BEFORE THE APPELLATE TRIBUNAL FOR ELECTRCITY
(APPELLATE JURISDICTION)

APPEAL NO. 61 OF 2010

Dated : 9th May, 2011

Coram; Hon'ble Mr. Rakesh Nath, Technical Member
Hon'ble Mr. Justice P.S. Datta, Judicial member

In the matter:

Torrent Power Limited,
Torrrent House,
Ashram Road,
AHMEDABAD- 380 009. …Appellant (s)

Versus

Gujarat Electricity Distribution Company Ltd.
1st floor, Neptune Tower, Opp. Nehru Bridge,
Ashram Road,
Ahmdabad-380009. Respondent(s)

Counsel for the Appellant : Ms. Deepa Chawan
Mr.Hardik Luthra
Mr.Chetan Bundela
Mr. Samir Shah
Mr. Alok Shukla
Mr. H.S. Jaggi

Counsel for the Respondent: Mr. Sanjay Sen
Ms. Shikha Ohri
Ms. Surbhi Sharma
Mr. S.R. Pandey & Mr. Sunil Sharma
Mr. Achintya Dwivedi &
Mr.Dharmendra Bemal

JUDGMENT

HON'BLE MR. JUSTICE P.S. DATTA, JUDICIAL MEMBER

1. This appeal by the Torrent Power Ltd. which is a company under the Companies Act, 1956 engaged in the business of generation and distribution of electricity in the state of Gujarat is against the order dated 9th December, 2009 passed by the Gujarat Electricity Regulatory Commission, the respondent herein, which by the said order decided and disposed of the petition filed by the appellant for Annual Performance Review (APR) for the financial year 2008-09 and determination of tariff for the FY 2009-2010, for the business of generation and distribution under the MYT control period of the financial year 2008-09 to FY 2010-11. It is placed on record that the Commission on17th January, 2009 in case No. 939 of 2008 determined Annual Revenue Requirement, wheeling charges and Retail Supply

Tariff for the control period FY 2008-09 to FY 2010-2011. The said order dated 17th January, 2009 was challenged before this Tribunal in appeal No. 68 of 2009 which has since been disposed of on 23rd March, 2010 and the Tribunal's decisions on certain points reached therein will be taken cognizance of while deciding the issues covered under this appeal.

2. It is contended that the impugned order dated 9th December, 2009 is erroneous and contrary to the law as also the materials on record in so far as it relates to rejection of the appellant's claim to the following expenses for the Annual Performance Review (APR)/tariff determination period:

(A) Sharing of gains on account of controllable factors contrary to the Regulations.

(B) Erroneous treatment to interest on working capital.

(C) Erroneous revision of Distribution Loss Trajectory

(D) Misconstruing of the statutory Regulations resulting in non-consideration of actual PAF and PLF for the generating stations.

(E) Misconstruing of the statutory Regulations resulting in denial of eligible incentive on Plant Load Factor (PLF) for F.Y. 2008-2009.

(F) Non-consideration of TPL-D (Ahmedabad) receivables by deducting TPL-Generation ARR in calculation of Working Capital requirement contrary to the Regulations.

(G) Erroneous treatment in respect of applicability of the Tax Rate for TPL-G towards Income Tax.

(H) Disallowance of Income Tax to earn Return on Equity (RoE) as post tax.

(I) Classification of cost items as controllable and uncontrollable contrary to the Regulations.

(J) Error in computing the Wheeling Charges.

(K) Discriminatory treatment to Renewable Purchase Obligation (RPO)

3. By way of elaboration it is pleaded that Regulation 11 of the Gujarat Electricity Regulatory Commission (MYT Framework) Regulations, 2007 (for short, the Regulation, 2007) reads as under:

"11: Mechanism for sharing of gains and losses on account of controllable factors

11.1 The approved aggregate gain to the Generating Company or Licensee on account of controllable factors shall be dealt with in the following manner:

(a) One-third of the amount of such gain shall be passed on as a rebate in tariffs over such period as may be specified in the

Order of the Commission under Regulations 9.7;

(b) One-third of the amount of such gain shall be retained in a special reserve by the Generating Company or Licensee for the purpose of absorbing the impact of any future losses on account of controllable factors under clause (b) of Regulation 11.2' and

(c) The balance amount of gain may be utilized at the discretion of the Generating Company or Licensee.

11.2 The approved aggregate loss to the Generating Company or Licensee on account of controllable factors shall be dealt with in the following manner:

(a) One-third of the amount of such loss may be passed on as an additional charge in tariffs over such period as may be specified in the Order of the Commission under Regulation 9.7; and

(b) The balance amount of loss shall be absorbed by the Generating Company or Licensee.

4. It is the case of the appellant that by the impugned order the Commission has disregarded the sharing of gains and losses as envisaged in Regulation 11 of the GERC MYT Framework Regulations, 2007 and contrary thereto it held that 1/3 of the amount as contemplated in Clause (b) of paragraph 11.1 shall be additionally passed on in the form of rebate on tariff. It is contended that the word "shall" as it occurs in Regulations 11.1(b) demands mandatory compliance and it does not allow variation therefrom,

but the Commission having overlooked the provision of the Regulations which is mandatory in nature passed the order impugned thereby subjecting the appellant to an adverse financial impact. It is contended that Maharashtra State Electricity Regulatory Commission (Terms and Conditions of Tariff) Regulations, 2005 has similar provision for the sharing of gains and losses on account of controllable factors and the State Commission of that State has treated the gains on account of controllable factors in line with their Regulations.

5. With respect to the alleged erroneous treatment to interest on working capital the Commission has compared the interest on working capital as per norms with that incurred through external funding and difference has been termed as efficiency gain. Thus, the interest on working capital funded through internal accruals has been considered as efficiency

gain and passed on to the consumers. The Commission completely disregarded Regulation 20(1)(v) of the GERC (Terms and Conditions of Tariff) Regulations, 2005(for short, the Regulations, 2005) and has not calculated the interest on working capital for the generation business on the basis of the actual cost. According to the appellant, the working capital requirement is assessed on day to day basis as per prevalent business conditions and an utility like the appellant may decide to meet its working capital requirement in infusing its own funds from time to time. So far as the generation business is concerned the working capital requirement in terms of the GERC (Terms & Conditions of Tariff) Regulations, 2005 is on four items namely (a) cost of fuel for two months in the case of coal and one month in the case of gas, (b) O &M cost for one month, (c) maintenance spares at 1% of the gross fixed assets and (d) receivables on sale for two months. In respect of distribution business the first item as in the case of generation business is not required, but the other three items are equally applicable to the distribution business. Based on this, the working capital requirement has been computed at base price by the Commission in accordance with the Regulations. Now, according to the appellant, the working capital requirement varies due to the variation in the cost of fuel, power purchase, O & M cost and receivables. Therefore, the Commission should have recomputed the working capital requirement as per the formula as per actual cost as part of the annual performance review exercise and the variation in the working capital requirement with that approved in the MYT should have been segregated between the uncontrollable and controllable factors. Therefore, based on such segregation the Commission should have shared the gains and losses pertaining to the controllable factors, while variation on account of uncontrollable factors should have been entirely passed on to the consumers. Variation in the working capital requirement has been uncontrollable because of the factors like fuel cost, power purchase cost and increase in receivables. Thus, the interest on working capital arrived at by applying interest rate is uncontrollable and to be allowed to be recovered as per regulation 20(i)(v)(b) of the GERC (Terms and Conditions of Tariff) Regulations 2005 which reads as thus:

> *"(b) Rate of interest on working capital shall be on normative basis and shall be equal to the short – term Prime Lending Rate of SBI as on 01.04.2004 or on 1st April of the year in which the generation station or a unit thereof is declared under commercial operation, whichever is later. The interest or working*

capital shall be payable on normative basis notwithstanding that the generating company has not taken working capital loan from any outside agency"

The appellant referred to in this connection this Tribunal's decision in Reliance Infrastructure Vs. MERC and Ors. in Appeal No. 111 of 2008 wherein it was held as follows:

"Treatment of interest on internal sources:

(5) The Appellant has employed internal sources to meet the demand for working capital. The Commission has not denied the interest on the working capital employed from internal sources. The Commission has treated such interest as efficiency gain to that one-third of such gain could be shared with the Distribution Company/ consumers. …………………………………………… ………………………………………………………… …..

(6) It is submitted on behalf of the Appellant that when working capital is funded though internal sources of the Appellant, the internal funds also carry cost. It is further submitted that such funds employed elsewhere would have carried interest income.

(7) The Commission observed that in actual fact no amount has been paid towards interest. Therefore, the entire interest on working capital granted as pass through in tariff has been treated as efficiency gain. It is true that internal funds also deserves interest in as much as the internal funds when employed as working capital loses the interest it could have earned by investment elsewhere. Further the licensee can never have any funds which has no cost.

