Before the Appellate Tribunal for Electricity
(Appellate Jurisdiction)

Appeal No. 100 of 2007 and IA No. 122 of 2007

Dated: December 4, 2007.

Present: - Hon'ble Shri H.L. Bajaj, Technical Member
Hon'ble Mrs. Justice Manju Goel, Judicial Member

Karnataka Power Transmission Corporation Ltd.
Kavery Bhawan, K.G. Road
Bangalore-560009 .....Appellant

Versus

1. Karnataka Electricity Regulatory Commission
   6th & 7th floors, Mahalakshmi Chambers
   9/2, M.G. Road, Bangalore

2. Bangalore Electricity Supply Co. Ltd.
   K.R. Circle, Bangalore-560001

3. Hubli Electricity Supply Company Ltd.
   P.B.Road, Nava Nagar Hubli
   Karnataka

4. Mangalore Electricity Supply Co. Ltd.
   Paradigm Plaza, Mangalore, Karnataka

5. Gulbarga Electricity Supply Co. Ltd.
   Station Road, Gulbarga, Karnataka-585102

6. Chamjundeshwari Electricity Supply Co. Ltd.
   927, L.J.Avenue, Saraswatipuram, Mysore
   Karnataka

7. Coordinator, Consumer Care Society
   1939, 27th Cross, Banashankari 2nd stage
   Bangalore

8. Convenor, Bharathiya Kissan Sangha & Malnadu
   Niravari Consumers Federation,
   Sirsi, Karnataka

9. R.K. Rangrej, Chairman, Electricity Sub Committee,
   Gadag Dist. Chamber of Commerce and Industry
   APMC Road, GADAG

10. Secretary, FKCCI
    K.G.Road, Bangalore-560009

11. Bangalore Watersupply and Sewage Board
    Kavery Bhawan, Bangalore

12. Y.G. Muralidharan, Consumer Advocate
    Karnataka Electricity Regulatory Commission
    M.G.Road, Bangalore

13. General Secretary
    KASSIA, Vijayanagar
    Bangalore ....Respondents

Counsel for appellants: Mr. M.G.Ramachandran,Advocate
Mr. Anand K. Ganesan and
Ms Swapna Seshadri, Advocates
Mr. V.Hiremath, Director (Law)

Counsel for respondents: Mr. Apoorva Misra, Advocate,
For Resp.No.1 KERC
Mr. Rohit Rao N.Advocate for
Resp.No. 10, FKCCI.
Mr. Amit Kapur, Advocate
Mr. Alok Shankar, Adv.for Resp.I
Mr. Avijeet Lala, Adv.
Mr. Sunil Kumar for KERC
Mr. S.S.Patil, President and
Mr.M.G.Prabhakar, Member,
Energy Committee, FKCCI
Mr. Mansoor Ali Shoket, Advocate
Mr. Kunal Rajpal for KERC
Mr. Somiran Sharma for FKCCI
Mr. Rajnish Ranjan for KERC
Ms Poonam Verma, Advocate
Ms Minu Rani Adv.for Resp.I

Judgment

Per Hon'ble Mr. H.L. Bajaj, Technical Member

This appeal filed by Karnataka Power Transmission Limited (in short KPTCL) is directed against the tariff order dated July 6, 2007 passed by the Karnataka Electricity Regulatory Commission (in short KERC or the Commission) vide which it decided on the revenue requirements and the Multi Year Tariffs for KPTCL for the tariff period 2007-08, 2008-09 and 2009-10.

2. The facts of the case are briefly stated below:

3. Earlier KPTCL was both the transmission licensee and bulk supply licensee entrusted to carry out the transmission and bulk supply business in the state of Karnataka and this position continued till June 10, 2005. Effective June 10, 2005 the bulk supply business of KPTCL has been divested from KPTCL with the Power Purchase Agreements which KPTCL had with generating companies being assigned and vested in the distribution companies. Accordingly, for the tariff period 2005-06 onwards including for the multi year tariff period of 2007-08 to2009-10 decided by the impugned order, KPTCL is a transmission licensee and revenue requirements and tariff for KPTCL has to be decided in its capacity as a transmission licensee only.

4. On November 30,2006 KPTCL filed the petition for determination of its revenue requirements and tariff for the tariff period 2007-08, 2008-09 and 2009-10 (three years)

under the Multi Year Tariff regulations of the Commission. In the tariff petition KPTCL, besides claiming the projected revenue requirement during the above tariff period of three years, also claimed the following:

I. Effect to be given to the order dated October 19,2006 passed by the Tribunal in appeal No. 107 of 2006 in the earlier case of KPTCL, whereby the Tribunal had set aside the order of the Commission on the disallowance of part of the power purchase cost paid/payable by KPTCL to M/s. Tanir Bhavi Power Corporation Ltd. (hereinafter called Tanir Bhavi). In the said order this Tribunal had held that the entire power purchase cost at US dollar 0.04 (namely 4 cents) should be allowed to KPTCL in the tariff as per the award given by the Arbitration Tribunal of three former Hon'ble justices of the Supreme Court of India and the power purchase cost to be allowed should not be restricted to US $ 0.0209 as decided and allowed

by the Commission during the tariff period 2000-01 onwards.

II. Effect to be given to the principles laid down in another order dated August 29, 2006 passed in appeal No. 84 of 2006 in the case of KPTCL relating to the tariff year 2006-07, wherein this Tribunal had held that the Commission should ordinarily allow the investment as proposed by the KPTCL, which KPTCL as the utility is in a better position to judge and the Commission can always apply the prudence check on the investments made at appropriate stage and adjust the equities.

