Before the Appellate Tribunal for Electricity
(Appellate Jurisdiction)

Appeal No. 151 of 2009 & IA No. 265 of 2009

Dated : 23rd December, 2009

Coram : Hon'ble Ms. Justice Manju Goel, Judicial Member
Hon'ble Mr. H.L. Bajaj, Technical Member

IN THE MATTER OF :-

Dodson-Lindblom Hydro Power Ltd.
6, Shiv Wastu, Tejpal Scheme Road No.5,
Vile Parle (E),
Mumbai – 400 057 … Appellant(s)

Vs.

1. **Maharashtra Electricity Regulatory Commission**
World Trade Centre No.1, 13th Floor,
Cuffe Parade, Colaba,
Mumbai – 400 001

2. **M/s. Maharashtra State Electricity Distribution Co. Ltd.**
Prakashgad, Bandra (E),
Mumbai – 400 051 … Respondent(s)

Counsel for the Appellant(s) : Mr. M. G. Ramachandran,
Mr. Anand K. Ganesan,
Ms. Swapna Seshadri and
Mr. Saurabh Mishra,
Advocates

Counsel for the Respondent(s) : Mr. Buddy A. Ranganadhan,
Advocate for Resp. No.1, MERC

Mr. Abhishek Mitra and
Mr. Raunak Jain, Advocates
for Resp. No.2, MSEDCL

J U D G M E N T

Justice Manju Goel, Judicial Member

This appeal challenges the order of Maharashtra Electricity Regulatory Commission (the Commission for short) dated 08.07.09 determining the tariff for the Bhandardara-II Hydro Power Project (BHEP for short) run by the appellant. BHEP was commissioned in 1999. It has a 34 MW hydro power facility on river Pravara located about 12 km downstream from Bhandardara-I hydro power facility. The station is operated on water released from Bhandardara-I and the sluices of the Bhandardara Dam. Water released from Bhandardara-II is taken for irrigation through canals having total capacity of 1045 cusecs. BHEP-II was being operated only at a partial load of 18 MW as downstream canals were not capable of carrying the full discharge of 2700 cusecs required for full capacity operation. The plant has been designed as peaking power station to operate for 3 hours each during morning and evening peak taking into consideration downstream Nilwande Dam. However, the construction of Nilwande Dam had been delayed due to shortage of funds and accordingly the capacity of BHEP-II was not being fully utilized. The Government of Maharashtra decided to invite bid to make over the project to a private entrepreneur. The cost of the

project was assessed at Rs.92 Crores. The appellant M/s. Dodson Lindblom Hydro Power Project Ltd. (DLHPPL) submitted a bid which was accepted by Government of Maharashtra. As per the bid condition, Rs.60 Crores was required to be paid upfront and additional installments of Rs.262.70 Crores during the lease period of 30 years such that NPV of all payments was Rs.92 Crores as per schedule given in Appendix 'B' to the tender. The energy generated from BHEP-II was to be sold to Maharashtra State Electricity Board (MSEB). The MSEB submitted a proposal to the Commission for approval of tariff from BHEP-II at 3.05 per kWh for the base year with an annual increase of 5% intending to enter into a long term PPA for 30 years. The Commission observing that the project was working only at 18 MW capacity treated the project as a Small Hydro Project (SHP) till the height of Nilwande Dam was raised to 610/613 meters above Mean Sea Level and directed that the SHP tariff shall be applicable for Bhandardara-II till the height of the Nilwande Dam was raised to 610/613 meters. At that time the SHP tariff was 2.84 per kWh in the base year with 3 percent increase per year. The appellant entered into a PPA for 20 years as per the order of the Commission, mentioned above, dated 10.04.06. On 19.12.06 the appellant took over the project on payment of Rs.60 Crores. This was accomplished after the financial closure and getting the loan of Rs.54.62 Crores sanctioned by financial institutions. On the tariff, as determined for SHP projects, the appellant generated and supplied power to MSEDCL (successor of MSEB) till March

2009. On receiving a communication from the Government of Maharashtra that the Nilwande Dam could be completed by June, 2008, the appellant on 28.05.2008 had submitted petition No. 27 of 2008 seeking determination of tariff on regular basis for the BHEP-II project. The Dam reached the height of 610/615 meter level on 07.07.08. After a technical validation session the appellant was required by the Commission to file a modified application which was submitted on 30.01.09. The Commission passed the impugned order on 08.07.09.

02) The appellant has challenged the tariff determined vide order dated 08.07.09 being aggrieved by the following disallowances:

(i) the appellant had contributed Rs.18 Crores towards the equity and borrowed a loan of Rs.54.62 Crores. The Commission treated the capital cost in the debt equity ratio of 91:09 and disallowed the ratio of 70:30 which is the normative debt equity ratio as per the Maharashtra Electricity Regulatory Commission (Terms & Conditions of Tariff) Regulations, 2005, hereinafter referred to as the Regulations.

