Before the Appellate Tribunal for Electricity
(Appellate Jurisdiction)

APPEAL NO. 66 of 2008

Dated: 18th August, 2010.

PRESENT: HON'BLE MR. RAKESH NATH, TECHNICAL MEMBER
HON'BLE MR. JUSTICE P.S. DATTA, JUDICIAL MEMBER

NTPC Limited
NTPC Bhawan
7, Institutional Area
Lodhi Road
New Delhi – 110003

…Appellant

Versus

1. Central Electricity Regulatory Commission
7th Floor, Core- 3, SCOPE Complex
Lodhi Road, New Delhi – 110003

2. (a) Transmission Corporation of Andhra Pradesh Ltd.
(APTRANSCO)
Vidyut Soudha
Khairatabad, Hyderabad- 500082

2(b) AP Eastern Power Distribution Company Ltd.
(APEDCL)
Sai Shakthi Bhavan
30-14-09, Near Saraswathi Park
Visakhapatnam – 531020

2(c) AP Southern Power Distribution Company Ltd.
(APSPDCL)
H. No. 193-93 (M) Upstairs
Renigunta Road,
Tirupathi – 517501

2(d) AP Northern Power Distribution Company Ltd.
(APNPDCL)
Opp: NIT Petrol Pump, Chaitanyapuri,
Warangal – 506004

2(e) AP Central Power Distribution Company Ltd.
(APCPDCL)
Singareni Bhavan
Red Hills, Hyderabad – 500004

3. Tamil Nadu Electricity Board (TNEB)
800, Anna Salai
Chennai – 600002

4(a). Karnataka Power Transmission Corporation Ltd.
(KPTCL)
Kaveri Bhawan, K.G. Road
Bangalore – 560009

4(b). Bangalore Electricity supply Company Ltd.
(BESCOM)
Krishna Rajendra Circle
Bangalore – 560009

4(c) Mangalore Electricity Supply Company
(MESCOM)
Paradigm Plaza, a.b. Shetty Circle
Mangalore – 575001

4(d) Chamundeshwari Electricity Supply Corpn. Ltd.
(CESC Mysore)
927, L.J. Avenue, New Kantharajaurs Road
Saraswathi Puram
Mysore – 570009

4(e) Gulbarga Electricity Supply Company Ltd.
(GESCOM)
Main Road, Gullbarga,
Karnataka – 585102

4(f) Hubli Electricity Supply Company Ltd.
(HESCOM)
II floor, Ejureka Junctin T.B. Road
Hubli – 560029

5. Kerala State Electricity Board (KSEB)
Vaidyuthi Bhavanam, Pattom
Thiruvananthapuram – 695004

6. Electricity Department (PUDUCHERRY)
NSC Bose Salai
Govt. of Puducherry
Puducherry – 605001

…Respondents

Counsel for the Appellant: Mr. M.G. Ramachandran,
Mr. Anand K. Ganeshan
Mr. Swapna Seshadri &
Ms. Sneha Venketaramani

Counsel for the Respondent: Mr. P. R. Kovilan &
Ms. Geeta Kovilan for TNEB, Resp. No. 3

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

JUDGMENT

The NTPC, the Appellant herein filed a petition before the Central Electricity Regulatory Commission (CERC), the Respondent No. 1 herein on 10.02.06, being petition No.179/2004 praying for determination of tariff for Talcher Super Thermal Power Station

Stage II for the period from 01.04.2004 to 31.03.2009 in accordance with the provision of the Tariff Regulations, 2004.

2. The Respondent No. 1 disposed of the petition by an order dated 31.1.2008 determining the tariff for the period under reference, and while doing so, many of the points advanced by the NTPC were overruled while some were accepted.

3. Feeling aggrieved by the order passed by the Respondent No. 1, the NTPC preferred this appeal to ventilate the points which did not prevail with the Commission, the Respondent No.1.

4. By way of introductory notes we put it on record that the generating station called Talcher Super Thermal Power Station Stage II consisting of Units I, II, III & IV each of 500 MW were put under commercial operation on 01.08.2003, 01.03.2004, 01.11.2004 and 01.08.05 respectively.

5. The tariff for the units I and II for the period from 01.08.2003 to 31.03.2004 was determined by the Commission by order dated

13.06.2005 in Petition No. 1/2003. Again, by order dated 14.01.2005 Respondent No. 1 had earlier allowed provisional annual fixed chares with effect from 01.11.2004 in respect of units 1, II and III and base energy charges during and after stabilization. The rate of infirm power was also made applicable from the date of synchronization of unit IV to the date of commercial operation of that unit. Further, the Commission by its order dated 01.09.2005 in IA No. 13/2005 had allowed provisional annual fixed charges for units I to IV based on the certificate of the auditors. The energy charges that were allowed during and after stabilization period were corrected subsequently by an order dated 09.11.2005.

6. Against the above background NTPC, the appellant herein, in respect of the period from 01.04.2004 to 31.03.2009 claimed annual fixed charges at Rs.55094 lakh, Rs.83846 lakh, Rs.70478 lakh, Rs.106687 lakh, Rs.103557 lakh, Rs.98643 lakh and Rs.93959 lakh between the said period from 01.04.2004 to 2008-2009. The NTPC furnished before the commission the details of working capital for the period from 01.04.2004 to 31.03.2009 and this working capital consisted of several heads such as coal stock, cost of secondary fuel

oil, O & M expenses, spares, receivables and interest on working capital that was claimed @ 10.25%. Interest on working capital of Rs.2281 lakh that stood as on 1.4.2004 gradually rose to Rs.4750 lakh in the year 2008-09.

7. NTPC put a sum of Rs.4,96,110 lakh as on 01.08.2005 as capital cost which was inclusive of IDC (Interest During Construction) and FC of Rs.65,315 lakh. That is to say, excluding these two items of expenses, the hard cost as on date of commercial operation of generating station came to Rs.430792 lakhs. Now, the NTPC furnished a list of deferred works amounting to Rs.73547 lakh inclusive of a sum of Rs.10000 lakh on account of contingency thereby making the completed hard cost at Rs.504339 lakhs.