5. In the impugned order, besides deciding on various aspects of the revenue requirements proposed by the KPTCL for the tariff period 2007-08 to 2009-10, the Commission has undertaken the truing up of the financials of KPTCL for the earlier periods 2000-01 to 2005-06 and as a result of such truing up the Commission has held that KPTCL has had surplus revenues during the above period which needs to be adjusted in favour of the consumers. Against such surpluses

found by the Commission an amount of Rs.545.87 crores has been adjusted for the claims of KPTCL on account of additional power purchased from Tanir Bhavi for the period 2000-01 to 2004-05 as directed in the order dated October 19, 2006 of this Tribunal. After such adjustment a sum of Rs. 37.28 crores is found to be deficit to be allowed in favour of KPTCL as pass through in the future tariffs. The Commission has allowed this amount of Rs. 37.28 crores as pass through together with a carrying cost @ 12% per annum in the tariffs for the period 2007-08 to 2009-10. Thus the Commission has held that the entire power purchase cost to KPTCL on account of Tanir Bhavi for the period up to 2004-05 which was not allowed earlier by the Commission stands allowed and adjusted in the above truing up exercise undertaken by the Commission.

6. In the impugned order the Commission has also directed KPTCL to remit Rs. 620.58 crores found as surplus in the hands of KPTCL in the tariff year 2005-06 as a result of the savings in the power purchase cost to KPTCL by reason

of good hydro thermal mix during the above year to the distributing companies. The Government of Karnataka had, however, initially issued orders and finally a policy directive under section 108 of The Electricity Act, 2003 whereunder the said amount of Rs. 620.58 crores has been appropriated by the Government of Karnataka to its benefit and, therefore, the said amount was not available to KPTCL or to the distribution companies to which it was to be remitted as per the directions of the Commission.

7. In the present appeal KPTCL has challenged the order of the Commission on the following specific aspects:

A. The legality of the action of the Commission undertaking truing up of the revenue requirements and revenues from the tariff of KPTCL for the tariff period 2000-01 to 2005-06 for the second time and finding revenue surpluses on the sale of energy of Rs. 834.87 crores as against the revenue deficit of Rs. 479.9 crores found in the earlier truing up undertaken on year on year basis based on

actual/audited accounts after the close of the relevant period;

B. Merit of the finding of the Commission that there were surpluses in the revenue of KPTCL in the previous years by assuming that the power purchases made by KPTCL during the period 2000-01 to 2004-05 to meet the actual distribution losses in excess of the loss levels approved by the Commission shall be notionally available for sale to consumers and, therefore, the sales revenues therefrom should be taken as revenues;

C. The failure of the Commission to allow in the tariff, the interest and finance charges on investments proposed as claimed by KPTCL during the tariff period 2007-08 to 2009-10 on the ground that such interest and finance charges shall be allowed only after the investments made are capitalized and the assets are put into use;

D. The failure of the Commission to implement the order dated August 29, 2006 passed by this

Tribunal in appeal 84 of 2006 and the order dated October 19, 2006 passed by this Tribunal in appeal No. 107 of 2006.

E. Direction given by the Commission to KPTCL to remit Rs. 620.58 crores to distribution companies despite the directive of the state Government under Section 108 of The Electricity Act, 2003 appropriating the said amount as its revenues;

F. The Commission not undertaking truing up relating to the tariff year 2006-07 in the absence of audited accounts though provisional accounts were made available;

G. The Commission not allowing the interest and finance charges for the year 2006-07 of Rs. 220.23 crores being interest on the belated power purchase payments made by KPTCL.

8. On the above challenge of the KPTCL the following issues arise for consideration of the Tribunal:

A. Whether the Commission was right in undertaking afresh the truing up of the financials of the KPTCL for the tariff years 2000-01 to 2005-06 by the impugned order while considering the multi year tariff for the period 2007-08 to 2009-10 after having carried out the truing up earlier based on actuals?

B. Whether the Commission was right in determining the surplus revenues for KPTCL in the second truing up undertaken by the Commission for the tariff years 2000-01 to 2004-05 when no such revenue surplus was found in the earlier truing up undertaken by the Commission?

C. Whether the Commission was right in implementing the principles contained in the order dated August 29, 2006 passed in appeal No. 84 of 2006 by the Tribunal in regard to investments by KPTCL on transmission system and interest and finance charges in regard to such investments?

D. Whether the Commission has implemented the order dated October 19, 2006 passed by the Tribunal in

appeal No. 107 of 2006 on the amount to be allowed for the purchase cost of power from Tanir Bhavi as US 4 cents during the tariff years 2000-01 to 2004-05?

E. Whether the Commission was right in directing KPTCL to remit Rs. 620.58 crores from its revenues to the distribution companies when the state Government had appropriated the amount under a policy directive issued under Section 108 of The Electricity Act, 2003?

F. Whether the Commission was right in not undertaking truing up relating to the tariff year 2006-07 in the absence of audited accounts though provisional accounts were made available?

G. Whether the Commission was right in not allowing the interest and finance charges for the year 2006-07 of Rs. 220.23 crores being interest liability on the belated power purchase payments made by KPTCL?

9. We now proceed to examine the issues framed above.

Issues A, B and D Truing up of the financials of 2000-01 to 2005-06 and Tanir Bhavi Additional Power Purchase Cost.