(8) The internal accruals are not like some reserve which does not carry any cost. Internal accruals could have been inter corporate deposits, as suggested on behalf of the Appellant. In that case the same would also carry the cost of interest. When the Commission observed that the REL had

actually not incurred any expenditure towards interest on working capital it should have also considered if the internal accruals had to bear some costs themselves. The Commission could have looked into the source of such internal accruals and the cost of generating such accruals. The cost of such accruals funds could be less or more than the normative interest. In arriving at whether there was a gain or loss the Commission was required to take the total picture into consideration which the Commission has not done. It cannot be said that simply because internal accruals were used and there was no outflow of funds by way of interest on working capital and hence the entire interest on working capital was gain which could be shared as per Regulation no. 19. Accordingly, the claim of the Appellant that it has wrongly been made to share the interest on working capital as per Regulation 19 has merit.

6. With particular reference to the independence of an utility to take prudent business decision relating to utilization of internal fund for its working capital requirements it is pleaded that it would be appropriate to peruse the decision of this Tribunal which held that the commercial plans of utility and the internal, commercial management, and domain of utility cannot be interfered with. (Karnataka Power Transmission Corporation Ltd. Versus Karnataka Electricity Regulatory Commission, Bangalore, Appeal No. 84 of 2006 dt. 29th August, 2006")

7. With regard to the distribution loss trajectory the Commission as per MYT Regulations has specified trajectory for distribution loss in the order dated 17.01.2009. It is submitted that MYT framework has been evolved to bring in efficiency through better performance with benefits to all the stakeholders. The actions of the licensee / utility like the appellant are driven by the principle of

rewarding the efficiency enunciated in the MYT framework order. Regulations 8.1 provides that the Commission may stipulate a trajectory which may cover one or more control period for certain variables. The Commission stipulated a distribution trajectory in the entire MYT control period. The distribution loss for the financial year 2009-10 was 10.25% for TPL-D (Ahmedabad) and 6.00% for TPL-D (Surat) as per specified trajectory. Regulation 4.2(e) of the MYT Regulations reads as follows:

> "*4.2 The multi-year tariff framework shall be based on the following elements, for calculation of aggregate revenue requirement and expected revenue from tariff and charges:*
>
> > *(e) Trajectory of specific variables as may be stipulated by the Commission, where the performance of the applicant is sought to be improved through incentives and disincentives.*"

The National Tariff Policy provides as follows:

> *"Suitable performance norms of operations together with incentives and dis-incentives would need to be evolved alongwith appropriate arrangement for sharing the gains of efficient operations with the consumers …. The norms should be efficient, relatable to past performance, capable of achievement and progressively reflecting increased efficiencies"*

It is contended that the Commission by the order impugned has revised the distribution loss trajectory for FY 2009-2010 on the basis of the actual loss level achieved in the financial year 2008-09. The Commission observed that the appellant had achieved lower level of distribution loss at 8.69% as against the MYT approved at 10.43% in the financial year 2008-09, Based on this, the Commission assumed that the loss for the Financial Year 2009-10 should be lower than the loss level achieved for 2008-09. Thus by using percentage reduction of 1.73% for the financial year 2009-10 over the financial year 2008-09 as approved in the MYT order, the Commission has revised the distribution loss in the year 2009-10 at 8.54% as against the MYT approved level of 10.25%. According to the appellant, the Commission has given similar treatment for distribution losses of Surat distribution area as stated in para 4.4.3 of the Tariff Order. In the case of Surat the loss approved in the MYT order for 2008-09 and 2009-10 was 6% , while the Commission revised it at 5.5% for FY 2008-09, and FY 2009-10.

8. According to the appellant, the Commission, contrary to the MYT Regulations and the very objectives of the MYT framework, acted in a manner as if when a

utility performs better the Regulator would continue to revise the benchmarks with the result that there is no incentive to the improvement in performance. Delhi Electricity Regulatory Commission, on the other hand, in its true up order for the financial year 2007-08 and ARR for 2008-10 has not revised the distribution loss trajectory although the two utilities namely, NDPL and BSES Yamuna Power Ltd. were able to achieve lower distribution loss in comparison to the target stated in the MYT order.

9. It is next contended that the Commission misconstrued the statutory regulations in such a manner that resulted in non-consideration of the actual Plant Availability Factor (PAF) and the actual Plant Load Factor (PLF) for the generating stations. Consequently, there has been disallowance of recovery of costs despite its performance being better than the norms of operations specified by the

respondent Commission in the Regulations. Regulation 15(i) of the GERC (Terms and Conditions of Tariff) Regulations, 2005 prescribed that the generators are required to ensure minimum target availability of 80% to recover the full capacity charges. The PAF and PLF considered in MYT order do not replace the performance norms specified by the GERC (Terms and Conditions of Tariff) Regulations, 2005 as the appellant's performance was better than the norms of operation specified by the Commission and it has been acknowledged by the Commission in its MYT order dated 17th January, 2009. Therefore, the PAF and the PLF considered by the Commission is not the trajectory to be specified to reach the normative level of performance. The MYT Regulations at 4.2(e) provides as follows:

(e) Trajectory for specific variables as may be stipulated by the Commission, ***where the***

performance of the applicant is sought to be improved *through incentives and disincentives."*

It is pleaded that the PLF is not within the control of the generator as it is depending on several uncontrollable factors; and the Maharashtra Electricity Regulatory Commission in its true up order has approved the gross generation as per actuals.

10. It is contended that the Commission has construed statutory regulations in such a way that it resulted in denial of eligible incentive for better PLF. Regulation 15(ii) of the Regulation, 2005 provide that all thermal power generating station should have target PLF of 80%. The appellant claimed incentives for its plants C,D,E, & F, as the actual PLF for the same was higher than the normative PLF which resulted in the

increasing generation to the extent of 570 MUs from the said stations.

11. It is contended that though the Commission is entitled to prescribe trajectory for variables in accordance with the GERC (MYT) Regulations 2007, approval of PLF in the MYT order does not amount to the trajectory. Regulation 8.2 of the MYT regulations deals with those variables for which trajectory has been defined. Regulation 8.2 of the MYT Regulations reads as under:

> "*Where the Commission has stipulated a trajectory for certain variables under this Regulations 8, the norms – specified in any other regulation, as the case may be, shall not apply with regard to such variables for such period as the trajectory has been so stipulated.*

12. Regulations 22 of the GERC (Terms and Conditions) Regulations, 2005 is referred to in this connection which provides as follows:

*"**Incentive:** Incentive shall be payable at a flat rate of 25.0 paise / kWh for ex-bus schedule energy corresponding to scheduled generation in excess of ex-bus energy corresponding to target Plant Load Factor."*

13. Thus, it is contented that Regulation 8.2 read with Regulation 4.2(e) of the MYT Regulations 2007 operates in a field different and distinct from Regulation 22 read with Regulation 15(ii) because Regulations 8.2 of the Regulations, 2007 permits Commission to specify the trajectory for certain variables, while Regulation 22 of the Regulations, 2005 provides for incentive for better performance. It is, therefore, incorrect for the Commission to alter its stated position in its MYT order while passing an order for APR during the same MYT period. For example, the Maharashtra Commission computed incentive based on 80% PLF or lower PLF in case of old generating plants.

14. It is next contended that the Commission in the impugned order deducted the amount of generation business receivables from the receivables of TPL-D (Ahmedabad) for computation of interest on working capital for TPL-D (Ahmedabad). In respect of TPL-D (Ahmedabad) for FY 2008-09 though the Regulations clearly contemplate taking into account receivables equivalent to two months', the Commission in the impugned order has deducted the receivables of the TPL-G(APP) which the Regulations do not contemplate. Similar erroneous computation of interest on working capital was made for FY 2009-2010. It was imperative to allow legitimate components of receivables without any deduction for calculation of interest on working capital for the distribution business. The working capital requirements for the TPL-D(Ahmedabad) and the interest on the same has been computed in accordance with the formula of applying the rate of

interest on the working capital requirement. Regulation 66 of the GERC Tariff Regulations, 2005 specified the formula for calculation of working capital requirement for distribution business considering the items such as (a) O&M costs for one month (b) maintenance spares at 1% of the gross fixed assets and (c) receivables equivalent to sale of two months. The Commission thus misconstrued the statutory regulations and acted contrary thereto.

15. It has been contended further that the Commission has apportioned income-tax paid by the Company amongst each business using profit before tax (PBT) principle of each business in final truing up. The appellant contends that Minimum Alternate Tax (MAT) rate was applicable for the FY 2008-09 for the purpose of income-tax of the Company as a whole consisting of core and non-core business. Tax is to be arrived at on profit and loss earned through generation and

distribution business as distinct from each other. As such, the income tax paid or payable for core business pertaining to generation and distribution should be applied separately as per the applicable tax rate. The tax rates applicable for generation business at Ahmedabad, and distribution business at Ahmedbad and Surat could be normal tax rate or MAT rate as per the applicable provisions of the Income Tax Act. Therefore, it is applicable income tax rate for generation and distribution respectively that needs to be considered so as to allow post tax return on equity as per the provisions of the Terms and Conditions of the Tariff Regulations. The appellant contends that applicable income tax rate for distribution business as per the provisions of the Income Tax Act 1961 is the MAT rate, while applicable tax rate for generation business at Ahmedabad is the normal corporate income tax rate at 33.9% which ought to have been allowed instead of MAT rate of 11.33%.