8. The Commission while determining the tariff for the period in question dealt with several issues namely un-discharged liability, initial spares, debt-equity ratio, target availability, return on equity, interest on loan, depreciation, advance against depreciation. O & M expenses, annual fixed chares, energy variable charges, reimbursement charges and cut off date. Of these issues, the bone of

contention rests with the issues of un-discharged liability, disallowance of interest during construction on the notional loan, treating depreciation as deemed loan repayment, cost of maintenance spares, ignoring the amount of the opening capital cost as on 01.04.2004 and application of the principle of "cut off" date.

9. The appellant argued before the Central Electricity Regulatory Commission that while arriving at the amount of the capital cost the Commission should take into consideration the amount of the liabilities in respect of which there was actually no cash out flow having regard to the regulation 17 of the Regulations, 2004. It was argued that the "actual expenditure incurred" cannot be restricted to actual cash out flow and it must cover the liabilities incurred or obligation suffered. As against this contention of the appellant, the Respondent No. 3, Tamil Nadu Electricity Board (TNEB) on the other hand, argued before the Commission that the tariff should not be allowed on outstanding liabilities. The Commission in this connection referred to its previous judgment in petition No.106 of 2006 and held that outstanding liabilities should not form part of the capital cost, as such negated the claim of the appellant.

10. Such negation of the claim of the Appellant is based on the observation of the Commission at para 29 and 30 of its earlier judgment passed in Petition No.106/06 preferred by NTPC in respect of determination of tariff of Rihand Super Thermal Power Station Stage II which is reproduced below:

> *29. From the various clauses of Regulation 20, it would be seen that emphasis is that when equity deployed is less than the normative equity of 30%, equity actually employed is to be the basis for determination of tariff. In case, the liabilities which are unpaid and are to be settled at a later date or time are included in the capital cost, as claimed by the petitioner, will inflate the amount of equity, dehors the Regulation 20, since it will not be equity actually employed. Therefore, inclusion of deferred liabilities in the capital cost would be in violation of Regulation 20 of the 2004 Regulations. In fact, Regulation 18 which deals with the additional capitalization specifically provides that the deferred liabilities comprising the expenditure incurred after the date of commercial operation, are to be considered as part of additional capital expenditure.*
>
> *30. We are also conscious of the fact that the basis for the entire scheme for determination of annual fixed charges specified in the 2004 Regulations is ``cost plus" approach. For this reason, the term ``expenditure incurred" or ``incurred" are qualified by ``actual" or ``actually" emphasizing ``something real" or ``real" expenditure as opposed to something constructive, or theoretical or speculative. In case the returns are allowed, without corresponding cash out flow, it will amount to unjust enrichment of the petitioner at the cost of the consumer who ultimately bears the burden of tariff. In the proceedings for determination of tariff for the period 2004-09, it has come to the notice of the Commission that in the past in several cases, the petitioner charged tariff*

after accounting for liabilities in the capital cost, for many years without incurring actual expenditure. We do not find recurrence of these cases. We may add that as and when the liabilities are settled by the petitioner, it becomes entitled to additional capitalization and consequently revision of tariff"

11. The appellant was, therefore, directed by order dated 8.2.2007 to submit certain information in relation to capitalization cost on 08.02.2007 as under;

a. Actual cash flow on capital assets as on 15.08.2005(for Unit I) and 01.04.2006 (for Units I & II).

b. Expenditure capitalized in the books of account on the respective date against the actual cash outflow as per (a) above

c. Deferred liabilities that is, the liabilities on account of which there was no actual cash out flow but for which commitments were made and

d. Reasons for not making cash outflows in respect of the deferred liabilities against (c) above.

12. In response to above, the appellant submitted the following details;

Rs. In lakh

	01.04.2004	01.11.2004	01.04.2005	01.08.2005
Capitalized gross block as per accounts	260533.04	382150.98	386243.38	496109.79
Liabilities capitalized	31557.58	46648.70	42689.45	58522.21

13. The Commission allowed a sum of Rs.48276 lakh as capital cost of initial spares which is within the allowable limit of 2.5% of the original project cost in terms of regulation 17 of 2004. Thus, the Commission found that excluding the outstanding liabilities in respect of which payments were not made till the date of commercial operation of the generating station, the capitalized cost came to be Rs.228976 lakh, Rs.335471 lakh, 343515 Lakh and Rs.437588 lakh as on 01.04.2004, 01.11.2004, 01.04.2005 and 01.08.2005 respectively after reduction in IDC due to average method of repayment. Now, the appellant claimed an amount of Rs.94,453 lakh towards interest and FC based on FIFO (First in first out) method of repayment of loan. According to the appellant, the amount of IDC was Rs.66644 lakh and the admissible interest and FC based on FIFO method of repayment of loan is Rs.94298 lakh but the Commission rejected this method of repayment of loan and followed the average method of

repayment of loan. Accordingly, capitalized cost considered for the purpose of tariff computation has been worked out at Rs.228963 lakh as on 01.04.2004, Rs.335471 as on 01.11.2004, Rs.343515 lakh as on 01.04.2005 and Rs.437529 lakh as on 01.08.2005. respectively.

14. As regards debt equity ratio, the Commission followed clause (2) of the regulation 20 of the Regulations, 2004 which is 70:30. Thus as on 01.08.2005, an amount of Rs.131259 lakh was considered as normative equity.

15. The target availability of 80% was considered for recovery of full fixed charges and computation of fuel element in the working capital, while return on equity was determined @ 14% per annum.

