Before the Appellate Tribunal for Electricity
(Appellate Jurisdiction)

Appeal No. 104 of 2008

Dated: April 8, 2009.

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

M/s G.V.K. Power (Goindwal Sahib) Ltd.
Paigah House, 156-159, Sardar Patel Road
Secunderabad-500003
Andhra Pradesh ....Appellant

Versus

1. Punjab State Electricity Regulatory Commission
SCO: 220-221, Sector: 34-A
Chandigarh-160002

2. Punjab State Electricity Board
The Mall, Patiala-147001
Punjab .....Respondents

Counsel for the appellant:	Mr. M.G. Ramachandran Ms Swapna Seshadri Mr. Anand K. Ganesan Mr. A.Akshaya Babu
Counsel for the respondents:	Mr. M.S. Marwah Resp.for PSERC Mr. A.S. Beriwal Rep for PSEB Mr. Sakesh Kumar Er. J.P. Singh, Dy. CE Ms Jayshree Anand for Resp.No.2 Mr. K.K. Mahalik for R-2

JUDGMENT

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

This appeal challenges order dated April 29, 2008 passed by the Punjab State Electricity Regulatory Commission (hereinafter referred to as the Commission) whereby the Commission has granted in-principle approval of the project cost of the 2 X 270 MW thermal power project proposed to be set up by the appellant in the state of Punjab.

2. Facts of the case to the extent relevant for this appeal are briefly given below:-

3. The appellant, M/s GVK Power (Goindwal Sahib) Limited is a company incorporated under the provisions of the Companies Act with the object of engaging in the business of establishing, maintaining, operating a Thermal power station at Goindwal Sahib in the state of Punjab and for supplying electricity from the said station.

4. The Government of Punjab invited bids from prospective project developers' proposals on the basis of an International Competitive Bidding in the year 1996 to establish a coal based thermal power generation project at Goindwal Sahib, Tarn Taran District, Punjab. The entire electricity generated from the said generating station was proposed to be sold to meet the ever increasing needs of the Punjab State Electricity Board, the Respondent No. 2 herein (hereinafter called PSEB).

5. The appellant was selected on the basis of lowest capital cost by the Government of Punjab under the said International Competitive Bidding Process to build, own and operate the said generating station at Goindwal Sahib.

6. Pursuant to the above the appellant and PSEB executed a power purchase agreement on April 17, 2000 and thereafter, in January, 2007, both the parties initialed a draft amended and restated Power Purchase Agreement (hereinafter called Draft amended and restated PPA) which is to be entered into after

completion of the required formalities including and in particular the approval of the Commission required under The Electricity Act, 2003.

7. Pursuant to the above draft amended and restated PPA initialed between PSEB and the appellant, PSEB filed before the Commission an application being No. 3 of 2007 for approval of the draft amended and restated PPA. The said approval of the Commission is required to be taken by PSEB as per Section 86(1) (b) read with Section 62(1) of The Electricity Act, 2003.

8. In the meanwhile, the appellant was advised to file a petition before the Commission for an in-principle approval of the estimated project cost of the generating station. Accordingly, on March 23, 2007, the appellant filed a petition being petition No. 4 of 2007 for the in-principle approval of the estimated project cost and financing plan. On May 07, 2007, the appellant filed an application under Regulation 10 read with Regulation 69 of the PSERC Regulations for amendment of

the original petition No. 4 of 2007 for incorporating the change in the capacity of the Project to 2X270 MW. The amended application was allowed by the Commission. As per the third proviso to Regulation 7 of the Central Electricity Regulatory Commission (Terms and Condition for Determination of Tariff) Regulations 2004, the in-principle acceptance of the project cost and the financing plan shall be the guiding factor for applying prudence check on the actual capital expenditure.

9. In the petition No. 4 of 2007 filed before the Commission the appellant submitted the entire details of the estimated project cost including such further details and particulars as directed to be furnished by the Commission and also the full justification for the project cost estimated by the appellant.

10. Pursuant to the petition filed by the appellant the Commission apart from hearing PSEB, issued public notices inviting comments from the general public to the petition filed by the appellant.

11. Thereafter, the Commission directed the issue of public notices and invited comments from the general public. PSEB filed its reply to the application in which PSEB did not raise any specific or detailed objection to the estimated capital cost of the power project proposed to be set up by the appellant. PSEB had only stated the factual developments in the case. Apart from PSEB two other objections were received pursuant to the public notice issued by the Commission.

12. Vide order dated April 29, 2008, the Commission disposed of the petition No. 4 of 2007 and decided on the in-principle project cost of the power project proposed to be set up by the appellant.

13. The Commission has approved the capital cost of Rs. 2622.48 crores as against the capital cost of Rs. 2987.86 crores proposed by the appellant leaving a gap of Rs. 365.38 crores and hence this appeal. Before approaching this Tribunal a

review petition was filed by GVK which was rejected by the Commission vide order dated August 06, 2008.

14. Mr. Ramachandran, learned counsel for the appellant has explained to us that GVK has not awarded the project execution on turn key basis by the entire project is given to one agency for implementation with overall responsibility of the entire project and delivery. He said that whereas such turnkey award contract minimizes the work for the project developer (the appellant), it increases the project cost substantially. Appellant having experience in such project execution decided to get the project executed under following different packages in order to reduce the project cost.

a. Boiler Turbine Generator Package to be executed by BHEL;
b. Balance of Plant Package to be executed by Punj Lloyd;
c. Other procurements;
d. Other contractors executing miscellaneous work; and
e. Management and coordination performed by GVK itself.

15. In the project cost projected by GVK amongst others, the break-up was given for Boiler Turbine Generator Package (BTG), Balance of Plant Package (BOP), Engineering erection, civil works and taxes and duties separately at item No. 4,5,6 and 7 as under:

Sl.No.	**Package**	**Amount (Rupees in crores)**
4	Boiler Turbine Generator Package	857.50
5	Balance of Plant	444.87
6	Engineering, erection civil works	624.13
7	Taxes and duties	245.52
	Total	2172.02

16. However, while giving approval the Commission has combined the Engineering, Erection, Civil Works (Item 6 above) and taxes and duties (item 7 above) into item 4&5 and the amount has been stated as under:

Sl.No.	**Package**	**Amount (Rupees in crores)**
4	Boiler Turbine Generator Package	1070.58

5	Balance of Plant	1005.00
6	Engineering, erection civil works	Including in BTG BOP contracts
7	Taxes and duties	Including in BTG BOP contracts
	Total	2075.58

17. Mr. Ramachandran submitted that the difference in the above two works out to Rs. 96.44 crores. The other items of capital cost claimed by the GVK and allowed by the PSERC are also contained in the appeal and the aggregate difference between the capital cost estimates given by GVK and approved by the Commission works out to Rs. 365.38 crores (Rs. 2987.86 crores – Rs. 2622.48 crores = Rs. 365.38 crores). He submitted that in the present case the capital cost proposed by GVK is comparable to that of the other projects and that this fact was placed before the Commission in their submissions dated September 06, 2007. He stated that GVK has proceeded to acquire the land and also made initial payments to EPC contractors, consultants aggregating to Rs.275.45 crores, clearly showing its commitment to the project.

