general procedure being followed now capacitor banks in MVAr to the tune of 30% of MVAr capacity of transformers are being installed simultaneously at all load handling transformers.

10.6 Appellant rightly pointed out that, contrary to what the Commission has said the MVAr drawl is linked to voltage and not with frequency at a given point in time and voltage conditions also depend on power drawl behaviour of other constituents in the system. Learned counsel for the appellant pleaded that MVAr drawl by HVPNL is not fully consumed in its transmission system. A major part of it is further drawn by Distribution Companies from HVPNL so the charges paid by HVPNL should be shared by Distribution Companies in the proportion of MVAr drawn by each. Special Energy Meters (SEMs) have been provided at the interface points between HVPNL and Distribution Companies. Accordingly, the appellant had proposed to recover reactive energy charges as recorded by SEMs installed at interface points between HVPNL and Distribution Companies to share reactive energy charges paid by HVPNL to CTU/other constituents.

10.7 It has been rightly submitted by the appellant that reactive energy drawls cannot be estimated and predicted as the power system behaves as per loading, voltage conditions and load generation balance in real time and therefore, projections are made based on past experience alone. To call such estimates as 'wild guess' is not fair. We also note that the reactive energy charges are not paid back from the NREB pool. On its part HVPNL has already installed capacitor banks and is in the process of installing additional capacitors.

10.8 We also agree that the reactive energy charges have to be shared by the Distribution Companies. But it is not correct to apportion and share all the charges only between the Distribution Companies. HVPNL must also bear the charges to the extent it draws the reactive energy. With the SEMs already installed and knowing the total drawl as also drawl by respective Distribution Companies, HVPNL share can be worked out and it must pay for the reactive energy drawn by it. There is no justification to deny this claim merely because there is vast difference.

10.9 In view of the above, we are of the opinion that the Commission should have allowed the reactive energy charges claimed notwithstanding the fact that the initial amount sought by the appellant was different and was reduced. However, the appellant is directed to follow the instructions of the Commission and furnish necessary details in future. This point is answered in favour of the appellant.

11. **(b) Whether the appellant is entitled to the interest element on account of alleged over capitalization also?**

11.1 The appellant contends that the interest capitalization should have been Rs. 204.04 millions against Rs. 336.68 millions considered by the respondent Commission. In support of its contention, appellant has submitted copy of the Audited Annual Accounts for FY 2004-05 showing interest capitalization of Rs. 172.14 millions. Commission has cited the following reasons for the difference in the appellant's submission and its order in the amount of interest capitalized due to the following three issues:-

(i) The Commission disallowed interest on capital expenditure on "yet to be sanctioned scheme".

(ii) Higher interest cost capitalized.

(iii) Lower "other finance" charges allowed by the Commission.

11.2 The Commission further contends that it allows only those expenses to be recovered from the consumers for which supporting documents are made available to the Commission as on date of the order, in the instant case March 7,2005. The Commission allowed the investments for Capital Expenditure amounting to Rs. 255.3 crores for which source-wise borrowing details were produced by the appellant. The appellant has adopted the four year average figure which is varying between 32.78% to 48.15%. The Commission pleaded that, in the absence of the scientific methodology based on actual progress of the capital the recommendation it retained the Capitalization Schedule of 30: 60:10 as adopted in the previous years for transfer of assets from Capital Work In Progress (CWIP) to Gross Fixed Assets (GFA). The Commission disallowed borrowings on 'yet to be sanctioned schemes", hence the corresponding guarantee fee payable to Government of Haryana on the ground was automatically disallowed. The appellant has considered the following Assets