16. As regards interest on loan, the Commission observed that in terms of regulation 20, the interest on loan should be computed loan-wise and minus the cumulative repayment. Now, as per the method adopted by the Commission for the tariff period from the year 2004 to 2009 normative repayment of loan or depreciation which is higher was considered as repayments. It was argued extensively before the

Commission by the appellant that this Tribunal in earlier cases held that depreciation cannot be linked with repayment of loan but has to be on normative basis only but the Commission did not accept the argument and followed their earlier orders passed in connection with different cases. Depreciation was calculated annually based on straight line method over the useful life of the asset and at the rates prescribed in terms of the Regulations. Advance against depreciation was restricted to the extent of the difference between cumulative payment and cumulative depreciation up to a certain year. As regards the expenses, the Commission followed the regulations and held that escalation of 4% was inbuilt in the normative O&M expenses specified by the Commission and accordingly it was worked out. Interest on working capital was on normative basis and it was arrived at Rs.4478 lakhs as in 2008-09 and the total annual fixed charges was arrived at Rs.86350 lakh.

17. With regard to `cut off' date, there was a lot of controversy in as much as the appellant in its affidavit dated 28.02.2007 claimed that the cut off date should be computed from the scheduled approved operation date of May 2006 and if such date is taken into

account the petitioner could be subjected to complete residual capital works up to 31.03.2008. But this contention was rejected by the Commission and it followed the clause IX of regulation 14 which defined the "cut off " date *as the date of first financial year closing after one year of the date of commercial operation of the generating station* and accordingly the Commission fixed 31.03.2007 as the ``cut off" date for the purpose of clause (1) of regulation 18. The Commission was not inclined to accept un-discharged liabilities and the amount of capital expenditure projected by the Appellant. The Commission differed with the appellant with respect to amount of opening capital cost which according to the appellant should be the amount as it stood on 01.04.2004. The Commission de-linked the depreciation with repayment of loan and also disallowed interest during construction on the notional loan.

18. Mr. Ramachandran, learned counsel for the Appellant broadly put forward the following points:

(i) Four units of NTPC were declared commercial on 01.08.2003, 01.03.2004, 01.11.2004 and 01.08.05

respectively. NTPC claimed capital cost based on the actual expenditure incurred on asset capitalized in accordance with Tariff Regulations, 2004 and in accordance with the practice consistently followed.

(ii) The Commission in its order dated 31.01.2008 did not consider the entire capital cost for the purpose of tariff. The Commission wrongly excluded the capital expenditure incurred by NTPC in respect of liabilities for which payments were not made till the date of commercial operation of the units III and IV of Talcher II. Further, the Commission in the impugned order has not considered the capital cost of existing Units I and II as admitted by the Commission prior to 01.04.2004. According to the appellant the capital cost as approved on 5th January, 1999 for Talcher STPS Stage II was Rs. 6532.61 crores and this has been subsequently reviewed, and approved revised cost estimate as on 7th July, 2007 is Rs. 5836.37 crores. Against this approved cost works have already been completed and capital as on 31st March, 2007 was Rs. 5045.85 crores. According to the appellant,

works for which orders have been placed will be completed in due course of time and will be claimed under deferred liabilities 'as and when this work would be put to use.' The order for the works amounting to Rs. 76 crores could not be placed by 30th March, 2007 for the reason that the rate quoted by BHEL was Rs. 65.74 crores but as the cost appeared to be high NTPC preferred to negotiate with BHEL and after negotiation cost was brought down to Rs. 56.53 crores and order was placed for purchase of total spare for Rs. 60.75 crores after 31.03.2007. However, orders were placed for minor civil and electrical works in plant and township and MGR areas amounting to Rs. 14.44 crores and these works are under execution.

(iii) NTPC had provided for repayment of loan based on the commercial operation of the station on First-in-First Out method so as to ensure that the higher cost loans are adjusted in the tariff of the generating station which comes into operation first and thereafter, the remaining loans are adjusted based on the commercial operation

date of the other generating stations thereby reducing the total interest liability for the Company and passing on the benefit of such reduced interest to the respondent purchasers. But, the Commission did not consider this aspect and reduced the interest during construction and in case of various units of Talcher II.

(iv) The Commission committed error in holding that depreciation available to NTPC is for repayment of loan and according to the appellant depreciation is available to utility whether any loan amount exists or not.

(v) According to the appellant, NTPC is entitled to additional capitalization of the capital expenditure within the original scope of work incurred after the date of commercial operation and up to the "cut off" date. The terms "additional capitalization", "cut off date" and ``date of commercial operation" have been wrongly understood by the Commission and the generating company cannot be subjected to penalty because of its efficiency in achieving commercial operation date before the scheduled approved date. The cut off date should be arrived at with

reference to scheduled approved date on the ground that the generating company was efficient and it had been in a position to commercial operation prior to the scheduled commercial operation date. Thus 31st March, 2007 should be recorded as "cut off" date so that additional capitalization could be included within the "cut off" date.

(vi) The tariff regulation 2004 came into force on 01.04.2004. NTPC began implementation of the Talcher super Thermal Power Station stage II in 1999 much before the notification of Tariff Regulations, 2004 came into force. Thus, Regulations, 2004, prescribing the cut off date should be given effect to only in case of those generating stations in which the work for establishing the generating stations which commenced on or after 01.04.2004 but not for those where work commenced prior to Regulations, 2004. Two units were completed and declared commercial by 01.04.2004 and the works in respect of the remaining two units were substantially implemented and were ready to commence therein

commercial operation within a period of one year or so. The Central Commission did not allow annual escalation on maintenance spares as part of working capital as allowed by the Regulations.

(vii) The Commission was not right in considering the opening capital cost of the existing units as on 01.04.2004 as different from the capital cost admitted by the Central Commission prior to 01.04.2004, whereas CERC Regulations 2004, under Proviso 17, provides that the capital cost admitted by the Commission prior to 01.04.2004 shall form the basis for determination of tariff. The details of the capital cost of Talcher-II not considered by the Central Commission and reduction in the interest during construction for the above station are as under:

Details	**1.4.2004**	**1.11.2004**	**1.4.2005**	**1.8.2005**
Capitalized Gross Block as per Accounts of NTPC	260533	382151	386243	496110
Liabilities included in above on annual basis	31557	46649	42689	58522
Reduction in IDC by CERC due to avg. method of repayment	13	31	39	59

Capitalized cost as allowed by CERC	228963	335471	343515	437529

(viii) The Commission was not right in making any reduction in the cumulative repayment up to 31.03.2004 while considering the reduced opening gross loan of the existing unit as on 01.04.2004. For computation of interest on loan with effect from 1st April 2004 the Commission considered the reduced gross loan as on 1st April, 2004 as consequential effect of reduced opening capital.