18. Learned counsel contended that the appellant is aggrieved by the reduction or non consideration of the following elements in the estimated capital cost of the project in the order dated April 29, 2008.

(a) Non-inclusion of the cost of initial recommended spares in the capital cost of BTG package;
(b) Non-inclusion of the cost of initial recommended spares in the capital cost of BOP package;
(c) Disallowance of site Grading and Ash Pond Development costs;
(d) Disallowance of start up expenses;
(e) Disallowance of expenses towards power and water for construction;
(f) Production of pre-operative expenses;
(g) Treatment of interest during construction;
(h) Reduction of contingency expenses;
(i) Reduction of financing charges and
(j) Disallowance of working capital margin

19. Mr. Ramachandran reiterated that at this stage only in-principle approval to the capital cost to be incurred by GVK on the project was sought for and the tariff will, however, be based

only on the actual capital cost which GVK incurs. In the event the actual capital cost is in excess of what is approved in the in-principle estimated capital cost GVK has to establish that the additional expenditure has been incurred not for any reasons attributable to the GVK or its suppliers or its contractors. The purpose of in-principle approval is to provide guidance to the project developer and facilitate the lenders and financial institutions to finalize the funding and financing arrangement. In this regard he has cited Clause 1(2) (a) of notification dated March 30,1992 of Government of India which reads as under:-

> *" 1.2 The capital expenditure of the project shall be financed as per the approved financial package set out in the techno-economic clearance of the authority. The Project cost shall include capitalized initial spares. The approved project cost shall be the cost which has been specified in the techno-economic clearance of the authority.*
>
> *The actual capital expenditure incurred on completion of the project shall be the criterion for the fixation of tariff. Where the actual expenditure exceeds the approved project cost the excesses as approved by the authority shall be deemed to be the actual capital expenditure for the purpose of determining the tariff.*

Provided that such excess expenditure is not attributable to the Generating Company or its suppliers or contractors;

Provided that such excess expenditure is not attributable to the Generating Company or its suppliers or contractors;

Provided further that where a power purchase agreement entered between the Generating Company and the Board provides a ceiling on capital expenditure, the capital expenditure shall not exceed such ceiling.

Provided also that in case of multi-unit project, the percentage of capital cost s specified by the authority in its techno-economic clearance shall be considered for fixation of tariff, on commercial operation of the progressive units but in case of delay in commissioning of second or subsequent units from the scheduled date, the project cost, for the period of delay, shall be retrospectively approved for the tariff purpose in the ratio of proportionate allocation of units;

Provided further that if the capital cost of the project increases, in comparison to the cost approved in Techno-economic Clearance, on account of foreign exchange variation or change of low or any other reason not attributable to the Generating Company or its suppliers or contractors and approved by the competent Government the project developers may approach the authority with the recommendations of the competent Government, not more than once in a financial year, for the mid term review of the project cost.

Provided further that the authority may for special reasons to be specified by the project developer, allow *the mid term review of the capital cost more than once in a financial year.*

20. Learned counsel brought to our notice the Central Commission Press release dated August 24, 2005 in-principle approval of project cost by CERC to promote investment in thermal generation:

> " *The Central Electricity Commission (CERC) has announced procedure for granting in-principle acceptance to the estimated cost of a thermal generation project. It is hoped that the regulatory comfort in the form of upfront in-principle acceptance of estimated project cost would help the independent power producers (IPPS) intending to generate and supply electricity in more than one state and companies owned or controller by the Central Government to achieve financial closure expeditiously. Once the CERC has accorded in-principle approval to the estimates of project capital cost and financial plan, the same shall be the guiding factor for applying prudence check on the actual capital expenditure. However, the tariff shall be determined on the basis of actual audited expenditure for the project found prudent by the Commission. The draft regulation was earlier published for comments from stakeholders in May, 2005 which has now been finalized after considering response received. The guidelines for competitive bidding for procurement of generation issued by the Central Government in January, 2005 do not stipulate that all future projects will come through the competitive bidding route. The projects can continue to come under regulated tariff regime.*

Accordingly, applications have been made before the Commission by IPPS for determination of tariff prior to commencement of construction of the generation station since it would give them a level of comfort. The Commission considered the matter and it was felt that existing tariff regulations should be amended to provide for in-principle acceptance of the capital cost of the project before commencement of construction. Request for grant of in-principle acceptance to project capital cost and financing plan would have to be made in the form of a petition with requisite details and a copy served to all prospective beneficiaries of the project. The application shall be posted on website of the applicant and a notice to that effect shall be published in the newspapers for inviting comments/suggestions from stakeholders/general public."

21. Mr. Ramachandran contended that in the impugned order dated April 30, 2008 the Commission had itself recognized the above as under:

"Regulations 20 and 37 of the Punjab State Electricity Regulatory Commission (Terms and Conditions for Determination of Tariff) Regulations, 2005 stipulate that in determining the cost of generation, the principles and methodologies specified by the Central Electricity Regulatory Commission (Terms and Conditions of Tariff) Regulations, 2004 (Regulations are to be kept in view. Regulation 5(3) of the latter Regulations provides that a generating company may make an application for determination of provisional tariff in advance of the anticipated date of completion

of the project, based on capital expenditure actually incurred up to the date of making the application, duly audited and certified by the statutory auditors. Regulation 17 further provides that the actual expenditure incurred on completion of a project shall form the basis for determination of final tariff. The second proviso to Regulation 17 lays down that any person intending to establish, operate and maintain a generating station may make an application before the Commission for in-principle acceptance of he project capital cost and financing plan before taking up the project. The third proviso further provides that where the Commission has given in-principle acceptance to the estimates of project capital cost and financing plan, the same shall be the guiding factor for applying a prudence check on the actual capital expenditure. Evidently these provisions have been incorporated so as to reduce uncertainty regarding tariff on completion of a project which will help investors in achieving financial closure of the project" (page 199)