(ii) The preoperative expenses of Rs.9.75 Crores which the appellant claimed to have spent towards capital

cost of the project were disallowed by the Commission. The appellant claims to have spent preoperative expenses for securing the debt finance for the BHEP-II project which included the processing fee paid to the banks and financial institutions, commitment fees, fees paid to financial, technical and legal consultants, guarantee fee paid to the banks and Government of Maharashtra, stamp duty for lease deed, security documents and registration etc. and fees paid to the Registrar of Companies.

(iii) The Commission did not grant the full amount claimed towards renovation and modernization. The appellant contends that the appellant was required to make provision for a spare runner as an essential capital spare. The Commission did not approve of the cost of spare runner as cost towards R&M. The Commission considered for capitalisation, during 2007-08, only Rs.61.14 Lacs out of Rs.100.53 Lacs and for 2008-09 Rs.17.30 Lacs out of Rs.58.25 Lacs while the balance was attributed to routine O&M cost.

(iv) The Commission did not allow any payment for generation above design energy and therefore, the appellant is being discouraged from generating secondary energy which is leading to a situation where water flow is allowed to be wasted without generation although secondary energy could be generated at the lowest variable energy rate in any power station in Maharashtra which is about 1.19 per kWh.

(v) The Commission considered auxiliary consumption only at the normative level on 1.2% of gross generation although the actual auxiliary consumption was 1.44%. The appellant is aggrieved that the Commission ignored the fact that the power station being a well type underground power station and on account of presence of upstream and downstream reservoir leading to water seepage inside the power house requires continuous running of drainage and de-watering pumps.

(vi) The Commission has made the unscheduled interchange rates applicable to the appellant as per the Regulations. The appellant contends that the Regulations do not deal with the provision for

irrigation based hydro power plant where scheduling based power requirements is not possible and BHEP-II being a must run type plant unscheduled interchange rates should not be made applicable.

(vii) The appellant has expressed grievance as the Regulations require pro rata reduction of recovery of annual fixed charges in case the generating station achieves capacity index below the normal levels. The appellant contends that for irrigation based projects the maximum available capacity is highly dependent on the level of Nilwande Dam as well as Randha Weir and, therefore, incentive and dis-incentive for failure to achieve capacity index needs to be re-worked.

(viii) Coming to declaration of capacity, the appellant contends that the Regulations in this regard do not provide as to how to demonstrate the declared capacity for irrigation based power project where the effective head of turbine reduces depending upon the requirement of irrigation. The appellant contends that the declared capacity should be based on maximum available capacity.

(ix) O&M expenditure is allowed as a percentage of capital cost. The Commission has treated the transfer value of the project as the capital cost. The appellant contends that the Commission should take the real value of the project which would include Interest During Construction (IDC). The O&M cost has to be determined on the value of the project including transfer value of Rs.93.26 Crores as well as IDC.

(x) The tax component known as Minimum Alternate Tax (MAT) which is required to be paid mandatorily has not been fully considered by the Commission as a pass through. The Commission has allowed only 11.99% although the MAT rate has increased to 16.995% in the year 2008-09. The appellant wants that the increased payment of MAT be also allowed to be recovered.

(xi) The appellant is also aggrieved with the effective date of revision of tariff and the treatment given to under-recovery and over recovery. Since the new tariff is lower than the tariff fixed vide the earlier order dated 10.04.06, the retrospective operation of the new tariff would require an adjustment of

Rs.26.63 Crores in the future Revenue Requirements. The appellant contends that the earlier order dated 10.04.06 did not provide for any adjustment in the event of revision of tariff. Further, the appellant contends that no such adjustment/recovery should be made since the energy has already been delivered at the previous rates.

(xii) The appellant contends that as per tariff order return on equity comes to only 4.5% instead of 14% allowed as per the Regulations.

03) Commission filed a counter affidavit in order to justify the impugned order. The Commission's justifications on each issue will be discussed as we proceed with the discussion on each issue.

Decision with reasons:

Pre-operative expenses -

04) The Commission has disallowed the expenditure of Rs.9.75 Crores claimed by the appellant as pre-operative expenditure. In this regard the order of the Commission says the following:

"**II. Pre-Operative Expenses**

5.5 As regards pre-operative expenses, the Commission feels that the same has to be related to setting up of the project which is not the case here and has not accepted the pre-operative expenses of Rs.9.75 Crore. Moreover, the Bid Documents also do not specify any recovery of such expenses incurred for and prior to submitting the bids for the project. The Commission is of the view such costs incurred were towards the bidding for the project and cannot be a part of the capital cost of the project. The Commission therefore does not accept the request for considering the amortization of the pre-operative expenses for computing AFC."