Capitalisation Schedule to determine the amount of Fixed Assets added to Gross Block from the CWIP.:

| Particulars | 2001 | 2002 | 2003 | 2004 | Average |
|---|---|---|---|---|---|
| Opening CWIP (excluding General) | 1272.31 | 1603.61 | 1708.80 | 2930.21 | 1878.73 |
| Additions | 1549.63 | 1411.31 | 2650.32 | 2059.99 | 1917.81 |
| Total | 2821.95 | 3014.92 | 4359.12 | 4990.20 | 3796.55 |
| Transfer to GFA | 1218.34 | 1306.11 | 1428.92 | 2452.85 | 1601.55 |
| Balance CWIP (excluding Generation) | 1603.61 | 1708.80 | 2930.21 | 2537.36 | 2194.99 |
| % Capitalistion (Transfer to GFA/Total CWIP) | 43.17% | 43.32% | 32.78% | 49.15% | 42.18% |

11.3 The appellant has further stated that based on the above Schedule and the interest rates assumed on the loans drawn, the interest during construction to be capitalized has been computed. The weighted average interest on the loans comes to 9.40% in FY 2005 and 8.97% in Fy 2006, which has been capitalized on the balance of CWIP.

11.4 After hearing the arguments of both sides and taking into account various submissions made by the appellant and the respondents we hold as under:-

(i) In any prospective planning exercise it is normal to include projects which are not sanctioned but are likely to be sanctioned and executed during the forthcoming year.

(ii) From the four year data given in the above table at para 11.2 regarding percentage capitalization though the variation is from 32.78% to 49.15%, it will only be appropriate to take the average value of the four years. This is exactly what the appellant has done.

In view of the above we do not agree with the Commission and would decide in favour of the appellant and answer the point in favour of appellant holding that interest should have been allowed as claimed by appellant.

12. **( c) Is the appellant entitled to additional depreciation prayed for?**

12.1 The appellant contended that average rate of depreciation allowed by the Commission is 6.59% of the GFA as on April 1,2004. While rejecting the review petition the respondent Commission held that depreciation has been allowed on the basis of accounts of FY 2003-04 and that the same has been allowed on the basis of Annual Accounts of FY 2003-04 where it works out to 6.726%.

12.2 The respondent Commission took the view that on the date of passing of the order dated March 7,2005 and the subsequent Review Order, the latest Audited Accounts made available to the Commission by the appellant was that of FY 2003-04. Accordingly, the Commission calculated the average rate of depreciation on the basis of FY 2003-04 Audited Accounts. The Learned Counsel for the respondent Commission further stated that on the basis of information available and reflected in Schedule V of the Audited Accounts, the Gross Fixed Assets (excluding land) was Rs. 7941.13 crores, the depreciation for the year as per the Audited Accounts was Rs. 523.46 crores, hence 523.46 divided by 7941.13X 100 = 6.59%. Therefore, the Commission adopted 6.59% as the applicable rate. As on date of passing of the order no further details along with supporting data were made available to the

Commission. Hence, it did not qualify the grounds for review as stipulated in the Commission's Conduct of Business Regulations 2004, thereby the Commission declined to consider the appellant's plea even at the review stage.

12.3 Per contra the appellant holds that in its review petition filed with the Commission it had submitted a detailed computation sheet on depreciation as Annexure-II to the review petition. Had the Commission examined this attachment of the review petition, the matter regarding depreciation claim of the appellant would have been decided appropriately at the review stage itself. Appellant further stated that actual depreciation for FY 2004-05 was Rs. 706.98 millions, it may be seen from the Audited Accounts of the appellant (Annexure 'A', Page 39, Profit and Loss Accounts). The depreciation allowed by the Commission was Rs. 675.11 millions which is lower by Rs. 31.87 millions than the actual amount of depreciation, which is Rs. 706.98 millions.

12.4 The only reason cited by the respondent Commission for not allowing the depreciation claimed by the appellant is non submission of documents even at the review stage. As the appellant had produced the relevant papers to the Commission at the review stage, we allow the depreciation as claimed by the appellant and the point is answered in favour of appellant.