22. Learned counsel averred that in the review order dated August 06, 2008 the Commission has stated as under:

" *The Commission observes that in-principle approval can, at best, provide a rough estimate of project costs and that these would necessarily have to be fine tuned at a subsequent stage after the project has been completed. It is relevant in this context to note that Regulation 17 of the CERC (Terms & Conditions of Tariff) Regulations 2004 along with subsequent amendments clearly stipulates that the actual expenditure incurred on completion shall, subject to a prudence check by the Commission, form the basis for* *determining final tariff and that in-principle acceptance of estimated project cost and financing plan will only be the guiding factor for applying a prudence check on the actual capital expenditure. Accordingly, even on review, the Commission upholds the in-principle approval of the estimates of the project capital cost as already allowed in order dated April 29, 2008 "(Page 238)*

23. He cited our judgment in M.P. Power Trading Company Limited V/s Torrent Power Limited Appeal No. 11 of 2008 decided on January 19, 2009 in which this Tribunal has observed as under:

> *".....In-principle approval of the capital cost is granted to provide a guidance to the power generator as well as to the financing institution and to indicate the possible tariff which the new generator may expect. This approval is not a part of any adjustment".*

24. Mr. Ramachandran submitted that in Karnataka Power Transmission Corporation Limited V/s Karnataka Electricity Regulatory Commission & Others, 2007 APTEL 223 this Tribunal had held that the Commission should be slow to interfere with the estimation of the costs drawn by the utility and the Commission can always correct the discrepancies at

the time of actual determination of the cost after it has been incurred. The said decision has been followed by the Appellate Tribunal in other subsequent decisions including order dated May 08,2008 passed in appeal No. 129 of 2007, JSEB v/s JSERC and Order dated December 04, 2007 passed in appeal No. 100 of 2007, KPTCL V/s KERC & Others.

25. Mr. Ramachandran contended that in the present case the Commission has proceeded to reject the inclusion of the specific costs under the heads mentioned above, even if such costs are legitimately incurred without any default or failure etc attributable to GVK or its contractor or supplier and even if the incurring of such costs can be shown to be prudent, the apprehension of the appellants and also of lenders is that the Commission may not consider to include the same while determining the completed capital cost of the Project. This apprehension in the minds of the financial institutions and lenders is preventing due financial closure of the project which is essential for implementing the project. Mr.

Ramachandran submitted that without prejudice to this submission on the ten issues (a) to (j) on the reduction in the capital cost estimates for in-principle approval he would plead as under on each of the issues:

(a) Spares of BTG package.

26. Mr. Ramachandran contended that in the order dated April 30, 2008 the Commission allowed the BTG package as proposed by the GVK based on the letter of intent issued to BHEL at Rs. 1070.58 crores finding the same to be reasonable. The contract awarded to BHEL for BTG package is with a price variation formula and a part of the contract price needs to be paid in Euros & US$. In the review order dated August 06, 2008 under para 1, the Commission has rightly recognized that the BTG contract price has a price variation formula and the exchange rates used for conversion of Euros & US$ are respectively Rs. 57.50 and Rs. 41.00 while the actual exchange rates prevailing on the date of payment for the Euro/US$ will be applicable, while making the payment to BHEL. However,

the Commission did not separately deal with initial spares. The initial spares were not included in BTG package of BHEL. In the review order dated August 06, 2008 the Commission has observed as under:

> *"The Commission observes that there is no provision for spares in Annexure VI of the petition where project costs have been detailed. In a subsequent submission dated August 13, 2007, the petitioner while providing the break up of capital cost indicated initial spares as being a part of the total engineering, procurement and construction (EPC) costs. In the LOI placed on BHEL for BTG (clause 1(iv)), it is provided that itemized spares as recommended by BHEL for 3 years operation of the plant are to be ordered separately. In another submission dated January 16, 2008 (para 7), the petitioner mentioned that initial spares are not included in the LOI placed for the BTG package.*
>
> *It is evident that the petitioner has not made any clear and unambiguous statement as to whether any category of spares is a part of the LOI issued. However, relying on the LOI placed on the BHEL for the BTG, it appears that initial spares are included as a part of the BTG package specially when there is a clear indication in clause 1(iv) that itemized spares as recommended by the BHEL for 3 years operation of the plant are to be ordered separately. In the circumstances, the Commission concludes that cost of initial spares has already been catered for and no further provision on this account is warranted at this stage".*

27. He averred that GVK had filed submissions before the Commission in the proceedings in petition No. 4 of 2007. In these submissions it was pointed out that the initial spares related to BTG were not part of the BHEL quoted cost and they were extra items. The letter dated November 12, 2007 written by GVK to BHEL was placed on record wherein it has been stated under scope of services spare parts- itemized price of spares as recommended by BHEL for 3 years operation of the plant to be ordered separately. In para 7 of the submissions dated January 16, 2008 made by the appellant it was specifically stated that the initial spares are not included in the LOI of BTG package and that only mandatory spares are included in cost figures. The provisioning of Rs. 39.65 crore (as indicated in form 5B submitted vide letter dated August 13, 2007) is towards the initial spares of BTG and BOP package.

28. Mr. Ramachandran contended that in view of the above, the specific case of GVK before the Commission has been that the initial spares are not included in the BHEL BTG package.

He submitted that as there is nothing on record to show anything to the contrary in the circumstances, the conclusion reached by the Commission that the initial spares are included in the BTG package is not correct.

(b) Non-inclusion of the cost of initial recommended spares in the capital cost of BOP package.

29. Mr. Ramachandran submitted that as in the case of BTG package the BOP package of Punj Lloyd also excluded the initial spares. In the order dated April 29, 2008 the Commission did not specifically deal with initial spares. The Commission however, accepted the cost of Rs. 1005 crores for BOP package of Punj Lloyd as reasonable. In the review order dated August 06, 2008 the Commission has held as under:

> *"2. Balance of Plant (BOP)*
> *The petitioner has in this context argued that the Commission has failed to take into account the cost of spares in the BOP package. The Commission observes that there is no separate mention of spares in Annexure VI where itemized project costs have been brought out nor is there any reference to this in the LOI placed on M/s Punj Lloyd Ltd. In their submissions of January 16, 2008, the petitioner has mentioned that mandatory spares are included in the BOP cost and it is only in their final submissions of*

April 15, 2008 that it has been indicated that the BOP cost package of Rs. 1005 crores does not include the cost of spares. It is evident that as in the case of BTG, the petitioner has not brought out spares as a separate item of cost right up to April 15, 2008 nor has any clarification been given as to what constitutes mandatory or initial spares. Significantly, there is also no mention of spares in the LOI. In the circumstances, the Commission is inclined to hold that the cost of initial spares has been provided for and there is no occasion for making a separate provision on this account. For these reasons, the Commission sees no reason for deviating from its findings in the order of April 29, 2008".