(ix) The commission was not right in disallowing escalation @6% per annum on maintenance spares as part of the working capital from the date of commercial operation of the units as provided in Regulation 21 (v)(a)(iv).

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19. Mr. M.G. Ramachandran, learned Counsel for the appellant raised a volley of questions covering the areas of dispute between the appellant and the Respondent No. 1 and has cited a good number of decisions of the Supreme Court as also of this Tribunal in identical matters which we will presently consider. While none has appeared

on behalf of Respondent No.1, Mr. P.R. Kovilan learned counsel appeared for Respondent No.3 namely Tamil Nadu Electricity Board(TNEB).

20. According to Mr. P.R. Kovilan, Learned Counsel of the Respondent No.3, un-discharged liabilities are trade finance given to the purchaser by a seller which normally carries 0% rate of interest and considering the same as equity and order for 16% return along with Income Tax or weighted average rate of interest would be prejudicial to end consumer. With respect to the capital cost, it has been argued that equity deployed in excess of 30% of the project cost is to carry notional interest and the same is to be added to the project cost. With reference to the Regulation 17 of the CERC(Terms and Conditions of Tariff) Regulations, 2004 which is applicable for the period between 2004-09, it has been submitted that the terms "shall form the basis" does not mean that the same is to be considered literally for the purpose of determination of tariff. With reference to the "cut off" date, the Respondent No. 3 defends the order of the Commission.

21. Mr. Ramachandran assiduously argued that in view of the decisions of this Tribunal passed in two sets of appeals being 151/07 and 152/07 relating to other generating stations of the appellant, the question of what is called un discharged liability is no longer *res integra*. He took recourse to *Black's Law Dictionary, 7th Edition that defines the term `incur' as-`to suffer or to bring on oneself' and also Law Lexicon (P Ramanatha Aiyar, 1997 Edition)* which defines incur as -`to become subject` to or liable for by an act or operation of law. Mr. Ramachandran also relied on the decision in *Madras Industrial Investment Corn. Ltd.-v-CIT(1997)4 SCC 666, Indira Nehru Gandhi-v- Raj Narain 1975 (Supp) SCC 1, CIT, Gujarat-v-Tejaji Farasram Kharawalla Ltd. (1968) 1 SCR, 37, Chakoo Bhai Ghelabhai –v-State of Orissa(1956)7 36*, to drive home his point that an expenditure is not necessarily confined to the money which has been actually paid out but covers the liability which has accrued or which has been incurred even though it may have to be discharged at a future date.

22. To appreciate the concept of ``un-discharged liabilities'', it will not be out of place to put on record Regulation 17 and 18 of the CERC Regulations 2004 as under:

"17. Capital cost- Subject to prudence check by the Commission, the actual expenditure incurred on completion of the project shall form the basis for determination of final tariff. The final tariff shall be determined based on the admitted capital expenditure actually incurred up to the date of commercial operation of the generating station and shall include Capitalized initial spares subject to the following ceiling norms as a percentage of the original project cost as on the cut off date:

(i) *Coal- based ignite-fired generating set-2.5%*
(ii) *Gas Turbine/Combined Cycle generating stations – 4.0%*

Provided that where the power purchase agreement entered into between the generating company and the beneficiaries provides a ceiling of actual expenditure, the capital expenditure shall not exceed such ceiling for determination of tariff:

Provided further that any person intending to establish, operate and maintain a generating station may make on application before the Commission for `in principle' acceptance of the project capital cost and financing plan before taking up a project through a petition in accordance with the procedure specified in the Central Electricity Regulatory Commission (Procedure for making application for determination of tariff, publication of the application and other related matters) Regulations, 2004, as applicable from time to time. The petition shall contain information regarding salient features of the project including capacity, location, site specific features, fuel, beneficiaries, break up of capital cost estimates, financial package, schedule of commissioning, reference price level, estimated completion cost including foreign exchange component, if any, consent of beneficiary licensees to whom the electricity is proposed to be sold etc.

Provided further 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 prudence check on the actual capital expenditure:

Provided further that incase of the existing generating stations, the capital cost admitted by the Commission prior to 1.4.2004 shall form the basis for determination of tariff(emphasis provided)

Note

Scrutiny of the project cost estimates by the Commission shall be limited to the reasonableness of the capital cost, financing plan, interest during construction, use of efficient technology, and such other matters for determination of tariff.

18. Additional capitalization : (1) The following capital expenditure within the original scope of work actually incurred after the date of commercial operation and up to the cut off date may be admitted by the Commission, subject to prudence check:

(i) Deferred liabilities:

(ii) Works deferred for execution:

(iii) Procurement of initial capital spares in the original scope of work, subject to ceiling specified in regulation 17:

(iv) Liabilities to meet award of arbitration or for compliance of the order or decree of a court: and

(v) On account of change in Law.

Provided hat original scope of work along with estimates of expenditure shall be submitted along with the application for provisional tariff.

Provided further that a list of the deferred liabilities and works deferred for execution shall be submitted along with the application for final tariff after the date of commercial operation of the generating station.

(2) Subject to the provisions of clause (3) of this regulation, the capital expenditure of the following nature actually incurred after the cut off date may be admitted by the Commission, subject to prudence check:

(i) Deferred liabilities relating to works/services within the original scope of work:

(ii) Liabilities to meet award of arbitration or for compliance f the order or decree of court:

(iii) On account of change in Law:

(iv) Any additional works/services which have become necessary for efficient and successful operation of the generating station, but not included in the Original project cost and

(v) Deferred works elating to ash pond or ash handling system n the original scope of work.