13. **(d) Whether the appellant is entitled to depreciation in BBMB/IP station assets?**

13.1 The appellant contended that the respondent Commission disallowed the diminution in value of investments in BBMB and IP Station amounting to Rs. 107.04 millions on the ground that the asset on which the diminution in the value of investments are claimed by appellant are not part of its licensed business and hence this cost cannot form part of the ARR and the Transmission and Bulk Supply Business. The appellant pleaded that it has

ownership interest in BBMB and IP Stations, therefore, the generation assets of these projects need to be depreciated like any other generation projects. Learned Counsel for the appellant further pleaded that as per the Electricity Act, 2003, the business relating to generation of power is any way not a licensed activity and therefore the appellant does not need any separate generation license for these projects. The Commission is allowing all the expenses except depreciation incurred for generation of power relating to these projects therefore there is no rationale for disallowing depreciation of these projects. Appellant contended that depreciation is an integral part for generation cost of any power station. The Commission is allowing such cost to Haryana Power Generation Ltd. and in case BBMB/IP Stations were owned by HPVNL it would any way have allowed depreciation. The appellant contended that how the depreciation could be disallowed merely by change of ownership from one person to the other. Appellant pleaded that it has inherited these projects from erstwhile Haryana State Electricity Board and these have not been acquired at a later stage.

13.2 Per contra on behalf of respondent Commission it is contended that the appellant claimed diminution in the value of BBMB generation assets which is neither reflected in the cost, nor incurred by the appellant nor claimed by BBMB and is also not actually paid by the participating states. Thus there is no documentation/supporting data before the Commission to consider. The Commission further held that as far as having a replenishment fund at the time of redeeming of BBMB projects by way of depreciation reserve is concerned, is not tenable. In future the participating states may not even have the need for replacing BBMB stations thus there is no commitment even today, the capital cost from year to year is borne by Government of Haryana and not from revenue of the appellant. The appellant is only paying operational and maintenance expenses, which the Commission allows them to recover by way of per unit net rate for the BBMB power supply.

13.3 The Commission took the stand that while regulating public utility funds for capital projects are separately provided either by the Government by way of grant or equity contribution or by the Commission by allowing the required amount of borrowing and interest expenses on the same, depreciation amount is utilized for loan repayment/refurbishment, thereby reducing the burden of interest on the consumers. Thus, the depreciation for capital replacement does not exist in the cost plus regulatory regime.

13.4 Finally the BBMB projects were built with public fund and the Parliament, in its wisdom while enacting. The Punjab Reorganisation Act, 1966 had provided that in return for the power supply to the participating states they will be required to pay only the full cost of maintenance incurred by the BBMB. It is therefore, not the intention of the Parliament to charge any profit, return etc. over and above the maintenance and capital cost, on the power supply from BBMB. To allow any other charge as sought by the appellant would also be at variance of the provisions of The Punjab Reorganisation Act, 1966.

13.5 The appellant contended that it is incorrect for the Commission to hold that cost of BBMB and IP Stations assets have not been incurred by the appellant. This cost has been incurred by the appellant and as such these are appearing in its Balance Sheet. Appellant is also providing depreciation/ diminution on these assets on year to year basis in its accounts. The cost of generation of power of any station includes the depreciation components and therefore there is no rationale for non inclusion of the same in the cost of generation. Appellant pointed out that no generating station pays for depreciation to anyone else but the same is used for replenishment or refurbishment of the assets as and when the need arises. Appellant argued that had the project been built with the public funds, then the cost of these assets would not have appeared in its Balance Sheets. Appellant also stated that the Regulatory Commission of Punjab and Rajasthan have allowed the depreciation on BBMB

projects as part of the cost of generation of power of BBMB in the ARR and Tariff of PSEB and RRVPN.

13.6 After hearing both sides we are persuaded to hold that in view of the fact that generation does not require any license, value of BBMB/IP stations assets appear in the Balance Sheet of HVPNL and that replacement will be required after useful life of assets, the depreciation on BBMB/IP station assets deserves to be allowed as claimed by the appellant. Hence this point is answered in favour of the appellant.