30. Learned counsel for the appellant stated that in the submissions filed before the Commission it was pointed out that the BOP package did not include the initial spares. In para 7 of the submissions of January 16, 2008 made it was specifically stated that the initial spares are not included in the LOI of BTG package and only mandatory spares are included in cost figures. The provisioning of Rs. 39.65 crores as indicated in form 5B submitted vide letter dated August 13, 2007 is towards the initial spares of BTG and BOP package. He contended that in view of the facts the specific case of GVK before the Commission is that the initial spares is not included

in the BOP package also. He contended that there is nothing on record to show any thing to the contrary and, therefore, in the circumstances the conclusion reached by the Commission that the initial spares are included in the BOP package is not correct.

(c) Disallowance of Site Grading and Ash Pond Development cost:

31. Mr. Ramachandran contended that in the order dated April 29, 2008 the Commission did not allow an expenditure of Rs. 49 crores claimed by GVK for site grading and ash pond development cost on the ground that it is included in the Non EPC work of Rs. 86 crores. The relevant part of the order dated April 29, 2008 read as under:

> *"The Commission is inclined to allow the amount of Rs. 86 crores for non EPC works but does not approve an additional amount of Rs.49 crores for site clearing/grading and Ash pond reported separately in the latest filing by the petitioner as the same are considered included in the total non EPC cost of Rs. 86 crores intimated earlier".*

32. He submitted that in the order dated August 06, 2008 the Commission has held as under:

“ 3. Site grading and Ash pond development costs

The petitioner’s main contention is that full costs on account of site leveling/grading and expenses for providing a flood protection embankment and development of ash pond have not been allowed by the Commission. The Commission observes that Annexure VI of the petition which brings out the estimated project cost has no separate provision for site grading and ash pond development. In submissions of August 13, 2007, the petitioner while providing the break up of capital cost indicated ash disposal area and site development as part of the non EPC and site development costs respectively. Again, in the petitioner’s filing of December 08,2007, site grading, site drainage and ash pond etc. were intimated as part of the non EPC works with site specific features having been clearly outlined giving reference to high quantum of back filing, non availability of adequate back fill material and need to provide impervious lining of ash pond etc. The fact that development of the ash disposal site would be covered under the scope of non EPC works is again confirmed in the petitioner’s submissions dated January 16, 2008. Quite evidently, such costs were known and had been initially factored into the estimates of project capital cost. It is only at the penultimate stage that the petitioner had, in their submissions of April 15, 2008, indicated (without any supporting data) that Rs. 49 crores is being separately provided for site grading and ash pond development. It is also necessary to recall that in the petitioner’s *filing of January 16, 2008, it was unambiguously confirmed that total contract price would not exceed Rs. 2987.86 crores and this included a total of Rs. 86 crores as non EPC component. In the circumstances, it is reasonable to assume that all site development costs including grading, leveling and ash pond development and construction of protection embankment are a part and parcel of non EPC and site development works and that a claim of an additional Rs. 49 crores in similar works is untenable and clearly an after thought".*

33. Mr. Ramachandran contended that as indicated in the submission made by GVK on April 15, 2008 before the Commission the final package which was worked out, particularly, in regard to the BTG package and non-EPC works connected with the BTG package involved non-EPC works of Rs. 86 crores, excluding the cost of Site Grading and Ash Pond Development work which was separately estimated at a cost of Rs. 49 crores thus, aggregating to Rs. 135 crores for other works (non-EPC works) and that the break up of Rs. 49 crores being the cost of Site Grading and Ash Pond Development is given in Annexure 4 to the submissions made on April 15, 2008. Annexures 5 and 6 of the submissions dated April 15, 2008 deals with the cost of non-EPC works and cost of Railway siding respectively. He contended that no part of the cost of Site Grading and Ash Pond Development has been included in any of the items in Annexure 5 or Annexure 6 and accordingly

the amount of Rs. 49 crores being the cost of Site Grading and Ash Pond Development cannot be said to be included in the amount of Rs. 86 crores.

(d) Disallowance of Start-up expenses

34. Mr. Ramachandran submitted that the only ground for not allowing the start up expenses of Rs. 15 crores claimed by GVK has been that it can be off set against the amount that may be recovered from infirm power sale. In the review order dated August 06,2008 the Commission stated as under:

> *"4. Start up expenses*
> *The petitioner claims that disallowance of Rs. 15 crores on account of start up expenses is not justified as the power procurer will only reimburse the cost of coal and fuel oil used for generation of infirm power supplied to it but not the other costs involved, details of which have been furnished in the petitioner's filing of April 15, 2008. It is not disputed that revenues occurring from the sale of infirm power will become available to the petitioner for defraying costs on account of start up expenses. From the details provided in the submissions of April 15, 2008, the Commission notes that cost of coal and fuel constitute almost the entire start up expenses claimed. As these expenses are admittedly going to be met by the power procurer, the claim as per the petitioner's own submission gets reduced to a minuscule amount which has no significant bearing on the totality of costs for a project of this magnitude. The Commission,*

accordingly, does not find sufficient justification in the claim for allowing the start up expenses.”

35. Mr. Ramachandran contended that the above position of the Commission is contrary to the established practice being followed in deciding on the estimate of capital cost. The recovery of price of in-firm power is uncertain. The practice followed is to adjust the in-firm power cost by reduction in capital cost. He said that at the time of grant of approval to the actual capital cost GVK does not dispute that the entire net revenue from the infirm power ought to be adjusted in the capital cost to be finally worked out and the petitioner is duty bound to do so. However, the disallowance of start up expenses at his stage on the presumption that the total revenue from the sale of infirm power will equalize or exceed the start up expenses is not correct. He contended that there is no basis whatsoever to proceed on such assumption particularly at this stage when financials are being worked out on estimates and that there will be an opportunity at the stage of final approval of the project cost based on actuals to adjust the revenues from

infirm power against capital cost. He submitted that this has been the consistent practice followed in all generation projects and the same should be followed in this case also.

(e) Disallowance of expenses towards power and water for construction.