(3) Any expenditure on minor items/assets like normal tools and tackles, personal computers, furniture, air-conditioners, voltage stabilizers, refrigerators, fans, coolers, TV, washing machines, heat-convectors, carpets, mattresses etc. brought after the cut off date shall not be considered for additional capitalization for determination of tariff with effect fr5om1.4.2004.

Note

The list of items is illustrative and not exhaustive.

(4) Impact of additional capitalization in tariff revision may be considered by the

Commission twice in a tariff period, including revision of tariff after the cut off date.

Note 1

Any expenditure admitted on account of committed liabilities within the original scope of work and the expenditure deferred on techno-economic grounds but falling within the original scope of work shall be serviced in the normative debt-equity ratio specified in regulation 20 (emphasis supplied)

Note 2

Any expenditure on replacement of old assets shall be considered after writing off the gross value of he original assets from the original project cost, except such items as ae lised in clause (3) of this regulation.

Note 3

Any expenditure admitted by the Commission for determination of tariff on account of new works not in the original scope of work shall be serviced in the normative debt-equity ratio specified in he regulation 20.

Note 4

Any expenditure admitted by the Commission for determination of tariff on renovation and modernization and life extension shall be serviced on normative debt-equity ratio specified in regulation 20 after writing off the original amount of the replaced assets from the original project cost"

23. It has been argued that when a capital asset is purchased the liability is assumed. Such liability is not deferred. Only the payment

in respect of the same is deferred. Thus the words "actually incurred" containing in the Regulation 17 of the Act would refer to the liabilities incurred and the same would not refer to the actual cash outflow. We find that in appeal No. 151 and 152/07 NTPC Vs CERC reported in 2008 ELR (APTEL)916, this Tribunal dealt with the issue in the following way:

> *"17. This Regulation is fully comprehensible with the above understanding of the word ``actually incurred". Regulation 18 is dealing with capital expenditure incurred after the date of commercial operation and up to the cut off date. The nature of such capital expenditure can be: deferred liability and work deferred for execution and the like. Such capital expenditure which were contemplated for being under taken originally but was deferred and actually undertaken after the date of commercial operation will be treated as additional capitalization. In regulation 18, the word repeatedly used is "deferred liability" Obviously deferred liability is the liability which has not yet been assumed. When a capital asset is purchased the liability is assumed. Such liability is not deferred. Only the payment is deferred. Regulation 18 is not dealing with deferred payments but is dealing with deferred liabilities. Work deferred for execution means works not already taken. Certain works, within the original scope of work may not have been undertaken before the date of commercial operation. If it is so done, the same will be available for recovery through tariff under Regulation 18. It must however be ensured that no capital expenditure which is claimed under Regulation 17 is claimed again as Additional Capitalization under Regulation 18.*
>
> *18. There is yet another angle to this aspect. As soon as the plant is put into operation the depreciation will begin. Even if 10% of the capital cost for the plant is retained with the intention of payment on a subsequent date depending upon satisfactory performance of the plant, the capital asset that depreciates is not the 90% of it but the whole or 100% of it. There is no reason why the generating company should be deprived of its entitlement to recover such depreciation on 100% value of the asset simply because a part of the*

value has been retained to ensure efficient performance of the capital asset.

19. We are, therefore, of the opinion that the entire value of the capital asset, as soon as the same is put into operation is recoverable by way of capital cost under Regulation 17 itself, not withstanding the fact that the part of the payment for the capital asset has been retained."

24. In NTPC Vs CERC reported in 2009 ELR (APTEL) 337 it was held inter-alia that Regulation 17 makes it clear that actual capital expenditure on completion of project i.e. up to the date of commercial operation is to be the basis for determination of tariff and it does not deal with deferred liabilities, while Regulation 18 uses the expression `deferred liability' but not the payment. Thus it was held that the words 'actual expenditure' incurred contained in Regulation 17 refer to the liabilities incurred and the same would not refer to the actual cash outflow.

25. Having considered the decisions of the Hon'ble Supreme Court as cited at paragraph 21 of this judgment and the decisions of the this Tribunal it has to be stated in favour of the appellant that the findings of the commission while interpreting Regulations 17 and 18 does not appear to be sound. In view of the settled legal position, we feel

comfortable to say in agreement with the appellant and decide the same in favour of the appellant.

26. The issue as discussed above is, therefore, linked with the question as to what would be opening capital cost as on 01.04.2004. According to the Appellant, the gross block as on 01.04.2004 was Rs.260623 lakhs and as on 01.08.2005 it came to Rs.496110 lakh. Mr. Ramachandran argued that there was no reason to reject the amount of capital cost as was admitted by the Commission prior to 01.04.2004 as the basis for determining the tariff. Mr. Ramachandran lays emphasis on the lone proviso to Regulation 17 which means thus :

> *"Provided further that in case of existing generating sttions, the capital cost admitted by the Commission prior to 01.04.2004 shall form the basis for determination of tariff."*

27. From para 21 of the Judgment of the Commission , it appears that Central Commission has considered the capital gross block as per the account as on 01.04.2004 of Rs.260533 which has been reduced by the sum of Rs.31557 lakh on account of the liabilities included in the above on an annual basis of Rs.31557 lakh and arrived at the capital

cost actually incurred as on 01.04.2004 at Rs.228976 lakh. This sum of Rs.228976 lakh has been taken as the capitalized cost actually incurred after deduction of liabilities on annual basis. If the liabilities accrued or undischarged liabilities are included, the opening cost as on 01.04.2004 would be Rs.260533 lakh as claimed by NTPC. We find ourselves in agreement with Mr. Ramachandran that subject to prudence check, if the claimed liabilities which pertain to a pure question of fact really do amount to what is called undischarged liabilities then in terms of regulation 17 they have to be admitted as capital cost and accordingly, the capital cost needs to be re-determined by the Commission.