05) It is contended by the appellant that the Commission proceeded on a misplaced assumption that an expenditure of Rs.9.75 Crores was incurred by the appellant towards the bidding for the project. The Commission reiterates in its counter affidavit that this is a case of transfer of project by the Government of Maharashtra to the appellant and not a case of setting up of a new project. It is further contended that in the case of a new project the project developer has to incur the cost of technical studies, cost of obtaining clearance etc. for developing the project and such expenditures form part of capital cost. It is further contended that normal pre-operative expenses are in the range of 3 – 5 % whereas

the pre-operative expenses claimed by the appellant are around 15%.

06) The appellant in its written submission has given a breakup of Rs.9.75 Crores claimed as pre-operative expense. They are as under:

"(a)	*Technical & Management Fees*	*Rs.4.587 crores*
(b)	*Financing & Legal Fees*	*Rs.3.562 crores*
(c)	*Administration Expenses*	*Rs.1.026 crores*
(d)	*Machinery, Tools & Equipments*	*Rs.0.574 crores*
(e)	*Furniture & Fixtures*	*Rs.0.001 crores*
	Total Pre-operative Expenses	***Rs.9.750 crores"***

07) It is submitted by the appellant that all these expenditures were incurred after the bid and are project specific expenses which were incurred for the purpose of running the project.

08) It appears to us that the Commission did not sufficiently scrutinise the petition of the appellant so far as it relates to claim for Rs.9.75 Crores and rejected the entire claim on the assumption that these expenses were pre-bidding expenses and, therefore, not permissible to be recovered through tariff. The Commission, therefore, further needs to revisit its decision in this regard.

09) The Commission is fully entitled to carry out prudence check and disallow as much of the expenditure claimed as may be found to be imprudent. No part of the expenditure can be disallowed simply on the ground that it is more than the usual pre-operative expenditure. The Commission has to keep in view the project specific requirements and the peculiar situation in which the project was transferred including the fact that the project was running far below the design capacity and was a part of the irrigation project. This is all that we have to say in respect of appellant's claim for pre-operative expenses.

Renovation and Modernisation:

10) The Commission has not approved of the Renovation and Modernization (R&M) expenses claimed by the appellant for recovery through tariff. A major item disallowed is the expenditure incurred for a spare runner which the appellant considers necessary to acquire as it is a long delivery item and may be required anytime which the appellant feels wise to keep available in view of the nature of the project. The appellant is aggrieved that in disallowing the R&M expenditure claimed the Commission has solely relied upon the report of a technical expert Mr. V.V.R.K. Rao without any opportunity being given to the appellant to respond to the report or for any discussion or hearing either before Mr.V.V.R.K.Rao or before the Commission in respect of the report. The Commission in its counter affidavit contends that the decision

of the Commission is not based on the report of Mr.V.V.R.K.Rao although it has taken the opinion of Mr. V.V.R.K.Rao in this regard. The relevant portion of the impugned order can be read in order to ascertain to what extent the Commission has relied upon the report of Mr.V.V.R.K.Rao .

> *"As regards the Renovation & Modernisation expenses incurred, the technical expert, Shri VVRK Rao has opined that the identified "R&M Works" are based on inspection report prepared in December 2004 by the consultant Mr. Erskine L. Flook. The works proposed are categorized as Maintenance, Rehabilitation and Upgrades (Rs.3.15 Crore), Automation (Rs.2.6 Crore) and long term works (Rs.4.25 Crore) to be carried out within 10 years. Shri Rao opined that normally, R&M works may become necessary and are taken up when substantial part of the normal life of the plant has elapsed and performance of the plant is impaired. The items covered are more of the nature of normal maintenance works and cannot be considered as Renovation & Modernisation activities. Moreover, the provision in the Bid Document also stipulates that any expenditure incurred by the bidder for better performance, maintenance, repairs, etc., shall be at the risk and cost of successful bidder.*

Shri Rao further opined that under the long-term works, DLHPPL has proposed to procure a spare runner at a cost of Rs.4.0 Crore on the basis of the inspection report. In this regard, the consultant has expressed some concern regarding the quality of repair work on the turbine runner and recommended further inspection after one year of service, which has perhaps, not been done. Further, the inspection report recommends that the runner replacement could be considered when Nilwande dam is raised to its final level. At that stage, as per the consultant "opportunity exists to alter the design to improve operation at the higher tail water levels as well as increase the output of the generating unit at future reduced heads". Shri Rao suggested that a spare runner is not warranted at this stage of the project. DLHPPL could approach the Commission at an appropriate future date with data on how much higher output could be realized with the proposed change of runner and the cost economics. The rehabilitation work of the draft tube gate hoist could also be considered at that time.