36. Mr. Ramachandran contended that the only ground on which such expenses had been disallowed is that they already form a part of BTG, BOP and non EPC cost allowed. He submitted that in the order dated April 29, 2008 the Commission has held as under:

> *"Power and Water for construction.*
> *The petitioner envisages an outlay of Rs. 12 crores for the purpose. The Commission notes that this cost is included in the BTG as well as BOP contracts while the cost associated with providing power and water at the construction site is included in the estimate for non EPC works. As such no provision is required to be separately made for this purpose".*

37. Learned counsel also brought to our notice that in the order dated August 06, 2008 the Commission has held as under:

> *" The petitioner has submitted that these costs are to be incurred for the development of infrastructure for*

power distribution and the cost of energy and water on works not included in the main packages. It has been further clarified that PSEB will make power available at site at 33 kV or above and that a sub station would be developed to step down the voltage 11 kV and also provide internal distribution of power.

The Commission notes that the provision of Rs. 12 crores in the estimates was for construction power and water charges. Even in the break up of the cost, provided for the first time by the petitioner in its filing dated April 15, 2008, the major portion is for defraying the construction power and water charges. Such expenses for BTG and BOP works are to be paid by the respective suppliers/contractors, as provided in their respective LOIs. As regards creating infrastructure for these facilities and payment of such charges for non EPC works, the same are covered in the non EPC estimates. Accordingly, the Commission finds no reason to change its earlier decision on this issue."

38. Learned counsel submitted that the BTG and BOP packages do not cover the entire expenses for the development of the infrastructure for the power distribution and energy consumed, the statutory fees etc paid. The amount of Rs. 12 crores claimed by the petitioner is the amount which GVK is required to incur to install a sub station to reduce the voltage level to 11 kV and make arrangement for distribution of

electricity for construction purposes and GVK will be making payment to PSEB for such supply of electricity. He contended that the amount of Rs. 12 crores estimated by GVK be allowed for the above purpose, subject however, to appropriate the adjustment to be done based on actual cost incurred by GVK and subject further to prudent check at the time of approval of the final capital cost on the date of the commercial operation.

(f) Production of Pre-operative expenses.

39. Mr. Ramachandran contended that the reason given for reducing preoperative expenses from Rs. 50 crores to Rs. 15 crores in the Commission's order dated April 29, 2008 is as under:

> *"Pre-operative expenses:*
> *A sum of Rs. 50 crores has been provided by the petitioner on this account. The Commission notes that the bulk of the work relating to this project will be through two major contracts for the BTG and BOP packages which include erection, testing and commissioning. Moreover, railway siding work is to be carried out on an estimated contract price of Rs. 35 crores with the remaining non EPC works of Rs. 51 crores roughly mounting to 2% of the total project cost.*

As such, the establishment that the petitioner will need to deploy during the project period for supervision and management is not likely to be very large. The cost estimate provided in this regard thus appears to be very much on the higher side and the Commission considers that a sum of Rs. 15 crores, is sufficient to meet these costs".

40. Learned counsel stated that the review order dated August 06, 2008 the Commission has stated as under:

" *The petitioner has contended that a reasonable estimate of Rs. 50 crores on pre-operative expenses had been made but the same has been severely curtailed by the Commission. It is noted that such expenses are to be incurred largely for administrative and supervisory costs during the course of executing the project. It has also been observed that major portion of the total works are included in the BTG, BOP and non EPC works packages, leaving only a very small quantum of work that need to be directly supervised by the petitioner. It is true that acceptance of such costs would ultimately be subjected to a prudence test when tariff determination is to take place but this can not be construed as a mean that the reasonability of such expenses is not to be gone into at this stage. The Commission has already held that Rs. 15 crores would be sufficient to meet the costs in this respect and it does not see any reason to arrive at a different conclusion now".*

41. Learned counsel contended that the Commission has reduced the claim for pre-operative expenses from Rs. 50 crores

to Rs. 15 crores on the grounds that the bulk of the work is going to be done by BTG and BOP contractors. He reiterated that GVK is implementing the project on non-turnkey contract basis and there are substantial pre-operative expenses to be incurred by GVK. The Commission has not considered the various co-ordination and other related works to be done by GVK itself as the contract is not given on turn-key basis. The amount of Rs. 50 crores claimed towards pre-operative expenses is based on the reasonable estimates made by GVK on the advise from experts, consultants and financial institutions funding the project. These have been projected after great deal of deliberation. The financial institutions consider such expenses as an essential part of the project cost and financial closure to be achieved by GVK is dependent on appropriate estimation of such expenditure. Learned counsel contended that the substantial reduction of this expense at this stage will cause serious prejudice to the implementation of the project cost. And that anyway the in-principle approval to the project cost by including such expenses as estimated by GVK are subject to prudent check after the actual costs are incurred and therefore, the interest of PSEB and the public at large will be fully protected by the Commission at appropriate stage.

(g) Treatment of Interest during construction.

42. Mr. Ramachandran submitted that the estimated cost of Rs.2987.86 crore submitted to the Commission in May, 2007 was based on the assumption that 50% debt would be raised in US$ and 50% debt in INR. Subsequently in view of the limitations in raising debt in US$, the appellant had submitted to the Commission that it will be raising the entire loan in INR. This has been recognized in Commission's order dated April 29, 2008 under head "Interest During Construction". In the review order dated August 06, 2008 the Commission has clarified as under:

> " *The petitioner has submitted that the Commission has reduced the claim of IDC by adopting a different method of calculation. Even when a debt equity ratio of 80:20 has been allowed by the Commission, the IDC calculation in the impugned order assumes that*

the petitioner will bring in 50% of the total equity before drawing upon any installment of the loan. On the other hand, the petitioner proposes to initially bring in 30% of the total equity which is in line with the financing requirements. The petitioner has further submitted that drawdown of debt takes into account the supply schedule as provided in the EPC and non-EPC contracts while that for other expenses is based on estimates. It has been argued by the petitioner that as IDC will eventually form a part of the project cost based on the actual amount spent, the amount claimed should be accepted at the stage of granting in principle approval.