28. With respect to disallowance of interest during construction the NTPC appealed to the Commission to adopt FIFO method which the Commission did not agree to. The point was examined earlier by this Tribunal and in NTPC Vs CERC & Ors. reported in *2008 ELR(APTEL) 0916* it was held as follows:-

> "21. *The other issue in the matter relates to repayment of loan and interest during construction. The Appellant NTPC has several generating stations. It takes loans on the strength of corporate balance sheet and allocates the borrowed funds to its generating stations instead of borrowing separately for each project. When a*

plant is under construction, the appellant is entitled to interest during Construction (IDC for short) on the funds which had to be borrowed. The repayment would begin as per terms of the loan agreement. The appellant claimed that it be allowed to firstly adjust the entire installments falling due to the lender in the debt repayment of the generating projects under commercial operating and not to apportion and allocate the same to the project under construction. According to NTPC this would allow costliest loan to be retired fist fully thereby reducing the interest on outstanding debts. This method has been described as First in First out method (FIFO).The Commission rejected the FIFO method. Appellant in the appeal asked for implementation of its FIFO method. However, during arguments the appellant has given up the claim for adopting FIFO method for repayment of corporate loan. However, it is contended on behalf of the appellant that if loans repaid are attributed proportionately to certain projects under construction for which tariff is yet to be fixed and revenue is yet to be earned, such repayment should be deemed to have been made out of the internal or borrowed funds. NTPC submits that if the repayment of loan taken by NTPC is accounted for during the period prior to the commercial operation of the generating stations, in the ratio of allocation of loan to respective generating stations, the amount of repayment should be considered as having come from internal sources of NTPC or from other borrowings. This submission is quite logical in as much as before the date of commercial operation the project under construction does not earn any revenue and does not generate any fund from which loan can be repaid. In such situation if the project under construction repays a part of the loan, the funds for the same has to come either from the NTPC i.e. owner or from funds borrowed from other sources. In either case such sum will entail a return in the form of interest.

22. The NTPC submits that deployment of such internal sources of NTPC for the purpose of repayment of loan of the project under construction before the date of commercial operation should be considered as deemed loan from NTPC to the project. Accordingly, NTPC should be entitled to claim notional interest on such loan as interest during construction.

23. The respondents do not dispute this proposition. On behalf of the Respondents No.7 TNEB, it s contended that funds deployed for repayment of loan during construction should earn interest only if such amount is actually borrowed and not if the amount comes

from NTPC's own sources. This, however, is not a correct view, if NTPC employs its own funds, over and above equity, there is no reason why NTPC should not earn interest thereon.

24. We, therefore, find that the Commission's decision not to follow the FIFO method does not call for any interference but that repayment assumed for generating station during the period prior to the date of commercial operation be deemed as loan from NTPC and interest during construction be allowed on such loans"

29. Of course, though this Tribunal in another decision in NTPC Vs CERC & Ors. reported in 2009 ELR(APTEL) 337 held that "The First in First Out' method cannot be adopted it held however that the deployment of internal resources of NTPC which is in addition to the equity contribution should be considered as a deemed loan from the NTPC to the project. It has been argued that the Commission has not considered this aspect and has reduced the interest during construction in the case of various units of Talcher II and it was but logical to give effect to adjustments for repayment of loan taken by the NTPC commonly for funding two or more generating stations while not accepting the IDC as claimed by the appellant. In view of above ruling of this Tribunal without interfering with the Commission's decision not to follow the FIFO method, we direct the Commission to allow interest on deemed loan deployed from internal resources of NTPC in addition to equity contribution in IDC.

30. As regards the question whether depreciation can be considered as `deemed loan repayment', it has been considered and held by this Tribunal in a batch of 19 appeals beginning with the Appeal No. 139/06 (NTPC vs CERC & Ors) that the computation of outstanding loan will be on normative basis only (instead of normative or actual whichever is higher). It has been decided therein that computation of outstanding loan will be on normative basis only and there cannot be any question of adjustment of the deprecation amount as deemed repayment of loan. To quote this Tribunal's findings(ibid) :

> *"In the orders of this Tribunal dated November 14, 2006 and January 24, 2007 it has been laid down that the computation of outstanding loan will be on normative basis only (instead of normative or actual whichever is higher) In view of this there is no question of any adjustment of the depreciation amount as deemed repayment of loan.*
>
> *It is to be understood that the depreciation is an expenses and not an item allowed for repayment of loan. If a corporation does not borrow, it would not mean that the corporation will not be allowed any depreciation. Depreciation is an expense it represents a decline in the value of asset because of use, wear or obsolescence. The Accounting Principles Board of USA defines depreciation as under:*
>
> *"The cost of a productive facility is one of the costs of the service it renders during its useful economic life. Generally accepted accounting principle, require that this cost can be spread over the expected useful life of the facility n sch a way as to allocate it as equitably as possible to the periods during which services are obtained from the use of the facility. This procedure is known as depreciation accounting, a system of accounting which aims to distribute the cost or other basic value of tangible capital assets,*

less salvage (if any), over the estimated useful life of the unit(which may be a group of assets). In a systemic and rational manner. It is a process of allocation, not of valuation".

It is well established that the depreciation is an expense and therefore, it cannot be deployed for deemed repayment of loan. In this view of the matter the CERC shall need to make a fresh computation of outstanding loan in the light of the aforesaid observation".

31. The Hon'ble Supreme Court in DERC v. BSES Yamuna Power Limited & others(2007) 3 SCC 33 has held inter-alia as under:

"40 Depreciation reduces the distributable profit without reducing the cash profit. The difference between the two is a sum which the company has to retain to meet the cost of replacement in future. We may clarify that depreciation is ordinarily not a `source of fund' under Commercial Accounting, however, as held by this Court in the case of Ahmedabad Miscellaneous Industrial Workers' Union vs Ahmedabad Electricity Co. Ltd. –AIR 1962 SC 1255, in the context of the Electricity Supply Act, depreciation enables the utility to work out the charges to be recovered from consumers for supply of electricity, one has to follow the provisions of the schedule to the said Electricity Act and that one has not to follow the provisions of the income-tax Act while calculating depreciation as one the items of expense under the Electricity Accounting."