16. The Commission has apportioned the amount of tax paid amongst each business of the TPL as per PBT of each business. The Commission in the MYT order dated 17th January, 2009 allowed income tax for FY2007-08 at the rate of 33.99% on the approved Return on Equity (ROE) citing Regulation 66(20) of the GERC (Term and Conditions of Tariff) Regulation, 2005. The appellant is aggrieved with the Commission's finding that the income tax should be computed by applying tax rate on the ROE and not after grossing up as the Commission held that it was not so permissible under the Tariff Regulations.. The appellant referred to Regulation 7 of the GERC(Terms and Conditions of) Tariff Regulations, 2005 which provides as follows:

"the income tax should be treated as an expense and the same needs to be recovered from the beneficiaries; however tax on income from non-core business shall not constitute a pass through component in tariff and tax on such other income shall be borne by the generating company or transmission licensee or the distribution licensee."

The Appellant refers to the regulations 66(20) of the Regulations deasling with reasonable and actual entitled expenditure properly to be incurred which is as under:

"66(20) Expenses arising from and ancillary or incidental to other business of licensee for which income have been included, but limited to the amount of income so included."

17. According to the appellant, it was imperative to allow income tax by applying applicable income tax rate on

ROE considering post tax ROE of 14% for the core business because actual income tax payable by it is cumulative effect of core and non-core business. The Commission in the impugned order has apportioned the income tax paid for FY 2008-09 on the basis of the segregate PBT approach, while in the MYT order the Commission allowed income tax for FY 2007-08 during the final true up by applying income tax rate on the approved ROE without grossing up. The Commission approved the Income tax for FY 2009-10 by again applying income tax rate on ROE without grossing up. The methodology of applying tax rate at ROE as adopted by the Commission in FY 2007-08 ought to be continued for future years with modification by applying tax rate on grossed up ROE instead of directly on ROE to earn post tax return as per regulations.

18. It is alleged that the Commission in the impugned order overlooked the requirement of looking into the variables, and erroneously categorized the cost items as controllable and uncontrollable for the FY 2009-10. The provisions of Chapter 9, 10 and 11 of the GERC (MYT Framework) Regulations, 2007 deal with APR and provide for identification of variation by the Commission as controllable and uncontrollable factors. For example, Maharashtra Commission has specified that factors for variation will be categorized as controllable or uncontrollable.

19. It is alleged that the Commission has committed error in computing the wheeling charges as it has not determined the wheeling charges in terms of the capacity to be reserved. The charges have been approved by the Commission in paise per kWh as against MW. However, the order of the Commission is not consistent with the provision of GERC (Open

Access in intra-State Transmission and Distribution) Regulations, 2005 that provides for determination of the open access charges in terms of the capacity basis. It is contended that if long term users are charged on the basis of energy wheeled instead of capacity reserved the appellant would not be able to recover its full cost in case of lower utilization of the capacity bookd. Again, the impugned order has encouraged new level of cross subsidy instead of reducing it in terms of Section 61(g) of the Regulations.

20. Lastly, it is contended that discretionary treatment has been meted out to renewable energy purchase obligation and the order is silent on the waiver sought by the appellant in respect of RPO obligation for FY 2008-09. It is contended that the appellant had impugned the MYT Order dated January 17, 2009 in Case No. 939 of 2008 in this Tribunal, in appeal No.

68 of 2009 wherein the GERC had erred in its treatment of the RPO obligations of the appellant. The Commission has now specified the RPO as a percentage of energy requirements instead of sales. In the MYT Order dated January 17, 2009 in Case No. 939 of 2008 the GERC has computed the RPO on the basis of energy sales. The relevant portion is extracted from para 4.3.5 of the impugned order below in relation to Ahmedabad.

"Purchase of 4% of total, 6% and 8% of total sales during 2008-2009, 2009-2010 and 2010-2011 including the backlog."

This has been now specified as under:

"The energy from wind has been computed as 5.24% (the RPO obligation approved in the MYT Order) of total energy requirement of Ahmedabad."

Similar treatment is also said to have been given to Surat distribution at para 4.4.5 of the impugned order.

21. The lone Respondent GERC filed a written note of submissions against the memorandum of appeal on 09.07.2010 to controvert certain points raised by the appellant. As regards sharing of gains, it contends that as the MYT Regulations did not specify any time frame for utilizing the reserve it was necessary for the Commission to specify the time. However, the Commission decided that reserve should be utilized in the interest of the consumers for reducing the impact of tariff shock. Thus, the Commission held that 1/3rd of the gains should be utilized by passing it to the consumers additionally alongwith the 1/3rd share available with the consumers. However, any gains or losses due to uncontrollable parameters have been fully

passed through as rebate / charges on tariff. The Commission says that there is no actual impact of Commission's decision on this point because there has been no change in the tariff order. The Commission calculated the total tariff rebate for the FY 2008-09 to be shared with the consumers and the amount has been actually used while computing tariff of the FY 2010-11 in the ARR order.

22. On the issue of alleged erroneous treatment of interest on working capital it is contended by the Commission that as the interest on working capital in the audited accounts is zero the efficiency gains has been computed accordingly. As the appellant admitted that there was no interest on working capital, the approved interest on working capital under the MYT orders shall fall under the category of gain. The entire interest on working capital cannot be considered as uncontrollable

and the Commission identified each component either as controllable or uncontrollable. The Commission says that while rectifying the computation of gains and losses suo motu it rectified the figure of working capital requirement of generation business. Therefore, the issue regarding actual fuel cost for normative equivalent has been duly addressed by the Commission in the subsequent order dated 11th March, 2010.

23. As regards alleged erroneous revision of distribution loss trajectory, the Commission says that the distribution loss has been estimated for FY 2009-10 only to estimate energy requirement and in the FY 2009-10 ARR order the gains/loss computation for FY 2009-10 has been done with respect to loss approved in the MYT orders and not with respect to the loss estimated in FY 2008-09 ARR order. The Commission further says that clarification with respect to the loss

estimated in FY 2008-09 has been given in the order dated 31.03.2010 passed in Review Petition No. 1001 of 2010.

24. With respect to alleged non-consideration of PAF and PLF it has been contended that PAF is not totally uncontrollable because it depends upon proper upkeep and maintenance work by the appellant which is controllable. In the case of station 'C' and Vatva the Commission treated PAF as uncontrollable . In case of PLF the Commission treated PLF for all plant as uncontrollable in the review order dated 31.03.2010.

25. As regards alleged denial of eligible incentive for better PLF, Commission says that Regulation 8.2 of MYT Regulations, 2007 when read with conjunction with Regulation 15(ii) of the Tariff Regulations, 2005 implies that the normative level of trajectory as prescribed

under Regulation 15(ii) should be replaced with the trajectory set out in Regulation 8 of the MYT Framework Regulation, 2007. According to the Commission, trajectory approved under the MYT Regulations shall prevail over the norms provided in the Tariff Regulations, 2005. PAF and PLF approved in the MYT order are higher than 80% which is normative as per the Terms and Conditions of the Tariff Regulations,2005. Therefore, the MYT framework should be used as basis for deciding the incentive framework. The very purpose of MYT framework is to provide performance trajectory for the utility and the trajectory specified in the MYT order has been estimated on the basis of past performance and projected fuel supply and maintenance issues.

26. As regards the alleged non-consideration of TPL-G receivables while computing TPL- (D) Ahmedabad

receivables for interest on working capital it is contended that the Commission has taken care to ensure that there occurred no double counting of receivables. The Appellant's unified corporate structure allows synergies between business units the benefits of which should be passed on to the consumers. As such, there cannot be any receivables arising out of TPL-G for TPL- D Ahmedabad.