10. Mr. M.G. Ramachandran, learned counsel for the appellant contended that the truing up of the Revenue Requirements and revenues of KPTCL undertaken by the Commission for tariff period 2000-01 to 2005-06 is for the second time after the Commission had already undertaken such truing up exercise in the past for each of the above tariff years at the time of considering the petition of KPTCL for revenue requirements and tariff for the succeeding year(s) and that the second truing was totally unwarranted and not justified and that the Commission cannot undertake such second truing up after a lapse of many years. He submitted that such second truing up was done without any petition for review of the earlier orders under Section 94 of The Electricity Act, 2003 and in any event such review based on any petition or otherwise even on suo moto action by the Commission had

become long time barred. He said that the second truing up has been done by the Commission unilaterally without initiating proper proceeding and without giving any opportunity of hearing to KPTCL to represent its case.

11. Learned counsel submitted that in the impugned order the Commission has observed as under as the basis for undertaking the second truing up (para 5.1 internal page 39 of the impugned order and pave 118 of the paper book).

> *" The Commission after its constitution in November 1999, has issued the following seven tariff orders till date wherein it has approved ERCs and determined tariffs of KPTCL/ESCOMs for the ensuing years.*
>
> *a) Tariff order 2000 dated December 18, 2000*
>
> *b) Tariff Order 2002 dated May 8, 2002*
>
> *c) Tariff Order 2003 dated March 10, 2003*
>
> *d) Tariff Amendment order dated December 15, 2003*
>
> *e) Tariff Order 2005 dated September 27, 2005*
>
> *f) Tariff Order 2006 dated April 7, 2006*
>
> *g) Tariff Order 2006 dated October16, 2006*
>
> *In the tariff review process in each of the above orders, the Commission has discussed the performance of the licensee, with respect*

to the Commission's approved figures vis-à-vis the actual as per provision/audited accounts under the chapter titled 'FY- in Retrospect'. However, the Commission had not carried forward any deficit/surplus of the respective year to the ensuing year except in Fy05 for KPTCL.

12. Learned counsel referring to the affidavit filed on behalf of the Commission before the Tribunal on August 14, 2007 as to the truing up, submitted that it has been stated as under:

(a) *During the financial years 2001-2006, ARR/ERC filing of the utilities was considered in the public hearing and the tariff approved based thereon for the ensuing financial year.*

(b) The actuals of the expenditure incurred and the revenue realized in the previous financial years as reflected in the annual accounts of the utilities was duly considered to arrive the revenue gap or revenue surplus in the previous year and reflected in an extracted/tabulated statement showing true up statement.

(c) However, the consequence of the true-up for the previous year (whether resulting in a surplus or shortfall) was not carried forward and given effect to in the ensuing year's tariff.

(d) As such, the action by the Commission to take the net effect of actual annual shortfall(s) and surplus(s) during financial year 2001 to financial year 2006-07 is not a case of double counting or reopening true-up accounts".

13. Learned counsel further submitted that in the impugned order another reason for the second truing up given by the

Commission is as under (internal page 43 of the impugned order and page 122 of the paper book):

> *It is further noted that Section 61 (f) of the Act and clause 5.0 of the National Tariff Policy required the state Commissions to be guided inter-alia by Multi-Year Tariff (MYT) principles. The Commission is of the view that an MYT framework is an incentive based regime where in the performance of the licensee is monitored against the Commission's approved targets thereby incentivising better performance and penalizing under performance.*
>
> *In this backdrop, the Commission is of the view that it is appropriate to review the past performance of the licensee which eventually should facilitate the Commission in fixing realistic targets instead of desired targets. Therefore, the Commission in this tariff order, has reviewed the past performance of the licensee and also trued up the cost parameters based on actuals. Hence, truing up the cost based on actual would support the*

Commission in fixing realistic targets for the control period.

14. Learned counsel for the appellant contended that in the above context the truing up was intended and can be only for the purposes mentioned above namely either:

(i) for giving effect to the consequences of the deficit or surplus already found by the Commission during the first true up; or

(ii) finding the base for the Multi Year Tariff for the years 2007-08 to 2009-10 and it cannot be used to correct the past years revenues.

15. He argued that on its own reasoning the Commission could give only consequential effect to the finding already reached in the first truing up undertaken by the Commission earlier and the Commission was not entitled to find new surpluses in the revenues. The Commission had in the earlier truing up found for the tariff years 2000-01 to 2003-04 an aggregate deficit of Rs. 479.90 crores as under:

Year	Amount of deficit/ surplus
2000-01	- 601.01
2001-02	- 22.31
2002-03	+ 49.45
2003-04	+ 93.97
Aggregate	- 479.9 (minus)

16. He contended that in the second truing up the Commission has, however, found sufficient surplus in the revenues of KPTCL to wipe out not only the above deficit of Rs. 479.9 crores but also adjust an amount of Rs. 545.87 crores which the Tribunal had directed to be allowed on account of difference in the power purchase cost paid to Tanir Bhavi by KPTCL but not allowed earlier by the Commission in relation to the tariff years 2000-01 to 2003-04. Thus the second truing up is not for giving consequential effect to the deficit/surpluses already found in the first truing up and the second truing up has been undertaken to re determine the

surpluses/deficits for the above years afresh, contrary to the reasons given for such truing up.