14. **(e) Whether the appellant is entitled to receive reasonable return of 0.5% on the approved loan and Income Tax thereon?**

14.1 Appellant contended that the Commission has disallowed reasonable return amounting to Rs. 168 millions claimed by the appellant on the ground that the Commission is allowing financial charges as part of interest costs. The appellant fairly argued that interest and reasonable return are two separate components of the ARR and the same cannot be substituted with each other. While the interest is allowed to meet the debt services obligation, the reasonable return is a part of earnings of the owner. Moreover, the ARR guidelines issued by the Commission provides for a return @ 0.5% on the loans, hence the view of the Commission runs counter to its own guidelines. The appellant has not claimed any return on its equity capital or net worth because the above guidelines provide for return on computation of capital base besides a return on loans. Since the capital base of the appellant was negative it could not claim any return on the same. But the appellant has a net worth of Rs. 4811 millions and still it is unable to claim any return on the same because the ARR guidelines do not provide return on net worth/equity. It would be relevant to point out that the ARR guidelines issued by the Commission in the year 1998 were based on Schedule VI of the Electricity (Supply) Act, 1948. As this Act has been repealed with the

enactment of the Electricity Act, 2003, the Schedule VI is no more applicable as such the said guidelines on ARR are obsolete. As the Commission has not allowed reasonable return it has also not allowed Income Tax amounting to Rs. 13.17 millions. The appellant rightly contended that as its claim for reasonable return is legitimate, it should be allowed along with Income Tax element thereon.

14.2 Per contra on behalf of the respondent Commission it was argued that the guidelines of the Commission, with reference to Schedule VI of Electricity (Supply) Act, 1948, does provide for reasonable return on the amount of loan advanced by the State Government multiplied by ½ percent. The sub section (3) of Section 26 of Haryana Electricity Reforms Act 1997 states, " Where the Commission departs from factors specified in Schedule VI of the Electricity (Supply) Act, 1948 while determining the licensee's revenue and tariff it shall record the reasons therefore, in writing".

14.3 Respondent held that the aforesaid provisions of the repealed Act were more relevant for integrated State Electricity Boards to enable them to earn the stipulated 3% return and the fact that Government assistance to the SEBs came more in the form of Loans and Grants and not for unbundled and corporatised utilities like the appellant, whose license conditions provides for a return on equity/networth i.e. positive elements of the capital base. It was argued on behalf of the respondent Commission that accordingly, it allows interest on borrowings for capital expenditure, interest on borrowings for the allowable level of working capital, and over and above this also allows other financial charges including 2% guarantee fee charged by the Government for capital expenditure related borrowings of the appellant. Having allowed all borrowings related expenditure the Commission did not find it justifiable and fair in the interest of the consumers to burden them with a return on loan as claimed by the appellant. Accordingly the Commission had disallowed the same with the observations " As the Commission is allowing financial charges

as part of interest cost, the Commission disallows this amount as part of ARR for FY 2004-05."

14.4 We find and recognize that the appellant has not been allowed any return or profit although it has a networth of Rs. 4811 millions. In all fairness, entity in business operation should be allowed some kind of minimum return. The Commission has so far not revised or modified provisions of Schedule VI of the Electricity (Supply) Act, 1948. We are convinced that the reasons given by the respondent Commission for not allowing a reasonable return of 0.5% as per its own guidelines are not valid in law to justify its action. We decide in favour of the appellant. The Income Tax payable on the amount of reasonable return of 0.5% on the approved loans is also allowed as the Income Tax on profits is a legitimate business expenditure for the purpose of ARR and Tariff.