27. As regards the alleged erroneous treatment of tax rate applicable for TPL-G towards income tax, it is contended that the appellant in its tariff petition had asked for an amount of Rs. 113.29 crores towards income tax for their three business (Viz. TPL-Generation, TPL Ahmedabad Distribution and TPL – Surat Distribution). As against this, the actual income tax paid by the appellant for all the three businesses was Rs. 55 Crores only. Despite repeated reminders

from the Commission during the tariff order processing period to submit segregated details of income tax paid for each of the three businesses, the appellant did not submit the same. The details about MAT rate was not provided to the Commission during the tariff order processing period. The only details available with the Commission was segregated PBT based on which the total income tax was allocated amongst the three businesses. The Commission directed the appellant to submit segregated details of income tax paid by them for its three businesses. However, the same were not submitted by the appellant. The appellant submitted the details regarding actual pay out of income tax by them based on the profit before tax. The Commission computed income tax considering the actual pay out and then apportioned the same as per the profit before tax of each business. The details of the same are as under :

Particulars	TPL Corporate	TPL-Gen Ahmedabad	TPL-Dist Ahmedabad	TPL-Surat
Profit before Tax	484.81	100.37	134.82	20.95
Tax	55	11.39	15.29	2.38

It is contended that the appellant had paid tax of RS. 55 crore during the FY 2008-09. The Commission divided the tax amount in the regulated business and non-regulated business. If the appellant had any grievances against the tax amount approved by the Commission, the appellant should have demonstrated the same by submitting necessary evidence on record clarifying the tax calculated/paid by them for various activities to the Commission. The Commission had computed income tax considering the actual pay out and then apportioned it as per the profit before tax on each business as the total tax liability does not change.

28. With respect to the alleged disallowance of income tax to earn ROE post tax the commission says that the tax has been computed as per GERC Terms and Conditions of Tariff Regulations which provides that tax should be computed on permissible returns which is ROE. The terms and conditions of Tariff Regulations notified by the Commission read as under :

> "*The Commission may also allow reasonable expenditure to be incurred actually and properly on the following:-*
>
> *a) All taxes on income and profit calculated on permissible return as allowed by the Commission relating to business of electricity and also subject to the condition that the amount of taxes is actually paid as tax after taking into account refunds into consideration.*"

According to the above Regulations, the appellant is entitled to get the income tax on actual basis. The

Commission has granted income tax as per Regulation 66(20) of the Terms and Conditions of Tariff Regulations, 2005. It is submitted that the appellant had in Appeal No. 68 of 2009 challenged the calculation of income tax allowed by the Commission in MYT Order dated 17.01.2009 in case No. 939 of 2008 and claimed that ROE should be allowed at 14% post tax. This Tribunal had allowed the same observing that the ROE is to be allowed by grossing up of the Income Tax. The Commission has filed Review Petition against the order dated 23.03.2010 of the Tribunal in Appeal No. 68 of 2009 for certain clarifications. The Commission has allowed Income Tax on the RoE amount eligible to the appellant at the prevailing income tax rate. As regards the income tax allowed by the Commission for the year 2007-08 on grossing up the basis of RoE i.e. post tax is not correct. Para 3.21 order dated 17.01.2009 in Case No. 939 of 2008 stipulates that the Commission has allowed income tax at Rs. 68.20 crores for the FY 2007-08 on ROE of an amount of Rs. 200.65 crore.

29. As regards the alleged erroneous classification of cost items as controllable, the Commission says that it considered controllability / uncontrollability of factors before deciding on a cost item as controllable / uncontrollable. This is amply evident through Commission's finding regarding station availability, PLF, capital expenditure, depreciation in the impugned order dated 09.12.2009 wherein the Commission has considered the causative factors behind the items and then classified them as controllable or uncontrollable

30. With regard to the alleged error in computation of wheeling charges the Commission says that the issue was also raised by the appellant in the Appeal No. 68 of 2009 against the Commission's order dated 17.01.2009 in Petition No. 939 of 2008. Since the appeal was

pending at the time of issue of the impugned order dated 09.12.2009, the Commission continued the methodology adopted earlier.

31. With respect to the alleged discriminatory treatment of renewable purchase obligation, the Commission stipulates that the Commission's Power procurement from Renewable Sources Regulation specifies that:

> *"3.1 Each Distribution Licensee shall purchase a defined minimum quantum of its total consumption of electricity during a year from renewable sources."*

The term "Total consumption" means energy requirement, not sales. The Commission has considered the waiver sought by the appellant by seeking details about the appellant's efforts in procuring RE power by advertising in various newspapers and acknowledging the same. The Commission has considered the practical constraints faced by the appellant in sourcing RE power and has accordingly not imposed any penalty in RPO for the year 2009-10. It has been clarified that the Renewable Purchase Obligation of the appellants is calculated on the basis of submissions made by the appellant.

32. After the impugned order was passed the appellant filed a petition praying for clarification / rectification being Petition NO. 1001 of 2010 which has been disposed of by the Commission by an order dated 31.03.2010; and by virtue of this order the scope of the present appeal has been narrowed down only to certain issues. However, in the said clarificatory order the Commission dealt with (a) future liability of income tax, (b) allowance of gains on account of distribution loss as per MYT trajectory, (c) sharing of gains due to improvement in distribution loss for both TPL-D (Ahmedabad) and TPL-D (Surat), (d) reconciliation of energy balance of TPL-D

and consideration of actual generation on TPL-G (app), (e) amount of gains/losses on account of TPL-G (APP) non-factoring in TPL-D ARR for its rebate / recovery, (f) treatment of sale of surplus power to GUVNL, (g) gains on account of improvement in auxiliary consumption, (h) consideration on bad debt written off instead of provisions for bad-debt, (i) revised computation for gains / loss on account of controllable expenses in TPL-G (APP), (j) revised computation for gains / losses on account of controllable expenses TPL-Ahmedabad., (k) revised computation of gains / losses on account of controllable expenses in TPL-Surat (l) revised gap / surplus and (m) interest on security deposit as uncontrollable items of expenses.

33. In the Commission's written note of submission filed in response to the memorandum of appeal the clarificatory order dated 31.03.2010 has been referred to and after the Commission filed its written notes of

submission the appellant filed a rejoinder which we state herein below. In the rejoinder, the appellant states that the four issues namely (a) disallowance of income tax to earn return on equity as post tax, (b) classification of cost items as controllable and uncontrollable, (c) error in computing the wheeling charges and (d) the discriminatory treatment meted out to the renewable purchase obligation (RPO) are covered by a decision of this Tribunal dated 23.03.2010 in Appeal No. 68 of 2009 (Torrent Power Ltd. Vs. Gujarat Electricity Regulatory Commission) although the Commission filed a review petition being petition no. 09 of 2010 seeking review of the said judgment dated 23.03.2010 on two grounds namely (a) disallowance of income tax to earn return on equity as post tax, and (b) transit loss of coal.

34. With respect to sharing of gains, the appellant does not say any thing new but reiterates its contention in more detail in the affidavit in rejoinder.

35. With regard to the alleged erroneous treatment of interest on working capital it reiterates its earlier contentions.

36. With respect to the alleged erroneous revision of distribution losses the appellant does not press this point as the clarificatory order date 31.03.2010 is said to have addressed the grievance of the appellant.

37. With respect to the ground of alleged misconstruing the statutory regulations resulting into non-consideration of actual PAF and PLF it is contended by the appellant that in the clarificatory order dated 31.03.2010 the Commission treated PLF for all plants as uncontrollable but in case of PAF the appellants contends that in station 'C' and Vatva it has considered the PAF as uncontrollable. The appellant submits that the

estimates of PAF based on the planned and the forced outages of the plant on the basis of past performance to arrive at the correct energy requirement during MYT process. The Commission in MYT order dated 17.01.2009 has found these estimates in line with the past trends and has accordingly approved it as was projected by the appellant.

38. It is contended that the Commission did not deal with in the clarificatory order the statutory regulations concerning eligibility to incentive for better PLF for FY 2008-09.

39. With regard to the non-consideration of TPL-D (Ahmedabad) receivables the appellant reiterates its earlier contentions made in the memorandum of appeal.

40. With regard to the treatment of tax rate applicability to TPL-D towards income tax it is contended that the Commission should be directed to calculate the income

tax in accordance with the judgment dated 23.03.2010 of this Tribunal.

41. On the basis of the aforesaid pleadings we consider the following issues:

    i. Whether the Commission was justified in passing 1/3 of the gains on account of controllable factors to the consumers instead of entitling it to the special reserve maintained by the appellant so as to absorb its future losses?

    ii. Whether the Commission was justified in not allowing interest on working capital to the appellant instead of passing on to the consumers as gains?

    iii. Whether the Commission misconstrued the statutory regulations resulting in non-consideration of actual PAF and PLF for the generating stations?

iv. Whether the Commission was justified in construing the regulations resulting in denial of incentives on PLF for FY 2008-09?

v. Whether the Commission was justified in not considering of TPL -D (Ahmedabad) receivables by deducting TPL-G ARR in calculation of working capital requirement?

vi. Whether the Commission was justified in the treatment in respect of the applicability of the tax rate for the TPL G towards income tax.

vii. Whether the disallowance of income tax to earn ROE as post tax justified?

viii. Whether the classification of costs items as controllable and uncontrollable contrary to the regulations?

ix. Whether the Commission committed error in computing the wheeling charges?

x. Whether the Commission's order in respect of renewable purchase obligation (RPO) a discriminatory treatment?