The petitioner has rightly observed that IDC is likely to form part of the project cost based on the actual amount spent on IDC. Since the petitioner had not furnished any details in respect of the supply and construction schedule for EPC as well as non EPC works, phasing of expenditure by the Commission in its order of April 29,2008 was presumptive and based on historic considerations and industry practice. IDC as per actuals would be considered at the time of tariff determination except where reasonableness of such cost is not substantiated. Accordingly, for the purpose of in-principle approval of the estimates of project capital cost, phasing of expenditure adopted by the Commission is in order. As regards the upfront equity contribution by the petitioner to be expended before any installment of the loan is drawn, the Commission has no objection if the petitioner brings down the same to any value between 30% to 50% (in place of 50% taken into order dated April 29, 2008), provided the petitioner can manage additional term loan without any extra cost to the project capital cost estimates, on this account. The Commission further observes that all the other pleadings made in the review petition *were already on record and have been considered before passing the order dated April 29, 2008 and there is no patent error of law or fact therein that warrants review of the IDC cost as approved by the Commission".*

43. Learned counsel averred that in view of the clarification given by appellant he be permitted to proceed on the basis that the IDC will be adjusted as per actuals but subject to prudence check and based on the petitioner bringing in equity in the proportion of 30% and phasing of expenditure adopted by the Commission is indicative only. He submitted that the phasing of the expenditure has been submitted to the Commission on January 16, 2008. The phasing of expenditure in the first year, 2nd year and 3rd year up to the COD and thereafter three months after the COD has been decided in a manner which is not consistent with the finalized packages with the contractors and therefore cannot work. The contractors will not accept such phasing of expenditure, when the contracts with them stands concluded and cannot be re-opened at this stage.

44. Mr. Ramachandran contended that the phasing out has been done only on assumptions and without regard to the expenditure to be incurred as per the BTG and BOP packages and non-EPC contracts concluded or to be concluded by the petitioner and that the direction that 50% of the total equity to be expended before any part of the loan is taken is completely contrary to:

- Debt Equity Ratio of 80: 20 approved for the project; and
- Normal practice adopted in financing generation projects.

(h) Reduction of Contingency charges.

45. Mr. Ramachandran stated that in the order dated April 29, 2008 the Commission stated as under:

> "Contingency
> *GVK has provided a sum of Rs. 66.85 crores for unforeseen expenses. As a bulk of the expected outlay has been firmed up in terms of a contract for the BTG, BOP package and the Railway siding, there is a need to provide contingency only for remaining non EPC works estimated to cost Rs. 51 crores. Accordingly, the Commission considers that the*

provision of Rs. 5 crores, is sufficient and reasonable for this purpose".

46. He submitted that in the review order dated August 06, 2008 the Commission has stated as under:

> " *In the review petition, it is stated that contingency totaling 66.85 crores has been worked out as 3% and 2.10% on EPC and non- EPC works respectively to meet any unforeseen increase in the project cost. It is further stated that the financial closure will not be possible if the contingency reserve is not allowed as financial institutions insist that the project should have suitable amount of contingency as part of the proposed capital cost. The Commission had given careful consideration to the submissions of the petitioner in earlier filing as well as in the review petitioner and notes that it had in the order of April 29, 2008 held that a provision for contingencies has already been made in the BTG, BOP and non EPC work packages which leaves works amounting to Rs. 51 crores for which contingency needs to be provided and Rs. 5 crores for this purpose as already provided appear to be sufficient. There is nothing in the arguments preferred by the petitioner at this stage which rebuts the findings of the Commission and accordingly there is no occasion for reconsideration of the same".*

47. Learned counsel reiterated that GVK is implementing the project on non-turnkey basis. The Commission has not considered the various possible eventualities where GVK may

have to incur he expenses not envisaged. There is no provision made for contingency while finalizing the BTG and BOP packages. He contended that the amount of Rs. 66.85 crores claimed towards contingency expenses is based on the reasonable estimates made by GVK on the advise from experts, consultants and financial institutions funding the project. These have been projected after great deal of deliberation. The financial institution consider such expenses as an essential part of the project cost and financial closure to be achieved by GVK is dependent on appropriate estimation of such expenditure.

48. He contended that the contingency reserves for expenditure to meet the unforeseen circumstances is essential and that if the contingency does not happen the expenditure will not be incurred and the actual capital cost alone is to be approved. He submitted that if contingency does happen money will be available for the project developer to proceed with the implementation and that GVK will have to then give the

justification at the time of determination of the actual completed capital cost.

49. He contended that the financial institutions do not approve the project without sufficient contingency reserves in the initial estimate of the capital cost and that the substantial reduction of this expense at this stage will cause serious prejudice to the implementation of the project.

(i) Reduction of Financial charges.

50. Learned counsel contended that the Commission has reduced the financial charges claimed by GVK from Rs. 70 crores to Rs. 16 crores only on the ground that the charges for financial and developmental charges etc. are not to be included. He averred that these are actual costs incurred by GVK for project financing and achieving financial closure in a prudent manner and with best possible rates. However, in the order dated August 06, 2008 the Commission has held as under:

"9. Financing charges.

The petitioner has urged that letter of credit (LC) charges are a part of the financing charges as payment security mechanism for the EPC and non EPC contracts. A copy of letter from the IDBI Bank dated May 08, 2008 showing the LC Commission that would be charged has also been filed. It is further stated that the provision for financial advisory fees @ 1% of the debt is based on supporting documents filed as Annexure-8 of submission dated December 08,2007. The petitioner's prayer is to allow financing charges at Rs. 70 crores inclusive of LC commission of Rs. 31.80 crores and financial advisory fees @ 1% of the debt. The Commission has carefully gone through the pleadings in the review petition and observes that similar submissions had been made earlier which were considered by the Commission while deciding this issue in order dated April 29, 2008. The letter of May 08, 2008 from IDBI submitted along with the review petition has been obtained subsequent to the order and was not on record at the time of passing the order. In any case, this pleading of the petitioner was taken into account while deciding the issue of allowing financing charges. As regards financial advisory fee, the same was not allowed as there was no document to substantiate this claim attached with Annexure-8. For all these reasons the Commission, even after reconsidering the submissions of the petitioner, is unable to find any additional justification in allowing increase in the financing charges".

51. He submitted that the letter dated May 08,2008 from the IDBI Bank showing clearly the liability to pay LC commission was filed before the Commission which has not been

considered. The financial advisory fees at the rate of 1% of the debt inclusive of taxes is economical and competitive for a loan of about Rs. 2400 crores to be syndicated from the financial institution and secured to the project. Such fees are payable by all infrastructure projects. Further, GVK had submitted the supporting vide its affidavit dated December 08, 2007.

(j) Disallowance of working capital margin.