17. As regards another reason given for truing up namely: to determine the base for Multi Year Tariff he submitted that the truing up exercise undertaken has not been used in any manner whatsoever for determining any base for multi year framework. The second truing up has, therefore, been undertaken by the Commission for extraneous and colourable purpose of depriving the KPTCL the legitimate claims of KPTCL based on the implementation of the order dated October 10,2006 passed by the Tribunal in appeal No. 107 of 2006 relating to power purchase cost paid to Tanir Bhavi when the Tribunal had corrected the order of the Commission of consistently taking the position that the full power purchase cost shall not be allowed as a pass through even after the award given by an Arbitral Tribunal of three former justices of the Hon'ble Supreme Court.

18. Mr. Ramachandran contended that the second truing up undertaken is without any direction by this Tribunal that such truing up be undertaken to implement the directions contained in the earlier order dated October 10, 2006 passed in appeal No. 107 of 2006.

19. Mr. Ramachandran contended that on merits also the truing up undertaken, the calculations and adjustments made are perverse and arbitrary and not sustainable. The Commission had calculated additional sales revenue for each of the above years by readjusting the quantum of power purchases ,losses to be accounted for and consequent sales revenue ignoring the basic fact that the additional quantum of power purchased by KPTCL to meet the distribution losses disallowed but actually in existence cannot be counted as the power available for sale to consumers and, therefore, there cannot be any deemed sales revenue of such power. As an example he cited that the KPTCL had projected in the tariff year 2000-01 the distribution loss level of 35.50% but the Commission had approved the loss level only of 31%

(Table 5.1 of the impugned order at internal page 48). Thus for every 100 units purchased by KPTCL for sale of energy to consumers the Commission will take into account 69 units as available for sale to consumers and therefore revenue from the sale of power was projected at the time of approval of the revenue requirements on the above 69%. However, as the actual loss level was 35.50% in addition to purchasing 100 units the KPTCL was required to purchase additional 6 to 7 units (total of about 106 or 107 units) at its own cost and without any tariff being allowed for the same so that KPTCL is left with 69 units for supply to consumers. He contended that KPTCL has thus already incurred the disincentive or deficit of purchasing additional units and that in the earlier truing up this position was accepted and KPTCL was not allowed the additional power purchase cost for procuring the additional power to meet the additional losses and that KPTCL also did not claim such additional power purchase costs in the earlier truing up and that in the impugned order the Commission on its own without any claim from KPTCL allowed the additional power purchase cost on such

additional units to meet the increased loss level but at the same time took into account that such additional power procured is available for notional sale and, therefore, assumed additional sales revenue and that this has resulted in double accounting against KPTCL and notional additional revenues in the hands of KPTCL.

20. Mr. Ramachandran contended that the Commission has assumed such additional sales revenue on notional basis in the above years as under:

Year	**Amount of additional sales revenue/deficit assumed (In crores)**	**Reference**
2000-01	247.63	Table 5.1 page 127
2001-02	333.08	Table 5.3 page 135
2002-03	254.16	Table 5.5 page 143
2003-04	(96.64)	Table 5.7 page 151
Aggregate additional revenue	738.23	

21. Learned counsel contended that even the amount of Rs. 96.64 crores surplus for the year 2003-04 was on account of efficiency gain for achieving more loss reduction and should not therefore be deducted and that the additional revenue wrongly assumed by the Commission is, therefore, the aggregate for three years from 2000-01 to 2002-03 of Rs. 834.87 crores. He asserted that Commission has, therefore, undertaken a purported truing up and determined additional sales revenue of Rs. 834.87 crores afresh (as against deficit of Rs.479 crores under the earlier true up) and this was not giving only a consequent effect for earlier surplus/deficit determined as sought to be submitted by the Commission.

22. Mr. Ramachandran contended that as against the above additional revenue assumed of Rs. 834.87 crores the additional power purchase cost allowed was Rs. 322 crores only and the difference of about Rs. 512.87 crores has assumed as surplus with KPTCL during the previous years on account of the above aspect. He said that with reference to the tables in the impugned order the Commission has

proceeded to apply the Commission approved loss level to actual power purchase quantum ignoring that the actual quantum of power purchase include such quantum which KPTCL need to purchase at its own cost without any burden to the consumers to meet the difference between the Commission approved loss level and the actual loss level.

23. He submitted that if the truing up had been undertaken in proper manner after due opportunity to KPTCL, the above would have been pointed out and in fact KPTCL could have legitimately claimed for the above years 2000-01 to 2005-06 that it should be allowed to carry forward a sum of Rs. 479.9 crores in addition to Rs. 545.87 crores with carrying cost to be adjusted for Tanir Bhavi power purchase cost. He asserted that KPTCL will be further entitled to carrying cost on the above amount of Rs. 479.9 crores and that accordingly, instead of adjustment of the power purchase costs of Tanir Bhavi in the table 5.14 at page 184 the amount to be allowed to KPTCL as pass through in the tariff for the years 2007-08 onwards would be as under:

Rs. In crores

Aggregate deficit to be allowed for the past year	479.9
Amount to be allowed for Tanir Bhavi Power Purchase cost	545.87
Total principal sum to be allowed as pass through in KPTCL tariff	1025.77

24. He contended that in addition KPTCL is entitled to carrying cost/interest at 12% on the above amounts from the respective years when they were due.