42. With respect to the sharing of gains on account of controllable factors the appellant argued that the Commission's finding is contrary to the GERC (MYT Frame Work) Regulations, 2007. We have reproduced in this connection regulation 11 of the Regulations, 2007 at paragraph 3 of the 'judgment' and we avoid repeating the same.

We find that the purpose of one-third amount under consideration in 11.1 (b) is to absorb the impact of future losses arising due to controllable factors under clause (b) of regulation 11.2. The regulations 11.2 provides the manner in which the approved aggregate loss to the licensee on account of controllable factors shall be dealt with. This regulations 11.1 and 11.2. (b) which have been framed by the State Commission under Section 181 of the Electricity Act, 2003 uses the word '*shall*' which in the absence of any qualifying word appears to be mandatory leaving no scope of discretion on the part of the Commission to do otherwise. Under the regulation 11 whatever is the entitlement to the end consumers by way of rebate is passed in tariff, and the amount exceeding thereto remains on the hands of the generating company or the licensee which has to be used in the 50:50 ratio in terms of (b) and (c) of the said regulations 11.1. The Regulator in their wisdom has thought it necessary to create a special reserve for the generating company or the licensee for the purpose of meeting the impact on any future loss due to controllable factors. Therefore, the said one-third of the amount which has to be put into as a special reserve cannot pass through the tariff by way of rebate to the comfort of the end consumers and to the discomfort of the generating company or the licensee which is not warranted in the law. Now, the Commission has contended that as the MYT Regulations do not specify any time for the utilization of such reserve except stating that it should be used in absorbing the impact of future losses the same should be specified by the Commission; as such the Commission decided that the reserve would be utilized in the interest of the consumers for reducing the impact of tariff shock. To our estimation, the Commission cannot in a tariff order interpret its own Regulations in a manner which is contrary to the provision of the Regulations and which because of the language thereof being very clearly employed does not approve of. The Commission cannot depart and make an arrangement contrary to the Rregulations clearly knowing that the arrangement it proposes to make is not in their own Regulations. The Commission in it written note of submissions lists the legislative intent correctly yet, while concluding it decided, however, to utilize the amount meant for reserve by passing it to the consumers in addition to the one-third share which under the law has also been passed through in tariff as rebate to the end consumers. It has been brought to our notice that the self same Commission in the case of M/s. Dakshin Gujrat Vij Company Ltd., a distribution licensee allowed only one-third of the gains derived from controllable parameters to the consumers. The Commission argued that there is no actual impact of Commission's decision on this point because there is no effect in the change in tariff in the said order. The Commission elaborates that it has simply calculated the total tariff rebate/hike for FY 2008-09 to be shared with consumers, i.e. the amount which has been actually used only while computing the tariff of FY 2010-2011 for the ARR order. This sort of reasoning is countered by the appellant's learned Counsel with the reasoning that the financial gap as at FY 2008-2009 has been arrived at considering two-third of the gains to be passed on to the consumers instead of one-third. When the provision to the Regulations, to our mind, has clearly provided that one-third of the amount is to be kept in reserve with the generating company or the licensee to meet the future losses, the matter has to rest there without any further deliberations as to whether any adverse financial impact in case of going contrary to the Regulations was perceptible. The GERC relied on Regulation 13.4 to contend that it has power to relax the Regulations so as to make departure there from. Regulation 13.4 reads as under:-

"Power of Relaxation :

13.4 The Commission may in public interest and for reasons to be recorded in writing, relax any of the provision of these Regulations."

The impugned order does not show that the Commission intended that its own Regulations 11 and 12 should be departed from in any public interest. The Commission departed from its own Regulations without showing any reason, and the arguments put forward in the written note of submissions were not used by the Commission in the impugned order while departing from its own Regulations. It appears that the reason given by the Commission in its written notes of arguments is intended to be used as supplemental to the impugned order. Order has to be explained or interpreted by the order itself. Reference may be had to the decision in *M.S. Gill V/s Chief Election Commissioned, New Delhi reported in 1978 (1) SCC 405.* It has been argued by the appellant that in case of Dakshin Gujrat Vij Co.Ltd. the treatment has been given to the utility by the Commission in line with the spirit of the law. We also notice that in case of loss on account of controllable factors two-third of such loss is absorbed by the generating company or licensee according to Regulation 11.2. However, in case of gain instead of passing on two-third to the generating company or licensee only one-third has been allowed and balance one-third is to be retained by the generating company or licensee in a special reserve for the purpose of absorbing any future loss on account of controllable factors. Thus, there is also no logic in the argument of the Commission that it has no impact on the appellant. Therefore, we are of the opinion that the finding of the Commission on this score is not legally justifiable and it needs interference.

43. With regard to interest on working capital, the Commission has compared the interest with that incurred through external funding and difference has been termed as efficiency gain. The Commission is of the opinion that interest on working capital funded through internal accruals has been considered as efficiency gain and

passed on to the consumers. This, to our perception does not seem to be in consonance with the spirit of the law. What are the requirements to be considered in working out the interest on working capital has been laid down in regulation 20 (v) (a) of the Tariff Regulations, 2005. According to this Regulation, working capital in case of coal based/lignite fired generating stations covers (i) cost of coal for one and half months for pit head generating stations and two months for non-pit head genera ting stations, (ii) cost of secondary fuel oil for two months, (iii) operation and maintenance expense for one month, (iv) maintenance spares @ 1% of the historical cost escalated at 6% per annum from the date of commercial operation, and (v) receivables for two months of fixed and variable charges for sale of electricity. In the case of gas turbine the components are fuel cost for one month and liquid fuel stock for half month apart from the last three of the coal based stations. It cannot be contradicted that the need of the working capital is calculated on the day-today business of the utility and the mode of funding the working capital is based primarily on the financial condition and economic scenario of the generating company or the licensee. It has been rightly observed that the working capital requirements vary with the variation in cost items for various reasons. It is not necessary to consider in detail the cost items for various reasons such as fuel price, power purchase, O & M cost and receivables. It is countered by the Commission that since the appellant has not shown any interest on working capital the approved interest on such working capital under the MYT Frame Work shall fall under the category of gain. The Commission reasoned that the interest on working capital cannot be treated as uncontrollable on the ground that some of the components are uncontrollable. Since the appellant has not claimed any interest on working capital no amount thereon should be provided to the appellant. This reason of the Commission does not appeal to us. It cannot be denied that the interest on working capital is based on controllable and uncontrollable factors. The variation on account of uncontrollable factors should have been entirely passed on to the consumers. Therefore variation in the working capital requirement requires to be segregated between controllable and uncontrollable factors. Uncontrollable factors are mainly the fuel cost, power purchase cost and increase in receivables as said above. In this connection, we may refer to Regulation 20 (i)(v)(b) of the GERC (Terms and Conditions of Tariff) Regulations, 2005 which is reproduced below:

> "*(b) Rate of interest on working capital shall be on normative basis and shall be equal to the short-term Prime Lending Rate of State Bank of India as on 1.4.2004 or on 1st April of the year in which the*

generating station or unit thereof is declared under commercial operation, whichever, is later. The interest on working capital shall be payable on normative basis notwithstanding that the generating company has not taken working capital loan from any outside agency"

In this connection, reliance has been placed on the decision of this Tribunal in *Reliance Infrastructure Ltd. V/s MERC and Ors. reported in 2009 ELR (APTEL) 672 which is as under:*

"*It is true that internal funds also deserve interest in as much as the internal fund when employed as working capital loses the interest it could have earned by investment elsewhere. Further, the licensee can never have any funds which has no cost. The internal accruals are not like some reserve which does not carry any cost. Internal accruals could have been inter corporate deposits, as suggested on behalf of the Appellant. In that case the same would also carry the* *cost of interest. When the Commission observed that the REL had actually not incurred any expenditure towards interest on working capital it should have also considered if the internal accruals had to bear some costs themselves. The Commission could have looked into the source of such internal accruals and the cost of generating such accruals. The cost of such accruals or funds could be less or more than the normative interest. In arriving at whether there was a gain or loss the Commission was required to take the total picture into consideration which the Commission has not done. It cannot be said that simply because, internal accruals were used and there was no outflow of funds by way of interest on working capital and hence the entire interest on working capital was gain which could be shared as per Regulation No. 19. Accordingly, the claim of the Appellant that it has wrongly been made to share the* *interest on working capital as per Regulation 19 has merit.”*

Thus we find that the issue on this account is no longer res integra. It has been rightly argued that as each item of ARR has been segregated as controllable and uncontrollable for calculation of gains and losses, the same should have been used for segregation of constituents of working capital requirements between controllable and uncontrollable factors. We are to observe in this connection that the Commission in its order dated 31.3.2010 passed in the clarificatory petition has revised its order of December 09, 2009 by allowing the TPL’s contentions on interest on working capital in respect of generating business. Therefore, this aspect of the matter concerning computation of working capital requirement considering actuals instead of MYT approved figures has been addressed to. The Commission has revised the workings for interest on working capital of TPL-G (APP) by re-computing it on normative basis considering the revised fuel cost numbers. In the order dated 9th December, 2009 the Commission gave a summary of interest on working capital expense for FY 2008-09 as follows:-

Particulars	MYT Order	Actual	Considered for APR for FY 2008-09
Interest on working capital	26.63 crore	0.00	26.63

In the clarificatory order the Commission revised the workings for interest on working capital of TPL-G (APP) by re-computing it on a normative basis considering the revised fuel cost numbers and accordingly the above table was revised to read as Rs.35.66 crores as considered for

APR of FY 2008-09. Learned Counsel for the appellant has a point when she says that the variation in working capital requirement should have been segregated between " controllable" and "uncontrollable " factors instead of treating entire interest on working capital as controllable in accordance with MYT Framework Regulations.