32. Again Hon'ble Supreme Court's observations at para 42 of the decision is as follows*:*

"In the present case, it has been held by DERC that since the DISCOMs herein were not obliged to redeem debt (as they had not undertaken any loans), they were not entitled to the higher rate of depreciation. This assumption of DERC is wrong. There is a difference between the concept of Depreciation and the concept of Advance Against Depreciation (AAD). In the case of AAD, loan repayment may be one of the relevant factors. In the present case, as stated above, we are concerned with the reduction of authorized

expenditure from 6.69% to 3.75%. In the present case, we are concerned with the reduction in rate of 6.69% to 3.75%. Therefore, in the case of reduction of authorized expenditure (depreciation) repayment of loan is not the relevant factor. Before concluding, we may state hat the basic object of providing depreciation is to allocate he amount of depreciation of an asset over its useful life and not actual life so as to exhibit a true and fair view of the financial statement of an enterprise. Useful life is a period over which a depreciable asset is expect to be used. Useful life of an asset in a capital intensive industry is generally shorter than its physical life. Useful life is pre-determined by contractual limits or by amount of extraction or consumption dependent on the extent of use and physical deterioration on account of wear and tear which depends on operational factors such as the number of shifts, repair and maintenance policy of the utility and reduced by obsolescence arising from technological changes, improvement in production method etc. In the present case, DERC has not considered the difference between the physical life of an asset and the useful life of the asset."

33. In fact, this Tribunal followed the decision of the Hon'ble Supreme Court and we are unable to understand what led the Commission to depart from the decision of the judicial authorities. However, the amount of depreciation is to be allowed irrespective of the question whether there is any liability to pay loan or not. In view of above we decide this issue in favour of the appellant and direct the Commission to make a fresh computation of outstanding loan in light of the above observations.

34. With regard to the cost of maintenance spares, it has been argued that the Commission has not allowed annual escalation on

maintenance spares as part of the working capital as permissible by the Regulations. The amount of maintenance spares claimed was Rs.3978 lakh and the figure came to Rs.6382 lakh in the year 2008-09. The Commission calculated it, to begin with, at Rs.2267.86 as on 1.4.2004 and worked it out at Rs.5056.31 in the year 2008-2009. Now, this point was examined by the Tribunal in the batch of 19 appeals (NTPC vs CERC & Ors) and it was observed:

> *"A. it is clear from the abovementioned Clause 18 of the CERC Regulations that additional capitalization after the date of commercial operation is recognized as part of the capital expenditure Historical cost does not literally mean that the cost on the date of commercial operation. The term historical cost is used so as to distinguish it from `book value' or `the replacement cost'. The cost of maintenance spares limited to 1% of the historical cost corresponds to the plant and equipment and installations which are required to be maintained. If the cost of the additional equipment is not included in the historical cost, how spares for the additional equipment be procured for maintenance of the additional equipment. In this view of the matter, the CERC needs to examine afresh in the light of the aforesaid observations".*

35. Further, this Tribunal in Appeal No. 54 of 2009 held as under:

> *"6. The second point relates to the disallowance of cost of maintenance Spares. According to the Learned Counsel for the Appellant, the Central Commission has not allowed the additional cost in regard to the maintenance spares corresponding to the additional capitalization while computing the historical capital cost. It is strenuously contended by the Learned Counsel for the Appellant that the Central Commission has permitted the cost of spares as per the capital cost frozen on the date of commercial operation without considering the additional capitalization undertaken from the date of he commercial operation as allowable under the Tariff Regulations 2004. It s further pointed out that this*

point also has been covered in the Judgment in Appeal No. 139 of 2006 dated 13.6.2007. in the Judgment, it has been held that the cost of maintenance spares needs to be calculated on the total capital cost inclusive of additional capitalization."

36. However, we find that the rulings quoted by learned counsel for the appellant relate to cost of maintenance spares on additional capitalization and is of no use in the present Case. In the present case the issue is non-allowance of 6% escalation on amount of maintenance spares after the date of commercial operation of the power station as a part of working capital. However, we find that in the impugned order the Commission has allowed maintenance spares @1% of admissible capital cost escalated at the rate of 6% per annum. Thus the impugned order does not need any intervention with regard to escalation in cost of maintenance and spares.

37. The question of Principle of "Cut Off Date" which in the circumstances has now been an academic one has been dealt with by the Commission in a manner different from what the appellant wished to have it determined.

Regulation 14(ix) and 14(x) of the Regulations 14 deals with cut off date and date of commercial operation as follows:

> "14 (ix) *Cut off Date means the date of first financial year closing after one year of the date of commercial operation of the generating station:*
>
> *14(x) `Date of Commercial Operation' or `COD' in relation to unit means the date declared by the generator after demonstrating the Maximum Continuous Rating (MCR) OR installed Capacity (IC) through a successful trial run after notice to the beneficiaries and in relation to the generating station the date of commercial operation means the date of commercial operation of the last unit or block of the generating station".*

38. According to the Appellant, it is possible for a generating company to declare the station commercially operational prior to completion of all works forming part of the initial scope of work. This is because the incurring of certain expenditure like expenditure on ash dyke, ash pond, MGR system etc. can be postponed till after the declaration of commercial operation. This is in the interest of the beneficiaries of power as well as consumers at large as they get electricity on an earlier date without having to contribute to the capital expenditure which the generating station may incur on other capital assets like ash dyke, ash pond, etc., mentioned above. It is also possible for a generating company to declare a plant to be commercially operable much before the scheduled commercial operation date if the generating company is efficient. In the present

generation station case, NTPC declared the various units of the generating station commercially operational much before the scheduled commercial operation date as under:

Unit	*Scheduled Commercial Operation Date*	*Actual Commercial Operation Date*
No.1	*February 2004*	*1.8.2003*
No.2	*November 2004*	*1.3.2004*
No.3	*August 2005*	*1.11.2004*
No.4	*May 2006*	*1.8.2005*

39. We find that in the Tariff Regulation 2001 there was no cut off date for the expenditure to be incurred in respect of generating station after being declared commercially operational. It has been argued by the appellant that the Tariff Regulations 2004 came into force on 1.4.2004 having been notified by the Commission on 26.3.2004. The appellant had planned and began implementation of Talcher STPS Stage II in the year 1999 which was much before the notification of the above Tariff Regulations, 2004 and thus the implementation of the project was taken up before the Notification of

the Tariff Regulations, 2004 prescribing the cut off date to be calculated and given effect to only in the case of those generating stations where works commenced on or after 26.3.2004 or 1.4.2004.