25. Responding to the contentions of the appellant, Mr. Amit Kapur, learned counsel for the Commission and Mr. Rohit Rao N. on behalf of FKCCI submitted that the Commission was required to undertake such truing up for the past years in view of the specific observations made and directions given by the Tribunal in Appeal Nos. 74, 75 and 76 of 2006; 77, 78 and 79 of 2006; Appeal No. 41 of 2005. Relating to utilities in other states in the larger interest of the consumers as it cannot allow KPTCL to keep back surpluses and that the Commission had duly allowed the extra power

purchase cost incurred by the KPTCL on the purchase of additional power and, therefore, the Commission was right in taking into account such additional power purchases for determining the additional sales revenue after duly applying the merit order and marginal cost calculation principles and that the Commission applied the loss level approved by the Commission even on the additional power purchases made by KPTCL for meeting the actual losses in excess of the level approved by the Commission to ensure that the KPTCL as a licensee function efficiently and with the approved loss level.

26. On behalf of the Commission and FKCCI Mr. Kapur submitted that insofar as the implementation of the order passed by the Tribunal in Appeal No. 107 of 2006 dated 19.10.2006 pertaining to the additional power purchase cost paid by KPTCL to Tanir Bhavi is concerned, the additional power purchase cost now taken into account by the Commission is inclusive of such additional power purchase costs payable to Tanir Bhavi and, therefore, the same stands allowed. He further submitted that KPTCL has not shown as

to how it had, in the past, met the Tanir Bhavi additional power purchase cost. He submitted that the Government of Karnataka has denied that such additional cost was paid through any subsidy from the Government and, therefore, it is certain that such additional power purchase costs have been paid by KPTCL from its revenues. He also submitted that KPTCL also delayed taking steps for creation of regulatory assets in terms of the directions given by the Tribunal in Appeal No. 107 of 2006.

27. Per contra, Mr. M.G. Ramachandran contended that the additional power purchase was met by KPTCL out of its resources including revenue subsidy given by the Government and not out of tariff previously allowed by the Commission or committed subsidy for tariff given by the State Government. He submitted that the Commission is wrong in accusing KPTCL for delaying the creation of regulatory asset as the Regulatory asset is to be considered only after deciding on the impact of allowing the cost in the tariff and only in the event there is significant tariff shock. He contended that the

question of regulatory asset will not arise till the decision of the Commission on the tariff increase to be allowed as a pass through and whether the same would create substantial tariff shock and that in any event the distribution companies have given the proposal for adjustment of the Tanir Bhavi additional purchase cost in three years time. He further contended that the Commission's assumption of notional additional revenue on the power procured for meeting the difference in the loss level approved by the Commission and actual loss level is misconceived and without any basis.

Analysis and decision:

28. We have heard contentions of the rival parties. Basic issue that has to be decided is: whether or not the Commission was correct in carrying out the truing up of revenue requirements and revenues of KPTCL for the tariff period 2000-01 to 2005-06. Invariably, the projections at the beginning of the year and actual expenditure and revenue received differ due to one reason or the other. Therefore, truing up is necessary. Truing up can be taken up in two

stages: Once when the provisional financial results for the year are compiled and subsequently after the audited accounts are available. The impact of truing up exercises must be reflected in the tariff calculations for the following year. As an example; truing up for the year 2006-07 has to be completed during 2007-08 and the impact thereof has to be taken into account for tariff calculations for the year 2007-08 or/and 2008-09 depending upon the time when truing up is taken up. If any surplus revenue has been realized during the year 2006-07, it must be adjusted as available amount in the Annual Revenue Requirement for the year 2007-08 or/and 2008-09. It is not desirable to delay the truing up exercise for several years and then spring a surprise for the licensee and the consumers by giving effect to the truing up for the past several years. Having said that, truing up, per se, cannot be faulted, and, therefore, we do not want to interfere with the decision of the Commission in this regard to cleans up accounts, though belatedly, of the past. It is made clear that truing up stage is not an opportunity for the Commission to rethink de novo on the basic principles,

premises and issues involved in the initial projections of revenue requirements of the licensee. We had occasion to deal with a similar situation in NDPL vs DERC, appeal No. 265 of 2006. The relevant part of our judgment in that appeal is reproduced below:-

> *"47. Second Truing up. Second truing up has been done on three scores namely employee expenses, depreciation and interest. It is contended by the Appellant that the second truing up is warranted only when there is difference between provisional accounts on the basis of which the first truing up is done and audited accounts which may, have been furnished after such truing up. In the present case admittedly there has not been any substantial change between the provisional accounts and the audited accounts. On all the three scores the Commission has done the second truing up on the basis of a revised policy e.g. on the count of depreciation it says that no depreciation should have been allowed on assets created by APDRP grant. Since the accounts were already before the Commission if it was not to grant any depreciation on the assets created out of APDRP grant the same should have reflected in the Tariff Order of the appropriate year. After the Tariff Order based on those*

accounts, namely for the Financial Year 2004-05, there is no occasion for the Commission to now introduce a new philosophy and approach for such assets acquired out of APDRP fund. It may further be said here that there is no rationale for declining to allow depreciation for assets acquired out of the APDRP grant because depreciation is a source of funding required for replacement of assets. Therefore, unless the Commission is able to say that APDRP grant will be available every year and there is no need to create funds for replacement of such assets, it cannot say that no depreciation on such asset may be given. Similarly, coming to the question of employees cost the Commission says, that other costs and allowance which were being paid to the existing employees had nothing to do with VSS scheme and, therefore, Commission decided to de-link other costs and allowances from the normative employee cost allowed by the Commission. This is again rethinking on the subject of employee cost. The previous years account cannot be trued up on such rethinking. The appellant on the other hand says that such allowances and costs could not have been de-linked as those who availed of VSS would have been paid these allowances had they continued in the employment.