44. The two questions namely whether the Commission misconstrued the statutory regulations resulting in non-consideration of actual PAF and PLF for the generating stations and the question whether the Commission was justified in construing the regulations resulting the denial of incentives of PLF for FY 2008-09 are being discussed. On the 1st question it appears that the Commission has agreed that the appellant's contention that the PLF should be considered as uncontrollable because actual PLF achieved by the plant primarily depends on system load which is not controllable factor for the generating station.

However, we find the provision in Regulation 15 (i) of the Tariff Regulations, 2005 as follows:

> *"15. Norms of operation: The norms of operation as given hereunder shall apply:*
>
> *(i)* ***<u>Target Availability for recovery of full capacity (Fixed) charges</u>***
>
> ***<u>(a)</u>*** *All thermal power generating stations 80%*
>
> ***Note***
>
> *Recovery of capacity (fixed) charges below the level of target availability shall be on pro rata basis. At zero availability, no capacity charges shall be payable.*
>
> *Further, where existing PPAs (including any charges, in the norms or parameters, made in the PPA following renegotiation between the Board and*

concerned generating company) lay down a different Parameter like PLF for recovery of the full fixed charges, such a parameter shall continue to govern the parties for the term of the contract, but not for any renewal of the contract or any extension of the term of the contract in accordance with its terms. Upon the expiry of the term of the existing PPA (including any changes, in the norms or parameters, made in the PPA following renegotiation between the Board and concerned generating company), the parties shall be governed by the terms of the Regulations for the time being in force."

45. Regulation 8 of the GERC (MYT Framework) Regulations, 2007 provides as follows:

"*8.1. The Commission may stipulate a trajectory which may cover one or more control periods, for certain variables provided that the variables for which a trajectory may be stipulated include but are not* *limited to generating station availability plant load factor station heat rate, auxiliary consumption specific oil consumption, transit loss transmission losses, transmission system availability distribution technical losses distribution commercial losses and collection efficiency.*

Regulation 1.2 of MYT Regulations reads as under:

"These regulations will be an appendix to the GERC (Terms and Conditions of Tariff) Regulation in the event of any inconsistency between the two regulations the Multi Year Tariff Framework Regulation would prevail".

The Commission is of the view that the trajectory approved by the Commission under the MYT Regulations as framed by the Commission shall prevail over the norms provided in tariff Regulations of the Commission. As the PAF and PLF approved by the Commission in MYT order are higher than 80% which is the normative as per terms and conditions of tariff regulations a set of parameters in the MYT framework order is required to be considered while calculating gains/losses. According to the Commission, the MYT order should be used as a basis for deciding the normative frame work. The very purpose of MYT Framework is to provide performance trajectory for the utility and accordingly incentives/disincentive is based on actual performance. The trajectory specified in MYT order has been estimated on past performance and projected fuel supply and maintenance issues. According to the appellant, PAF and PLF as considered in the MYT order do not replace the performance norms specified in the Tariff Regulations, 2005. The PAF and PLF considered by the Commission is not a trajectory to be specified to reach the normative level of performance. The same is provided in Regulations 4.2 (e) of the GERC MYT Regulations.

"(e) *Trajectory for specific variables as may be stipulated by the Commission,* ***where the performance of the applicant is sought to be improved*** *through incentives and disincentives:*

According to the appellant, as PLF is based on number of uncontrollable factors it has to be approved as per actual. For instance, the Maharashtra State Electricity Regulatory Commission in its true up order has approved gross generation as per actuals. In case of Tata Power – G(Case no. 111 of 2008 dated 28th May, 2009) the actual availability and generation both were lower than what was approved in MYT, while in the case of Reliance Infra-G (Case No. 120 of 2008 dated 28th May, 2009) the actual generation was more than MYT approved. In both the cases the MERC approved actual generation. However, the Commission in the clarificatory order dated 31stMarch, 2010 passed in GERC Case No. 1001/2010 has rectified the gross generation for FY 2008-09 by treating PLF as uncontrollable. But in the case of PAF the Commission was of the view that it cannot be treated as completely uncontrollable. The appellant contended that the estimates of PAF based on planned and forced outage of the plant is on the basis of past performance so as to arrive at the correct energy requirement during the MYT process. The Commission in the MYT order dated 17th January, 2009 has found these estimates in line with the past trends and has accordingly approved it as projected by the appellant. Now, the Norms of Operation specified in the Tariff Regulations would prevail over the MYT approved projections as far as the financial implications are concerned. The Norms of Operation cannot be different for different utilities except where performance of the utility is sought to be improved when the performance is below the norms. Thus, the appellant contends that interpretation by the Commission that the approval of the estimated figures which are higher than the norms amounts to the trajectory does not only penalize the performing utility but also amounts to discrimination and is against the very purpose of specifying the norms in the Regulations. Further, the contention of the Commission is also contrary to its own MYT order where it has clarified that the norms of 80% specified in the Regulations will be considered for actual performance for the purpose of payment of incentives. Therefore, the contention of the Commission that the approval of PAF and PLF amounts to trajectory is erroneous. To our mind, trajectory in respect of specific variables is stipulated by the Commission to inspire and induce the utility to improve its performance through incentives and disincentives. MYT Framework order and the Tariff Regulations do not clash with each other because they operate in their respective fields. There cannot be any question of one superseding the other . Norms of Operation stand uniform to all the utilities while trajectory differs from utility to utility. Thus there cannot be any good bye to the Norms of Operation specified in the Tariff Regulations. Regulation 4.2. (e) of the GERC MYT regulations confirms this position. To hold that the approval of the estimated figures which are higher than the norms amounts to trajectory is to discourage incentive when the incentive is really warranted.

46. In the MYT Framework Regulations it has been clarified that the norms of 80% as specified in the Regulations would be considered for actual performance for the purpose of payment of incentives. We may refer to in this connection the paragraph 4.1.17 of the GERC MYT order dated 17th January, 2009. Exclusive reliance of the Commission on regulation 8.1. to the exclusion of other regulations can hardly be appreciated. For the purpose of incentive the Terms and Conditions of Tariff Regulations have to be followed. Incentive is payable on the basis of actual generation in excess of generation beyond 80% normative PLF and it is evident from the MYT order dated 17th January, 2009. The paragraph 4.1.17 of the MYT order dated

17th January, 2009 passed in case No. 939 of 2008 dealt with incentive and is reproduced below:

"4.1.17 Incentive

As per Clause 22 of GERC Regulations, 2005, an incentive is payable at 25 paise / kWh for the actual generation in excess of generation beyond 80% normative PLF. This is not considered as part of ARR as it is not a cost component.

This is payable at the end of the year based on actual generation"

Therefore, the matter needs to be re-looked and revisited with by the Commission for appropriate order in the light of the statutory provisions discussed above.

47. The appellant is aggrieved by non consideration of TPL-D (Ahmedabad) receivables because of

deduction of TPL-G ARR in calculation of working capital requirements contrary to the Regulations. Regulation 66 of the Tariff Regulations,2005 is a specific provision dealing with principles, terms and conditions for determination of tariff along with their applications for distribution licensee. It has specified formula for calculation of working capital requirements for distribution business. According to the appellant, the Commission in the impugned order has wrongly deducted the amount of generation business receivables for TPL-D (Ahmedabad) for computing the interest on working capital which the Regulations do not approve of because interest on working capital facility would include O&M expenses for one month, maintenance spares at 1% of the gross fixed assets historic cost escalated at 6% per annum from the date of commercial operation and receivables equivalent to sale of two months. According to the appellant, working capital requirement for TPL- D (Ahmedabad) and the interest on the same should have been computed in accordance with the formula by applying rate of interest on the working capital requirement. Now, the Commission has viewed that to allow in the case of TPL –G receivables would amount to double counting of receivables because the appellant is a unified corporate structure that allows for synergies between business units benefits of which should be passed on to the consumers. In our estimation, the provisions of the Regulations allow the legitimate component of receivables without any deduction for calculations of interest on working capital for the distribution licenses. The same has to be allowed. It bears recalling that while computing gains on account of improvement in auxiliary consumption , the Commission in its order date 31st March, 2003 computed gains by considering the variable cost of respective generating stations based on the principles that generation and distribution business are two different entities. Further it was the Commission that directed the appellant to maintain separate books of accounts for the two businesses as mandated by the Regulations. If it is so, then it is difficult to appreciate as to how in respect of calculating interest on working capital of TPL-D(Ahmedabad) the Commission could deduct the amount of generation receivables from the receivables of TPL-D (Ahmedabad) because the Regulations do not say that where generation and distribution business form a part of single corporate entity deductions have to be made from the receivables of distribution. It is brought to our notice that for calculation of gains on account of auxiliary consumption and maintenance of accounts, the Commission considered each business separately but considered both businesses as part of single entity for calculation of interest on working capital. We therefore reverse the finding of the Commission on this score.