52. Mr. Ramachandran submitted that in the order dated August 06,2008 the Commission has stated as under:

> *" 10 Working capital margin (WCM)*
> *It is stated in the review petition that it is necessary that margin on working capital is funded with long term funds and should be included s a part of the project cost. It is further stated that the Central Electricity Regulatory Commission (CERC) while granting in-principle approval in the case of Essar Power Limited has allowed working capital margin of Rs. 60.37 crores in the order dated August 02,2006. Therefore, working capital margin should be allowed s a part of the capital cost.*
>
> *The Commission is of the view that cost of working capital margin forms a part of the Annual Revenue Requirement and is not a part of the project cost. The pleadings of the petitioner that CERC has included working capital margin in the project cost is not*

substantiated from a careful reading of the order in the case of Essar Power Ltd. The per MW cost of Rs. 2.52 crores approved by the CERC in para 17 of its order has been taken from para 8 thereof where the same has been worked out by excluding the working capital margin. The mention of including working capital margin of Rs. 60.37 crore in para 17 of the ibid order also appears to be anomalous because after including this amount in the capital cost, the per MW cost exceeds Rs. 2.52 crores approved by CERC. Moreover, in an immediately succeeding order dated August 22, 2006, CERC has, in the case of Torrent Power Generation Limited, clearly held (para 11) that as per its Regulations of 2004, working capital margin is not a part of the capital cost. Accordingly, the Commission reiterates its earlier findings on this issue."

53. He submitted that the margin on working capital has been disallowed from the project cost. It is necessary that margin on working capital is funded with long term funds as such and should be included as part of the project cost.

54. Second respondent, Punjab State Electricity Board, submitted that they would like that the issue of in-principle approval may be resolved at the earliest so that the state can receive power from this plant as the Punjab State has been expecting power from this plant for the last over a decade.

Learned counsel for the PSEB further submitted that the tariff for the power from the plant has to be determined by the Commission and the same will be acceptable to them as per the Power Purchase Agreement between the appellant and the Board.

55. Learned counsel Mr. Sakesh Kumar appearing for the Commission vehemently contended that all the issues raised by the appellant have been dealt in details in the order of the Commission. He averred that it cannot be the case of the appellant that whatever costs are given by it the same should be accepted by the Commission on the plea that this is the stage of in-principle approval.

Analysis and Decision

56. We have heard various contentions of all the parties and perused their submissions made.

57. At the outset it is to be understood that the appellant has sought in-principle approval from the Commission. Eventually

after the project is completed and before it is commissioned, the appellant is required to file petition for determination of the tariff for this station. In this context, it will be useful to recall our judgment in appeal 11 of 2008 dated January 19,2009 in which this Tribunal has observed as under:

> *" 9………In-principle approval of the capital cost is granted to provide a guidance to the power generator as well as to the financing institution and to indicate the possible tariff which the new generator may expect. This approval is not a part of any adjudication. The Commission certainly has the power to review a decision which was purely technical and administrative provided however, it is a bona fide exercise of its functions:*

58. We now proceed to analyse and decide each issue raised by the appellant with the aforementioned backdrop of the case.

Issue No. (a) Non-inclusion of the cost of initial recommended spares in the capital cost of BTG package.

(b) Non-inclusion of the cost of initial spares in the capital cost of BOP package.

59. It is a normal practice to procure the following spares for main plant and equipment.

(i) Mandatory spares

(ii) Recommended spares

(iii) Insurance spares

(i) Mandatory spares are such spares as are necessarily required and are procured along with the main equipment in the first instance itself.

(ii) As far as recommended spares are concerned, it is a normal practice to obtain prices of the recommended spares along with price of the main equipment. The engineering, operation and maintenance Engineers of the owner study the drawings and the equipment being procured. Based on their experience of operation and maintenance they decide as to which recommended spares should be procured by the owner. Normally these spares are not ordered along with the main equipment and are ordered about six months after the Award of the main equipment order when more equipment details and drawings are available.

(iii) Insurance spares are such of those spares as are capital intensive and require long delivery periods. Such equipment may or may not be used during the life of the plant but is necessarily purchased as an insurance so that in case these are required the entire plant will not remain in- operational because of non-availability of such spares. The appellant in the present case has rightly decided to order the recommended spares separately at a later stage.

60. The appellant in its letter dated November 12, 2007 to BHEL has mentioned that the spares recommended by BHEL for three years operation of the plant will be ordered separately.

61. Appellant has clarified in its submission on January 16, 2008 to the Commission that initial spares are not included in the LOI of BTG package and that only mandatory spares are included in BOP cost figures. It was further clarified that provisioning of Rs. 39.65 crores as indicated in the form 5 B submitted vide their letter dated August 13, 2007 is towards

the cost of initial spares of BTG and BOP packages. We are unable to agree with the observations of the Commission that as there is no mention of spares in the LOI "the Commission is inclined to hold that the cost of initial spares had been provided for and there is no occasion to make separate provision on this account". We have explained (supra) that recommended spares are normally ordered separately after due examination by the owner's engineer. It is the only mandatory spares which are ordered along with the main equipment. In view of this we allow Rs. 39.65 crores as cost of recommended spares for BTG and BOP packages for the purpose of in-principle approval. Actual prudent expenditure on all spares will be allowed by the Commission while determining tariff.

(c) Site Grading and Ash Pond Development Cost.

62. We note from the submissions of the appellant dated April 15, 2008 to the Commission vide which Letter of Intent (LOI) dated April 14, 2008 issued to M/s Punj Lloyd Ltd. is enclosed. In the scope of work for BOP in this LOI, under

exclusions 7 and 8, it is clear that site leveling, site grading and ash disposal area development works are excluded. Annexure IV gives the cost of site grading and ash pond as 490 million rupees. As this information was available with the Commission we do not find any reason as to why this cost of Rs. 49 crores should not be allowed at this stage of in-principle approval. In this view of the matter we, therefore, allow the appeal.

(d) Disallowance of Start up expenses.

63. We agree with the Commission's observations that the appellant will be able to recover the cost of infirm power and thereby recover the cost of fuel, start up power etc. from the receiver of the infirm power. However, it has to be kept in mind that the appellant will have to pay for the coal, fuel oil and start up power bill in the first instance. It is only after the infirm power has been supplied and billed that the appellant will be able to recover the cost in due course. It is therefore, necessary to allow the cost of start up expenses as estimated by the appellant. The cost of infirm power will eventually be reduced

from the capital cost of the project. In this view of the matter also we allow the appeal.

(e) Disallowance of expenses towards power and water for construction.