48. Similarly, so far as interest is concerned the second truing up is not based on difference between the audited

account and the provisional account and, therefore, could not have been done by the Commission. The Commission has no alternative but to allow all these expenses in the next truing up mechanism.

29. It is noted that the Commission had been carrying out the truing up exercises on year to year basis but had not given effect to the results of such exercises during all these years. Once the truing up exercise has been carried out, the Commission is not permitted to again take up the truing up exercise based on new assumptions.

30. It has been brought to our notice that whereas the Commission, in the first truing up exercise, had found a deficit of Rs. 479.9 crores, second truing up exercise by the Commission has resulted in sufficient surplus in the revenues of KPTCL to not only wipe out the deficit of Rs. 479.9 crores but also adjust an amount of Rs. 545.87 crores which this Tribunal had directed to allow on account of difference in power purchase cost paid to Tanir Bhavi. The main reason for this disparity, it has been contended by the

appellant, is on account of treatment of Transmission and Distribution losses.

31. We now advert to the T&D losses. The Commission is expected to fix the T&D loss targets in consultation with the licensee. Once the target for loss level is fixed, the licensee is expected to make all efforts to achieve the loss level. The consumers should not be made to bear the brunt of losses over and above the fixed target. In the case in hand, during one year, a loss level of 31% is fixed by the Commission. The cost of 100 units purchased and 69 units (100-31) sold should be considered in the ARR. However, KPTCL could achieve only 35.5% loss level which means that units required to be purchased will be about 107 so that 69 units are available for sale to the consumers. Whereas the Commission has allowed the cost of procurement of power of about 107 units, simultaneously by applying a loss level of 31% to 107 units, it has also assumed that there will be sale of about 5 units over and above the 69 units. This results in recovering from the licensee for the electricity which has not

actually been sold because of losses being 35.5% (actuals) against the set target of 31%. The additional imaginary sale of power assumed by the Commission is irrational, unreasonable as this electricity has not even reached the consumer end.

32. We need to balance the interest of the consumer and the licensee by ensuring that the licensee tries his best to achieve the said targets and is deterred to under achieve loss reduction. In the present case to sell 69 units KPTCL will be allowed purchase cost of 100 unit only as per the target of 31% set by the Commission and the licensee will have to pay for the power required over and above 100 units so that 69 units are sold to consumers. We decide that this deterrent of disallowing cost of electricity required over and above 100 units is sufficient and it will not be correct to assume an imaginary sale of electricity when the actual loss level is 35.5% and when the licensee has already been penalized by not allowing it the cost of power procurement over and above 100 units. This will ensure that the licensee functions

efficiently. Interest of consumers is not prejudiced because licensee is being allowed only purchase cost of power as per the loss level target set by the Commission.

The question before us is how much of power can be deemed to have been sold and what amount should be taken as the revenue from the sale of power. The Commission cannot be allowed to assess the revenue of the licensee on the imaginary sale of power as indicated above. The licensee has borne the burden of extra purchase of power for meeting the T&D loss over and above the target. The revenue of the licensee can be assessed only on the basis of actual sale. We, accordingly, uphold the objection of the appellant on this aspect and allow the appeal in respect of issues A&B.

Concedingly, the Commission has taken into account the additional power purchase cost payable to Tanir Bhavi as allowed by this Tribunal in appeal No. 107 of 2006. We direct that this element of additional cost may be succinctly reflected by the Commission while implementing this order.

Issue C Disallowance of Interest and Finance Charges

33. Mr. M.G. Ramachandran, learned counsel appearing for the appellant contended that KPTCL had claimed, in the revenue requirements for the tariff period 2007-08 to 2009-10, Interest and Finance Charges mainly relating to the funding of the Investments proposed in the Transmission Systems of KPTCL as under (as stated in table 6.1 of the impugned order):

2007-08	Rs. 495.85 crores
2008-09	Rs. 617.14 crores
2009-10	Rs. 757.26 crores

He submitted that the Commission has rejected the above claim for the interest and finance charges only on the ground that in terms of the order dated August 29, 2006 passed by this Tribunal in Appeal No. 84 of 2006, the Interest and Finance Charges related to investment in transmission system proposed cannot be allowed till the investment is capitalized. He contended that this is a complete misreading

of the order dated August 29, 2006 passed by the Tribunal by picking and choosing to read few lines of the order here and there out of the context. He asserted that the Tribunal did not hold that interest and finance charges are not to be allowed to a licensee till capitalization of the assets; and that this is contrary to the well established practice followed in the case of electricity licensees for the past several decades both in case of licensees under The Indian Electricity Act, 1910, to whom Sixth Schedule to The Electricity (Supply Act, 1948 applies and also in the case of Electricity Boards governed by section 59 of The Electricity (Supply) Act, 1948 and adopts the same principle as laid down Electricity (Supply) Act, 1948 in the above Sixth Schedule; and is also contrary to what the Commission had consistently followed hithertofore in the case of KPTCL; and contrary to what each of the other State Regulatory Commissions had consistently adopted; and contrary to the basic feature of tariff determination of electricity licensees thus seriously affecting the required cash flow to meet the investment requirements and thus affecting the proper maintenance of the system and at the same time

increasing the cost to the consumers substantially by adding, in future, the Interest During Construction (IDC) and higher return on equity and interest costs; and that this approach of the Commission is defeating the very purpose and objective of the principles laid down by the Tribunal in the order dated August 29, 2006.