48. The next question is whether the Commission was justified in its treatment of applicability of the tax rate for TPL-G towards Income-Tax. According to the appellant, minimum alternate tax rate is applicable for the FY 2008-2009 for the purpose of income tax for Company as a whole consisting of core and non-core businesses. Generation and Distribution business which are distinct from each other is the core business. Therefore, it is the applicable income tax rate for generation and distribution that needs to be considered so as to allow post tax return on equity in terms and conditions of the Tariff Regulations. The appellant claims deduction under Section 80(I) (A) of the Income Tax Act, 1961 for the purpose of income of distribution

business. Accordingly it has rightly been argued that minimum alternate tax rate is applicable only for the distribution business, while for the purpose of generation business it is the normal corporate income tax rate of 33.99% which is available instead of minimum alternate tax rate of 11.33%. The Commission observes that despite repeated reminders the appellant did not submit segregated details of income tax paid for each of the three businesses but as a whole the appellant paid Rs.55 crores only covering the three businesses which is why the Commission apportioned the tax payable in respect of the three businesses by dividing the amount of tax with the regulated and non regulated business. The Commission computed the income tax considering the actual pay out and then apportioned it as per profit before tax (PBT) of each business since the actual tax liability does not change. We direct the Commission to re-examine the matter in the line of the settled principles as held in this Tribunal's judgment dated 23.3.2010 in Appeal No. 68 of 2009 and dated 1.2.2011 in RP 09 of 2010 (Torrent Power Ltd. Vs GERC) and equally direct the appellant to furnish before the Commission all such materials as necessary for the purpose of and is directed by the Commission on this behalf. However, it is to be noted that the appellant would neither benefit not lose on account of income tax as laid down in the above judgment.

49. The next question is whether the Commission was justified in disallowing of income tax to earn return on equity as post tax.

This issue was already decided earlier by this Tribunal in appeal No. 68 of 2009 (Torrent Power Limited Vs. GERC) Paragraph 50 of the said judgment which we reproduce below is decisive on this point and we reiterate the same :

"50. Main contention of the Appellant is that whereas it had claimed Income Tax rate so as to

provide it a post tax regulatory return of 14%, the Commission in the impugned order has calculated Income Tax on the approved rate of return on equity which has resulted in a post tax return of 11.55% instead of this stipulated 14% return. As the Appellant has submitted that provisions of Regulation 66 and Regulation 7 of the GERC (Terms and Conditions of Tariff) Regulations, 2005 have to be read together, relevant extracts of these two Regulations, are extracted below:

Regulation 66: Principles, terms and conditions for determination of tariff along with their application for Distribution Licensee.

> *"The tariff shall be fixed in such a manner that a licensee ordinarily in any financial year will earn a permissible return which shall comprise of 14% on equity invested into capital expenditure (apportioned to the quantum for the purpose of performing the business electricity in the present debt equity on structure) plus permitted incentives minus penalties leviable under the Act/Regulations for that year. The incentives would result from normative targets on Aggregate Technical and commercial losses (AT&C) for the licensee. The Commission would define the AT&C targets in line with the regulation on Multi Year Tariff principles.*
> *…………"*
> *Regulation 7.1: Tax on Income.*
> *Tax on the income streams of the generating company or the transmission licensee or the distribution licensee, as the case may be, from its core business, shall be computed as an expense and shall be recovered from the beneficiaries.*

51. Regulation 7.1 states that tax on the income streams from the core business of the company shall be computed as an expense and the same shall be recovered from the beneficiaries. Regulation 66 stipulates that the tariff shall be fixed in such a manner that a licensee ordinarily in any financial year will earn a permissible return which shall comprise of 14% on equity. Here it is pertinent to advert to the following provision of the Income Tax Act, 1961 regarding Tax on Income.

"Income Payable " net of tax"

195. In a case other than that referred to in sub-section (1A) of Section 192, the tax chargeable on any income referred to in the foregoing provisions of this Chapter is to be borne by the person by whom the income is payable, then, for the purposes of deduction of tax under those provisions such income shall be increased to such amount as would, after deduction of tax thereon at the rates in force for the financial year in which such income is payable, be equal to the net amount payable under such agreement or arrangement."

52. A conjoint reading of the Regulation 7, Regulation 66 of the State Commission and Section 195(A) of the Income Tax Act, 1961 leaves no doubt that the recovery of income tax paid as an expense from the beneficiaries requires to be grossed up in such a manner as to ensure that the actual tax paid is fully recovered through tariff. Grossing up of the return would ensure that after paying the tax, the admissible post tax return is assured to the Appellant. In this way the Appellant would neither benefit nor loose on account of tax payable which is a pass through in the tariff. This would ensure that the Appellant *earns permissible return of 14% stipulated in Regulation 66 of the Regulations and mandate of Section 195A of the Income Tax Act is also complied with. The National Tariff Policy stipulates that the Regulatory Commission may adopt rate of return as notified by the Central Commission with appropriate modifications taking into view the higher risk involved in distribution and that a uniform approach is desired in respect of return on investment.*

53. We agree with the contention of the Respondent Commission that CERC Regulations, 2009 are not applicable in this case of the Appellant. However, the provisions of CERC Tariff Regulations, 2004 will be of relevance. The relevant clause regarding tax on income of these CERC Regulations is extracted below:

" 7. Tax on Income: (1) Tax on the income streams of the generating company or the transmission licensee, as the case may be, from its core business shall be computed as an expense and shall be recovered from the beneficiaries.

(2) Any under-recoveries or over-recoveries of tax on income shall be adjusted every year on the basis of income-tax assessment under the Income Tax Act, 1961, as certified by the statutory auditors.

Provided that tax on any income stream other than the core business shall not constitute a pass through component in tariff and tax on such other income shall be payable by the generating company or transmission licensee, as the case may be. Provided further that the generating station-wise profit before tax in the case of the generating company and the region-wise profit before tax in case of the transmission licensee as *estimated for a year in advance shall constitute the basis for distribution of the corporate tax liability to all the generating stations and regions.*

Provided further that the benefits of tax-holiday as applicable in accordance with the provisions of the Income-Tax Act, 1961 shall be passed on to the beneficiaries.

Provided further that in the absence of any other equitable basis the credit for carry forward losses and unabsorbed depreciation shall be given in the proportion as provided in the second proviso to this regulation.

Provided further that income-tax allocated to the thermal generating station shall be charged to the beneficiaries in the same proportion as annual fixed charges, the income-tax allocated to the hydro generating station shall be charged to the beneficiaries in the same proportion as annual capacity charges and in case of interstate transmission, the sharing of income-tax shall be in the same proportion as annual transmission charges."

54. The above provisions of Regulations, 2004 also make it clear that income tax payable on the income from the core business of the company is to be treated as an expense and recovered from the tariff payable by beneficiaries. The income earned by the licensee is net of tax and the tax payable is treated as a separate expenditure recoverable from the beneficiaries.

55. In view of the foregoing discussion and analysis, we set aside order of the State Commission in this view of the matter and direct *that it allows the income tax by grossing up to ensure the stipulated post tax return by the State Commission to the Appellant."*

50. We also state here that this matter was again clarified in RP No. 09 of 2010 in connection with appeal No. 68 of 2009 where it was observed as follows:-

"10. Regulation 7 clearly stipulated that the tax on income stream of the generating company from its core business shall be computed as expense and shall be recovered from the beneficiaries. The adjustment for under or over recovery of any amount from beneficiary has to be made by the generating company directly on the basis of income tax assessment under the Income Tax Act as certified by the statutory auditors. Regulation 66(20) only restricts the income tax to be allowed on the permissible return subject to actual payment.