40. True, it is only in the Regulation 2004 that concept of cut off date has been introduced. The cut off date means the date of first financial year closing after one year of the date of commercial operation of the generating station. We are unable to accept the submission of the appellant that cut of date must not relate invariably to the actual date of commercial operation because the language of regulations is clear and explicit. Absence of the cut off date in Regulations 2001 does not bring about any benefit to the appellant because it is plain that the date of commercial operation in relation to a unit means the date declared by the generator after demonstrating the maximum continuous rating (MCR) a successful trial run. Therefore, irrespective of the question whether concept of cut off date was or was not there in Regulations 2001, the position does not make any difference.

41. In the instant case, the Appellant has four units of the generating station. In case of generating station, the date of commercial operation in terms Regulations 2001 means the date of commercial operation of the last unit. Thus, what is called scheduled commercial date is the date ideally fixed for putting the concerned unit under commercial operation. Such an ideal date, the date targeted, may turn out to be a reality, may not be so. The units may be put under commercial operation ahead of scheduled date of commercial operation, or after that date. The date of scheduled commercial operation is the date ideally taken to be one by which the unit is expected to be commissioned. There may be a failure to adhere to that date, there may be a success also, and success may come before that date also. Therefore, in terms of the regulations the date of commercial operation must be to all intents and purposes the actual date of commercial operation.

42. We are unable to accept the submission of Mr. Ramachandran that the scheduled commercial date should be the basis for determining the cut off date. As already observed, the provision of the regulations admits of no confusion and ambiguity. Where the

plain meaning of the regulation is clear, no contrary reasoning is admissible.

43. Mr. Ramachandran has submitted that Commission has power to remove difficulties. Mr. Ramachandran referred to *Hindustan Steel Limited Vs A.K. Roy(1969) 3 SCC 513, NTPC v/s MP State Electricity Board* which is the decision of this Tribunal reported in *2007 ELR (APTEL)7 and MP transmission Co. Ltd. v/s Torrent Power Ltd. & Ors., 2009 ELR (APTEL) 124.* It has been argued that in a similar situation in the past the Central Commission conceded to the submissions of NTPC with regard to another generation station at Ramagundam Super Thermal Power Station Stage III in petition No. 10/2006 on 06.02.2007. In case of Ramagundam Stage III, the generating station was declared under commercial operation on 25.03.2005, ahead of scheduled date of commissioning of 16.12.2005. The Commission had held that the petitioner could defer the Commissioning of the plant by about a week and in that case the cut off date for capitalization of additional expenditure would have automatically been extended up to 31.03.2007 instead of 31.03.2006. The Commission considered it a fit case for invoking its power under

Regulations 12 and 13 of Regulations, 2004 for removal of difficulty or relaxation of the relevant provision. In the impugned order the Commission has not agreed to extend the cut off date for the reason that the first unit of the generating station was Commissioned in August, 2003 and the date of commercial operation of the generating station as a whole was 01.08.2005, which is about one and a half year after the notification of the Tariff Regulations, 2004.

44. The Appellant has submitted that the orders for certain works for a sum of Rs. 76 crores could not be placed by 31.03.2007 due to detailed review of initial spares. After detailed exercise enquiry for some of the spares was issued in July and September, 2006 against which offers were received from BHEL in September and November, 2006. The order could be placed after negotiation and brining down the cost only after 31.03.2007. Also some orders relating to Civil Works were placed after 31.03.2007. It has been argued by the learned counsel for the Appellant that the present case is a just and proper case for exercising the Power to Relax.

45. We have examined the details of the items where the orders were placed after the cut off date submitted by the appellant. These are essentially the initial spares required for the power plant. In view of the explanation offered by the appellant we are convinced that it is a fit case for consideration of the Commission to exercise its power to relax under the Tariff Regulations, 2004. Accordingly we remand this matter to the Commission to consider the request of the appellant to extend the cut off date appropriately in exercise of its power to relax.

46. Accordingly, on the following issues we are of the opinion that the findings of the Commission are not justifiable and they required to be re-examined in light of the settled legal position as have been discussed in the preceding paragraphs of this judgment:

(i) Undischarged liabilities.

(ii) Opening capital costs as on 01.04.2004 having regard to the proviso to regulation 17 of the Regulations, 2004.

(iii) Disallowance of interest during construction on notional loan.

(iv) Treating depreciation as deemed loan repayment

47. With regard to the "cut off" date the we remand the matter to the Commission to consider the submissions of the appellant to extend the cut off date appropriately in exercise of its power to relax under the Tariff Regulations, 2004.

48. With regard to escalation in cost of maintenance spares in working capital we are in agreement with the findings of the Commission.

49. The result of this discussion as aforesaid would be that the Respondent No. 1 is to re-examine the case and pass a fresh order on the issue referred to above in the light of the observations made in the body of the judgment.

50. Accordingly, we allow the appeal in part, set aside the order dated 31.1.2008 passed in Petition No. 179/04 to the extent as indicated above and remand the matter back to the Commission for re-examination on the issues as above so as to have a fresh decision reached in accordance with the law after hearing the parties.

(Justice P.S. Datta) **(Rakesh Nath)**
Judicial Member **Technical Member**

Dated : 18th August, 2010

REPORTABLE/NON-REPORTABLE.

PK