34. He submitted that by adopting the above process, the Commission has placed KPTCL in much worst position as compared to what KPTCL was before the order dated August 29, 2006 passed by the Tribunal in Appeal No. 84 of 2006. KPTCL was being allowed Interest and Finance Charges and other charges by the Commission on the proposed investments before capitalization (namely as and when incurred and that the Commission did not however, recognize the entire quantum of investment proposed. He said that KPTCL was aggrieved by the extent to which the same was not allowed by the Commission. He contended that the Tribunal had held that the Commission should not doubt the extent of investment proposed by KPTCL and that if there is

any variation, the same can be addressed later through prudent check and that the Appeal No. 84 of 2006 filed by KPTCL was allowed by the Tribunal and that KPTCL had succeeded in its challenge to the order passed by Commission. He contended that the Commission has used the order of the Tribunal to further prejudice KPTCL instead of correcting the errors in its earlier orders and give relief to KPTCL.

35. On the otherhand, Mr. Kapur responded that the Commission had understood the order of the Tribunal in Appeal No. 84 of 2006 as holding that Interest and Finance Charges are not be allowed till the investment is complete and the assets are capitalized and that the Commission has only followed the order as was understood by the Commission and if the Tribunal's Order has any other interpretation or implications, the same be clarified by the Tribunal.

36. Mr. M.G. Ramachandran, learned counsel submitted that the Commission has not given effect to the earlier decisions of the Tribunal in Appeal No. 84 of 2006 and

Appeal No.107 of 2006 namely in regard to interest and finance charges and in regard to additional power purchase costs and that thereby KPTCL has been deprived of substantial revenues.

37. Mr. Kapur contended that Tanir Bhavi additional costs dealt in Appeal No. 107 of 2006 have been allowed and that as regard Appeal No. 84 of 2006, the Commission has implemented the order of the Tribunal as per the directions contained in the order.

Analysis and decision:

38. Gravamen of the appellant is that it has been denied the interest and finance charges mainly relating to the funding of the investments proposed in the transmission system of KPTCL. It has not been contested that the Commission has been allowing the interest and finance charges related to investments in the past. Obviously, the principle laid down by this Tribunal in appeal No. 84 of 2006 has not been understood: liability of the consumer arises

only when the Commission, subject to prudent check, allows the expenditure on creation of assets and when the same is capitalized. This Tribunal in its judgment dated August 29, 2006 in appeal No. 84 of 2006 had decided on the issue:

> "*A. Whether KERC acted with authority, fairly and reasonably in interfering with the internal management and domain of the appellant Transmission utility with respect of its commercial plan and proposal to invest Rs. 2700 crores during 2006-07? Whether the consumers have any say with respect to proposal to invest for up gradation of transmission system better maintenance and quality service?"*
>
> Decision of the above issue by this Tribunal was as under:
>
> *"The consumers interest also do not arise at this stage for consideration nor they could be an objector in respect of proposal or plan or investment by utility as the liability of the consumers, if any, arise or there could be a passing by way of return on equity or interest etc. as such*

contingency arises only when the Regulatory Commission subject to its prudent check allows such expenditure, while fixing the annual revenue requirement and determining the tariff. Till then, the consumers have no say and there could be no objection from their side. When the consumers complain poor service or failure to maintain supply, to face such a situation the utility has to plan in advance, invest in advance, execute the project or scheme for better performance and maintain.

The Karnataka Electricity Regulatory Commission has not acted reasonably or fairly in interfering with the internal, commercial management and domain of the transmission utility with respect to its commercial plan and proposal to invest a substantial sum. We have made ourselves clear and in the future years to come the Commission will take this into consideration and will act accordingly. The point 'A' is answered in the above terms."

39. In view of the above judgment of this Tribunal the payments of interest and finance charges, pending final approval of the Commission, are merely provisional payments and, therefore, the Commission need not discontinue its decades old practice of allowing the interest and finance charges to the licensee till capitalization of the assets. If there is any variation in the expenditure made by the appellant and the approval accorded by the Commission, adjustments can always be made. Moreover, if the interest payments are not allowed till capitalization then the Interest During Construction will also form a part of asset base and for the useful life of the asset the return on the equity portion will be allowed to the licensee and this will not be in the interest of the consumer. It will therefore, be just, fair and equitable to continue to allow the interest and finance charges to the appellant as per Commission's well established practice and make required adjustments at the time of capitalization of assets as approved by the Commission. We order accordingly.

Issue E Directions to remit Rs. 620.58 crores.

40. The learned counsel for KPTCL submitted that the directions given by the Commission for remitting Rs. 620.58 crores to the Distribution Companies cannot be enforced against KPTCL on account of the policy directive given by the State Government under section 108 of The Electricity Act, 2003 and the fact that the State Government has not given the said amount to KPTCL and that in the absence of which KPTCL has no revenue to remit the amount.

41. Mr. Ramachandran further submitted that the policy directives of the State Government is a subject matter of proceedings in W.P. No. 11057 of 2007, pending before the Hon'ble High Court of Karnataka and the Commission is a party in the said proceedings and that implementation of any direction in regard to remittance of Rs. 620.58 crores should therefore, have to wait the decision of the High Court. He submitted that, accordingly, as at present, KPTCL cannot and should not be directed to remit the amount of Rs. 620.58 crores and that KPTCL has relied on section 108 of The

Electricity Act, which provides that the decision on the policy directives by the State Government is final and binding on the Commission and KPTCL.