11. This is the only difference in the State Commission's Regulations with reference to the Regulations of 2004 of the Central Commission in respect of Income Tax. The Central Commission's Regulations of 2004 allow income tax as pass through even on income over and above the permissible return on equity due to better performance over the generation norms. However, the State Commission's Regulations allow the income tax on the permissible return. The *principle of grossed up tax is applicable to both as decided by this Tribunal in the impugned judgment and in various other cases referred to by the Respondent.*

12. *Conjoint reading of the Regulations of the State Commission will imply that income tax has to be taken as expense subject to adjustment as per actuals as per audited accounts by the statutory auditors and to the extent of permissible return. However, tax on income on permissible return has to be 'pass through'. Thus the intent of the Regulations is that income on permissible return on core business in the hands of the generating company has to be net of tax. Thus the entire tax inclusive of grossed up tax is relatable to the core activity of the generating company. However, if there is any over-recovery of tax, the generating company has to reimburse the same as the same is adjustable as per actuals as per audited accounts by the statutory auditors.*

13. *The Tribunal's judgment dated 23.03.2010 in para 52 clearly shows that the Tribunal has considered Regulation 7 and Regulation 66 and Section 195 (A) of the Income Tax Act to arrive at the decision that grossing up of the tax has to be carried out to ensure that after paying the tax, the admissible post tax return is assured to the Appellant (Respondent in Review Petition), Torrent Power Limited. The Tribunal has also held in the judgment that the Appellant, Torrent Power Limited should neither benefit nor loose on account of tax payable which is a pass through in the tariff. Thus, there is no question of the generating company making profit on account of income tax. The excess recovery of income tax if any has to be reimbursed by the generating company to the distribution company as per the Regulations of the State Commission. In this case*

the excess recovery of income tax if any has to be adjusted in the true up of the financials. Thus the judgment dated 23.3.2010 needs no review. Accordingly the Commission was not justified in disallowance of income-tax to earn return on equity as post tax."

51. On the classification of cost items as controllable and uncontrollable as permissible in terms of the Regulations. This Tribunal has dealt this matter in appeal No. 68 of 2009 and we reproduce below what was held thereon:

> *"10. We note that the classification of various ARR items summarized in para 4.6.2 of the Impugned Order into controllable or uncontrollable items is in line with the MYT Regulations. It has been rightly admitted by the Commission that if there are any variations in various factors even in the controllable category of ARR items due to the factors enumerated in Regulations 9.6.1 and 9.6.2 (Supra) the same will be considered as an uncontrollable factor. The Regulations, by way of*

explanation do detail out various factors which fall beyond the control of the licensee and the same could be considered for allowing variations in the controllable items also. In view of this we do not wish to interfere with this decision of the Commission.

11. As far as the timing of truing up is concerned, the Regulation 12.1(b) (supra) clearly stipulates that approved gains and losses are to be passed through in tariff following the Annual Performance Review. In view of this we are not able to agree with the contention of the Commission that the truing up can wait till the next control period. Control period being three years, it cannot be the case of the State Commission that burden/benefits of the past years be passed on to the consumers of the future. It has to be kept in mind that postponement will entail carrying cost to the consumers as also cash flow problems for the licensee. National Tariff Policy also requires that "uncontrollable costs *should be recovered speedily to ensure that future consumers are not burdened with past costs………" (Clause 5.3(h)(4) extracted in para 15.*

12. We consider that it is necessary for the Commission to expeditiously carry out the truing up exercise both for controllable and uncontrollable items as soon as the audited data as per actuals is available and give effect to the approved gains/losses to be passed through tariff following the Annual Performance Review as stipulated in clause 12.1(b) of the MYT Regulations. This exercise need not wait for the next control period. We decide accordingly and direct the State Commission to undertake the truing up at the earliest once the actual audited data is available".

52. The question whether the Commission committed illegality in computing the wheeling charges

We are to note again the observations of this Tribunal in appeal No. 68 of 2009 wherein this point has been considered and settled at rest.

27. Gravamen of pleas of the Appellant is that whereas the GERC (Open Access in Intrastate Transmission and Distribution) Regulations require levying of wheeling charges in terms of capacity to be reserved in MW the Commission has determined the wheeling charges in terms of paise per unit. Here it is necessary to set out the Regulation 14(i) of the GERC Regulations:

(i) Transmission/Distribution (Wheeling) Charges.

The charges for use of the system of the licensee for intra-state transmission or distribution except intervening transmission facilities shall be regulated as under, namely:

(i) The annual charges shall be determined by the Commission in accordance with the terms and

conditions of tariff notified by the Commission from time to time and after deducting the adjustable revenue from the short-term users, these charges shall be shared by the long-term users;

(ii) (a) The charges payable by a short-term users shall be calculated in accordance with the following methodology:

ST RATE= 0.25X(TSC/Av CAP)/365 Where

ST RATE is the rate for short-term open access user in Rs. Per MW per day.

"TSC" means the Annual Transmission/Distribution Charges of the transmission or distribution licensee for the previous financial year determined by the Commission.

"Av CAP" means the average capacity in MW served by the system.

28. The Appellant had also pleaded that in case the capacity is not utilized and payment is made in terms of units transmitted, the transmission/distribution line will not be utilized and there will be under-recovery which will have to be compensated by other consumers which is not the intention of Section 42(2)(3) of The Act which provides for non-discriminatory open access but not any preferential tariff or treatment at the cost of other retail consumers. In view of the Commission's own Regulations requiring wheeling charges payable on the basis of capacity reserved and not on the basis of paise per unit, we are inclined to agree with the contention of the Appellant. We order accordingly.

29. We are unable to agree with the contention of the State Commission that the capacity in terms of MW at HT and LT was not available as the same has been given at Clause 1.48 of the tariff petition of the Appellant as submitted by Ms Chauhan as under:

clause 1.48: " The system peak demand of TPL-D for the year FY 2008-09 is 1494 MW. The contract demand for all the HT consumers is about 444 MW. Assuming that total contact demand of HT contributes to the system peak demand, the total demand of LT contributing to the system peak is computed as 1050 MW. The ratio of HT and LT voltage contribution to the peak i.e. 30:70."

30. We are inclined to agree with the contention of the Appellant that the apportionment charges need to be reviewed to take into account the fact that the consumers at LT level also utilize the HT system whereas HT consumers do not use the LT system.

31. In view of the foregoing we direct the State Commission to re-determine the open access charges in terms of the capacity reserved as per its own Regulations as also review the apportionment of wheeling charges with respect of HT and LT system."

53. On the last question whether the Commission committed discriminatory treatment in respect of renewable energy purchase obligation. This Tribunal in appeal No. 68 of 2009 held as follows:

37. Main grievance of the Appellant is that, for the year 2008-09, whereas the Regulations provide 2% as minimum quantum of purchase from renewable sources, the State Commission has added the backlog for the years 2006-07 and 2007-08 by relying on Regulation 3.2 of the power procurement from renewable sources regulations. We note that Clause 3.2 of the Notification (supra) stipulates that if due to increased sale of power in the current year from that of the previous year, there may be shortfall of the targeted quantum from the quantum that would arise from the increased sale, such amount resulted due to increased *sale would be added to the targeted quantum of Renewable Purchase Obligation for the next year. However, in this Appeal it is not the case. The Appellant has not been able to fulfill its obligations for the years 2006-07 and 2007-08 despite efforts made by it by inviting expression of interest from the renewable generators. This backlog of 2006-07 and 2007-08 cannot be added to the year 2008-09 as per Regulation 3.2 because the short fall has not been caused due to increased sales in the area of the licensee. We direct that the State Commission may review the targets for the years 2008-09, 2009-10 and 2010-11 depending upon the availability of the power from renewable sources".*

54. In the result, it is found necessary for the Commission to re-examine the following issues in respect of which we have differed with it on the basis of materials and in the

light of the principles discussed in the aforesaid paragraphs of the judgment and then pass a reasoned order on hearing the parties;

a) Passing of one-third of the gains to the appellant in the light of Regulations 11 and 12 of the MYT Regulations, 2007

b) Interest on working capital

c) Eligibility of incentives for the FY 2008-09.

d) Consideration of TPL-D (Ahmedabad) receivables instead of deducting receivable of TPL-G ARR in calculation of working capital requirements.

e) Treatment of applicability of the tax rate for the TPL-G

f) Allowance of income-tax to earn return on equity as post tax

g) Classification of cost items as controllable and uncontrollable.

h) Computation of wheeling charges

i) Treatment on renewal purchase obligation (RPO) Item Nos. (d to h) shall be given appropriate treatment in the light of the decision of this Tribunal in case of Reliance Infrastructures Ltd. Vs MERC 2009 ELR (APTEL) 672. and the decision dated 23rd March, 2010 passed in appeal No. 68 of 2009 as also the decision dated 5th January, 2011 passed in RP No. 09 of 2010 in connection with appeal No. 68 of 2009.

55. We, therefore, allow the appeal and set aside the impugned order remitting the case back to the Commission on the points indicated in the preceding paragraph without however any order

as to cost. The Commission shall pass a reasonable order upon hearing the parties.

(Justice P.S.Datta)
Judicial Member

(Mr. Rakesh Nath)
Technical member

<u>Dated 9th May, 2011</u>

<u>Index: Reportable/Non-Reportable</u>

<u>PK</u>