15. **(f) Whether the appellant is entitled to transmission losses on actual basis?**

15.1 The appellant's contention is that the Commission has allowed 4.62% transmission losses during 2004-05 against the actual losses of 5.27% upto February, 2005. Interstate and intrastate losses upto February, 2005 are 2.08% and 3.26% respectively. Appellant pleaded that the Commission itself had acknowledged that the appellant has a very little control over interstate losses. Accordingly, the interstate losses on actual basis should have been allowed. Appellant also contended that during FY 2004-05, energy handled by it is 19310.59 MUs (upto February 2005) which is much more than 18458.75 MUs (upto February, 2005) handled by it in FY 2003-04. Accordingly, Intra state losses have also increased marginally to 3.26% during FY 2004-05 (upto February, 2005) as against 3.15% during the FY 2003-04.

15.2 Per contra the respondent Commission pointed out that despite massive investments allowed by the Commission for strengthening the transmission system, appellant has been projecting transmission losses at higher level as given in the following table;-

| **Year** | **Actual** | **Applicant's proposed. (HVPNL)** | **HERC Allowed** |
|---|---|---|---|
| FY 2002-03 | 5.72% | 7.85% | 6.66% |
| FY 2003-04 | 4.62% | 6.00% | 4.50% |
| FY 2004-05 | 5.25% | 5.35% | 4.62% |
| FY 2005-06 (Upto June,2005) | 4.40% | 5.25% | 4.50% |

15.3 The respondent alleged that appellant cannot shirk the responsibility for the inter state transmission losses by saying that it has no control as it is drawing 3800 MW of power from Northern grid. The fact that the appellant is paying heavily to NREB for reactive drawal is sufficient reason to drive home the fact that the appellant has not taken sufficient measures for reactive compensation. The respondent Commission set out the following table regarding transmission losses and volume of energy handled:-

| | Energy Handled (MU) | Year on Year Increase (MU) | Inter-state Transmission Losses (%) | % increase/ decrease | Intra-State Transmission Losses(%) | % Increase/ decrease |
|---|---|---|---|---|---|---|
| FY 2002-03 | 19208 | - | 1.69% | - | 4.11 | - |
| FY 2003-04 | 20499 | 1291 | 1.51% | **-0.18** | 3.28 | **-0.83** |
| Fy 2004-05 | 21389 | 890 | 2.05% | **0.54** | 3.25 | **-0.03** |

15.4 From the above table despite increase in the volume of energy handled by the appellant in FY 2003-04 both the inter and intra State Transmission Losses witnessed decline, this trend continued in FY 2004-05 in the Intra-State Transmission Losses. The Inter state pooled transmission losses as per RLDC declined from 4.01% in FY 2002-03 to 3.55% in FY 2004-05. As against this the Regional declining trend in the case of the appellant the inter state transmission losses increased from 1.69% in FY 2002-03 to 2.05% in FY 04-05. Respondent pointed out that despite huge investments made in improvement of transmission system the appellant had not controlled the inter state transmission losses. Accordingly, for FY 2004-05, the Commission pegged the transmission losses at 4.62% i.e. at the level actually achieved during FY 2003-04. In view of the investments made, the Commission reduced it further to 4.5% in FY 2005-06.

15.5 Per contra the appellant held out that despite tremendous increase in quantum of power handled losses have not increased proportionally and this could be achieved with the help of investments made. These losses have not only been kept at minimum level but actually brought down. It is a technical fact that current is proportional to power handled but losses are proportional to the square of the current passing through any system. During FY 2003-04 and FY 2005 the increase in power handled has been in the order of 1.0864, 1.0713 and 1.0379 times over the previous years. Accordingly, the rise in losses during corresponding consecutive years was expected as 1.1803, 1.1477 and 1.0772 times, but the actual increase in losses within the Haryana as judged by the recorded figures as 0.729, 0.8077 and 1.1364 times respectively. This clearly establishes that Haryana system has been strengthened/ improved resulting in decreasing technical losses. The appellant rightly contended that it has no control over interstate transmission losses. Due to resource constraints and availability problems from the nearest generation points it has to resort to purchase power from distance places which, at times involves one or more Regions for transporting the procured

power to the point of use. These transmission losses of the respective regions have to be borne by the appellant over which it has no control. In particular case for 2004-05 the inter state losses recorded were high due to the fact that there was failure of monsoon in region. The hydro generation at BBMB was very badly affected and it had to purchase deficient power from NTPC, atomic power stations through bilateral arrangement from outside the northern region. As such, higher transmission losses were booked to HVPNL, it was necessary for the appellant to procure power even from far away places to meet the local demand of power.