42. In response, Mr. Amit Kapur stated that the direction given by the State Government is on the surplus accruing to KPTCL on account of favourable hydro thermal mix and, therefore, legitimately belong to the consumers and is a matter relating to tariff and is, therefore, illegal and void. He stated that in terms of section 62 (6) of the Act, KPTCL cannot retain amounts which legitimately belong to the consumers and further in terms of section 65, the State Government cannot issue directions in regard to subsidy without making payment for the same. He asserted that the appropriation of the surplus of KPTCL on account of hydro thermal mix by the State Government will amount to withdrawal of subsidy committed by the State Government and, therefore, will be in violation of section 65. He also relied on the decision of the full bench of the Tribunal in Appeal Nos. 4, 13, 14, 23, 25 etc. of 2005 decided on 26.05.2006

wherein the Tribunal has held that the Commission has the powers to enforce its orders on tariff against the State Government which is the 100 % shareholder of the utility.

43. Per contra, Mr. Ramachandran on behalf of KPTCL contended that the State Government had duly given the subsidy committed by it for all the tariff periods and the appropriation of the surplus from favourable hydro thermal mix is not a subsidy issue and in any event these are matters to be adjudicated by the Hon'ble High Court and till then the policy directive of the State Government is binding.

Analysis and decision:

44. We agree with the contention of the appellant that the issue regarding remittance of Rs. 620.58 crores to the distribution companies, being a subject matter of proceedings in the High Court of Karnataka cannot be decided at this stage. We, therefore, order accordingly.

Issue F Non-Truing up of 2006-07

45. Mr. Ramachandran submitted that by not truing up of financials of 2006-07, the Commission has not considered the truing up of various expenditures incurred on actual basis during 2006-07 based on the provisional accounts for the said years. He said that these include A & G expenses, depreciation, interest and finance charges, interest on additional power purchase cost (other than the Tanir Bhavi Corporation Limited) on the pretext, as given in the impugned order, that the annual audited accounts are not available. He stated that the truing up should be undertaken even on provisional accounts and can be readjusted again after audited accounts and in this connection, he placed reliance on the decision of the Hon'ble Tribunal in Appeal No. 269 of 2006 dated 23.05.2007 M/s. Poddar Alloys vs Uttaranchal Electricity Regulatory Commission & Another. He submitted that the truing up was most important as the financials of 2006-07 on actual basis was being adopted as base for Multi Year Tariff and that the State Commission had itself

recognized the need for such truing up to effectively undertake Multi Year Tariff as stated in the impugned order.

Analysis and decision:

46. This Tribunal in its judgment dated May 23, 2007 in appeal No. 269/06, Poddar Alloys vs. Uttaranchal Electricity Regulatory Commission has held that the truing up exercise should be taken up in two stages: firstly on the basis of the available data and information and secondly and subsequently truing up exercise can be taken up when Audited Accounts are available. We order accordingly. The Commission is directed to immediately take up the truing up exercise and decide tariff which should form the base line for the MYT.

Issue G Interest Charges

47. Mr. M.G. Ramachandran submitted that under the Interest and Finance Charges for the year 2006-07, the Commission has not allowed an expenditure of Rs. 220.23 crores being interest on belated power purchase payments without any justification and wrongly stating that there was a lapse on the part of KPTCL and that KPTCL is not in power

trading without noticing that the claim relates to the arrears of the period during which KPTCL was undertaking the functions of Bulk Purchase and Bulk Sale of Power, namely: the purchase of power for onwards sale. He also submitted that KPTCL being deprived of its revenues had to face financial difficulties and, therefore, the delay in the payment of power costs occurred and consequently KPTCL had to incur interest on the same.

48. The learned counsel for KPTCL urged that the Commission be directed to allow the adjustments and pass through in the tariff the amounts in the current tariff itself as otherwise the financials of KPTCL will be seriously affected. He submitted that the distribution tariffs for the tariff period 2007-08 to 2009-10 has not yet been finalized and, therefore, the Commission be directed to give effect to the adjustments without any further delay or other condition. KPTCL also claimed carrying cost at 12% as per the principles laid down by the Commission itself at internal page 117 of the impugned order.

Analysis and decision:

49. We note that the Commission has not allowed an expenditure of Rs. 220.23 crores, being interest on belated power purchase payment on the premise that KPTCL is responsible for the delayed payment. However, it has been contended by the appellant that the claims related to the arrears for the period during which KPTCL was undertaking functions of bulk purchase and bulk sale of power and that KPTCL was deprived of its revenues and therefore, had to face financial difficulties resulting in delay in the payment of power procurements cost. We do not find any justification for not allowing the interest charges to KPTCL; KPTCL was merely a bulk power buyer and seller and not repository of revenue stream. In view of this ground reality we direct the Commission to allow the interest on delayed payment and give effect to the adjustments in the distribution tariff for the periods 2007-08 to 2009-10 along with the carrying cost as per the principles laid down by the Commission.

50. In the result, the appeal is allowed to the extent indicated herein above. The Commission is directed to implement our orders within six weeks.

51. In view of this judgment in the main appeal, IA No. 122 of 2007 seeking stay is rendered infructuous and, therefore, stands disposed of.

(Mrs. Justice Manju Goel) (H.L. Bajaj)
Judicial Member Technical Member

GB
No. of corrections