64. In large projects it is a normal practice to provide power and water for construction to various contractors. The appellant has categorically stated that BTG and BOP packages do not cover entire expenses for the development of infrastructure for power distribution and energy consumed and statutory fees to be paid. The amount of Rs. 128 crores claimed by the appellant is required for installation of sub station to reduce the voltage to 11 kV, distribution system for construction purposes and energy payment to PSEB for supply of electricity. These are all actual expenses which will be allowed by the Commission only if these are prudently expended and therefore, we do not find any rationale in not allowing these at this stage of in-principle approval when the appellant is stating that the BTG and BOP packages do not

cover the entire expenses for development of infrastructure for the power distribution and energy consumed. In this view of the matter we allow the appeal.

(f) Production of Pre-operative expenses.

65. Large projects can be executed either on turnkey basis or on the basis of separately awarding various packages such as site development, BTG, BOP and Ash Pond etc. The role of owner in a turnkey project is minimum and the owner engineers have to supervise the projects on the whole with respect to quality and timely completion. However, when the project is awarded to several contractors on EPC basis for individual packages, the owner has important role to play with respect to overall supervision of all packages, contract management, inspection of equipment and works with respect to quality control, expediting supply, ensuring sequential dispatches of equipments, ensuring timely completion of works of one contractor to handover the same to the next contractor. It is a known fact that the project cost differential between

turnkey basis and non-turnkey basis projects is substantial. Such owners who have expertise available within their organizations always prefer to execute the projects on the basis of several packages rather than on turnkey basis. Such approach also enables their operation and maintenance engineers to take over the plant immediately on its completion.

66. In view of the aforesaid discussion we find rationale in the arguments of the appellant and decide that the sum of Rs. 50 crores provided as pre-operative expenses (being less than 2% of the project cost) be allowed. However, only the actual prudent expenditure of pre-operative activities may be allowed at the time of determination of the tariff.

(g) Treatment of Interest during construction.

67. We observe that the Commission has decided as under:

> *"As regards the upfront equity contribution by the petitioner to be expended before any installment of the loan is drawn, the Commission has no objection if the petitioner brings down the same to any value between 30% to 50% (in place of 50% taken into order dated April 29, 2008), provided the petitioner can manage*

additional term loan without any extra cost to the project capital cost estimates, on this account".

68. This issue lies in a narrow compass. The appellant proposes to deploy 30% of the total equity before the drawdown of debt. However, the Commission has decided that the appellant should bring equity between 30% to 50% of the total equity before drawdown of debt provided the appellant can manage additional term loan for funding equity between 30% and 50% without any extra cost to the project capital estimates on this account. This means that if the appellant brings in only 30% of the equity upfront, the remaining 20% of the equity will have to be arranged by the appellant through a term loan at his own cost thereby implying that asfaras the total project cost is concerned, Interest During Construction (IDC) on this component of equity borrowings will have to be borne by the appellant.

69. In practice, the lending agencies themselves do require that the project developer first deploys in a portion of his equity

to prove his commitment to the project. It is the lending agency itself which ensures, depending upon the credit rating of the developer, as to how much equity infusion can establish his commitment. In this case the lending agencies are ready to lend on 30% equity infusion by the appellant in the project. Of Course more equity infusion before borrowings does entail some reduction in the tariff as no return on equity or interest on the equity infusion forms part of tariff. In view of this it is always the intention of the project developer to infuse only as much equity as is required by the lending agencies. Balance has to be kept between the interest of the consumer and the project developer by the Commission. To be fair to all parties infusion of equity and debt must go simultaneously in equal proportions. In our view 30% upfront equity infusion is sufficient since the lending agencies have confirmed that only 30% of the total equity is required to be brought by the promoter. Therefore, in this view of the matter we allow the appeal.

70. The phasing of expenditure is done keeping in view the terms of payment of the various contract packages awarded by the project developer. Terms of payment have a direct bearing on the pricing of the equipment. Appellant has to make payments to various contractors based on terms of payment of each contract. In view of this the phasing of the expenditure cannot be done in isolation disregarding the terms of payment of the contracts. In view of this, we direct the Commission to redo the phasing of expenditure consistent with the finalized packages with various contractors.

(h) Reduction of contingency charges.

71. Large projects when executed on non-turn key basis always face several risks such as delayed deliveries of equipment, non sequential supplies, delayed execution of various works by one contractor forming inputs for another contractor. In large long gestation projects contingencies can and do arise. Financial Institutions like to see the completion of the project despite several unforeseen circumstances and,

therefore, do require that sufficient contingency reserves are available in the initial estimates before they approve the project and lend money for the same. It is difficult to assess requirement of funds due to contingencies but it is normal to provide 2-3% of the project cost as contingency reserves. In the instant case in hand though the individual contractors for various packages would have provided for contingencies in respect of their packages, it is the appellant who will be responsible for overall timely completion of the project despite delays of a package forming input for the other. This may call for compression of schedule requiring additional funds. A particular package contractor may have to overstay due to default of the other. To cover all such eventualities and cost escalations, it is desirable that contingency reserves are available with the appellant. The contingency reserves provided if not used will in anyway not form part of the project cost while determining the tariff by the Commission. In this view of the matter we allow the appeal.

(i) Reduction of financial charges.

72. In large projects requiring massive investments, it is necessary to depend upon the Financial Advisers who arrange loans from other Financial Institutions. Letter of Credit established by the purchaser of equipment guarantees timely payment to the suppliers. In view of this charges for Letter of Credit and Financial Adviser fees and charges do form part of project cost. In this view of the matter also we allow the appeal.

(j) Disallowance of Working Capital Margin.

73. Working Capital is required once the station has become operational. Interest on Working Capital forms a part of tariff. However, so as to arrange working capital, banks normally require some working capital margin which should be available with the owner. This Working Capital Margin is a sunk cost. Therefore the Working Capital Margin (virtually equity) has to be included in the capital cost of the project and return on this

component of equity also has to be allowed. Alternatively, the working capital margin itself could be arranged through debt and equity components in which case interest on the non equity component and return on the equity component would have to be allowed. In either case working capital margin being essential in the hands of the owner has to form a part of capital cost which may be funded partly by equity and partly by debt. Parties have confirmed that there is no regulation issued by the Commission in respect of Working Capital Margin. In view of the aforesaid discussion we allow the appeal in this view of the matter also.

74. In conclusion the appeal is allowed but with no order as to cost. The Commission shall abide by our directions in paras 61,62,63,64,66,69,70,71,72 and 73.

75. Pronounced in the open court on 8th day of April, 2009.

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