15.6 As far as the intra state transmission losses are concerned there has been only a marginal increase in intra state losses from 3.15% in FY 2003-04 to 3.27% in FY 2004-05 which is expected by the increase in energy handled.

15.7 We do observe that during FY 2005 the intra state losses have increased 1.1364 times against expected level of 1.0772 times which is not a good trend.

15.8 After hearing both sides and taking into account the various facts brought to our notice we note that the intra state transmission losses are concerned these have been more or less well under control. As far as inter state transmission losses are concerned we are of the view that the appellant has hardly any control over these losses and, therefore, these losses should be allowed on actuals. We, therefore, answer this point in favour of the appellant and hold that the appellant is entitled to consequential reliefs.

16. **(f) Exclusion of cash discount from other income.**

16.1 The appellant argued that it had raised working capital borrowings from banks so as to make timely payment to power suppliers, which results in availing cash discounts. The respondent Commission rejected the appellant's plea by merely saying that making timely payment of power purchase is a routine

business activity and hence does not require any additional working capital (or borrowing) than already allowed. The appellant submitted that other income projected by it for FY 2005-06 were Rs. 1331.37 millions which included Rs. 474.90 millions towards cash discounts likely to be availed from power suppliers for prompt payments. During the public hearing the appellant had pleaded that this amount should not be included in the other incomes if the Commission would allow interest on working capital on normative basis as appellant cannot avail this discount without short term borrowings. The Commission in its order dated March 7,2005 had excluded cash discount from other incomes on the basis of similar pleadings made during public hearing held on ARR for FY 2004-05. However, in the ARR order for FY 2005-06, the Commission has not excluded the above amount from other income and at the same time has allowed interest on working capital loans on normative basis. It is contrary to the respondent Commission's own ruling, which was given in its order dated March 7,2005 on the ARR and BST for FY 2004-05. The appellant argued that the level of borrowing i.e. equivalent to one month ARR is not sufficient to cover the funding, reasonable amount for sale of power. The Commission did not allow any working capital toward cost of stores and spare parts, O&M expenses and cash and bank balances. Appellant further argued that as per CERC norms, the receivables are allowed for two months. Thus the working capital borrowings allowed by the Commission are not even 50% of the desired level as well as of the norms fixed by the CERC. Appellant submitted that based on the above, the discount for prompt payment should be excluded from its other income so that the same could be utilized for meeting the interest of additional borrowing for working capital being made by appellant from the banks for making timely payments of the CPSUs which will also be in line with the orders passed by the respondent Commission for FY 2004-05.

16.2 After hearing both sides and keeping in view the fact that whereas as per CERC norms the receivables are allowed for two months and the HERC has

allowed for only one month. we would decide this point also in favour of the appellant and the appellant is entitled to consequential relief.

**17. (g) Whether the tariff order passed by the Commission is liable to be interfered or set aside?**

17.1 The points being common and identical in both appeals and therefore what we hold in one appeal equally apply to the other appeal, as it is identical in all respects.

17.2 In the end we conclude that as far as point (a) is concerned we allow this in favour of the appellant to the extent stated above.

17.3 Regarding points (b) to (f) we decide in favour of the appellant and the appellant shall have the consequential relief

18 In the result both appeals are allowed in the above terms.

19 Parties will bear their respective costs.

Pronounced in the open Court on July 7, 2006.

| (H.L. Bajaj) | (Justice E.Padmanabhan) |
| --- | --- |
| Technical Member | Judicial Member |