Shri Rao further opined that the works proposed under "maintenance and rehabilitation and upgrades" are of routine nature and mostly form part of normal maintenance and not of capital nature. They also do not

come under the category of "not included in the original project cost" as laid down in Regulation 30.3 of the MERC Tariff Regulations.

Considering the views of the technical expert, Shri VVRK Rao, the Commission has not considered any expenses towards the R&M works. DLHPPL may, if necessary approach the Commission later for prior approval of additional capital expenditure with appropriate justification addressing the comments of technical expert and with proper cost-benefit analysis. The Commission may consider the additional capital expenditure based on the prudence check of the same and approve the adjustment to the tariff approved in this Order."

11) It is clear from the portion of the impugned order extracted above that the Commission has based its decision entirely on the report of Mr.V.V.R.K.Rao. The Commission has not considered what part of the claim towards R&M expenditure should be allowed as pass through on any individual analysis of its own. It has entirely gone by the report of Mr. V.V.R.K.Rao.

12) It is contended on behalf of the Commission that although the report of Mr.V.V.R.K.Rao was relied upon by the Commission while passing its initial order there has been no violation of the principle

of natural justice in this regard. Further it is contended that the appellant had full opportunity of placing its case before the Commission.

13) The fact remains that the appellant was not provided with an opportunity to make any submission regarding the report of Mr.V.V.R.K.Rao. Nor did Mr.V.V.R.K.Rao hear the appellant. In this regard we find that the appellant is rightly aggrieved and that appellant needs to be given an opportunity to explain its position vis-à-vis the report of Mr.V.V.R.K.Rao.

14) It is also contended on behalf of the Commission that in accordance to the Amendment to the Guidelines for in principle clearance of proposed Investment Schemes dated 18.02.08 the in principle approval of the Commission has to be obtained by separate regulatory proceedings. The Commission points out that such in principle approval has not been obtained by the appellant and, therefore, the R&M expenditure claimed by the appellant cannot be allowed. Suffice it to say that R&M expenditure claimed by the appellant were incurred prior to the aforesaid guidelines being notified. Those guidelines are, therefore, not applicable to the case in hand. No part of the R&M expenditure claimed by the appellant can be disallowed on account of non-adherence to those guidelines.

15) We thus find that in respect of the R&M expenditures to be allowed to be pass through in tariff, the Commission needs to re-visit its decision after allowing the appellant an opportunity to explain its case vis-à-vis the report of Mr.V.V.R.K.Rao.

Secondary Energy charge:

16) The Commission has not accepted the request of the appellant for considering the incentive for secondary energy over and above the primary energy in accordance with the provision of CERC Tariff Regulations 2004. It is contended by the appellant that the concept of secondary energy charge is well recognised. If in a particular year the generation of electricity from water availability is more than design energy, the secondary energy charge is recoverable in addition to the annual fixed charge. It is explained by the appellant that design energy is defined as quantum of energy which can be generated in 90% dependable year with 95% installed capacity of the generating station. In case the total generation is less than design energy because of inadequate water flow, annual fixed charge is sufficient to recover the cost. Annual fixed charge comprises of the energy charge and capacity charge. The appellant contends that in case the appellant is unable to recover the secondary energy charge there is no incentive whatsoever to operate the plant after generating equivalent to design energy which amounts to wasting of opportunity to produce more than the design

energy even when the water flow permits such additional generation.

17) The Commission is aware of the CERC Regulations dealing with secondary energy. Yet the Commission has declined to grant the secondary energy charge relying upon its own Regulations. The relevant part of the Commission's decision is as under:

"XI. Design Energy, Primary Energy and Secondary Energy

75. The Commission has considered the Design Energy as stipulated in the Order dated April 10, 2006 in case No.1 of 2005 as listed below:

i. Pre Nilwande Phase – 34.10 MU
ii. Post Nilwande Dam (+613 M) – 43.40 MU (w.e.f. October 2009)
iii. Post Nilwande Dam (+648 M) – 36.26 MU (w.e.f. April 2012)

Further, the Commission has considered the dates for the increase in the height as submitted in Petition in the present case.

76. As regards Secondary Energy, the Commission has not accepted the request of DLHPPL for considering incentive for Secondary Energy (over and above the Primary Energy) in accordance with the provisions of the CERC Tariff Regulations, 2004, and has relied on the MERC Tariff Regulations, which stipulates the recovery of the AFC in two parts, i.e., Annual Capacity Charge and Energy charge. Regulations 28.2 and 35.2 of MERC Tariff Regulations stipulates as under:

"28.2 Tariff for sale of electricity from a hydro power generating station shall comprise of two parts, namely, recovery of annual capacity charge and energy charges.

Provided that the annual capacity charges for a hydro power generating station shall be computed in accordance with the following formula:

Annual Capacity Charges = (Annual Fixed Charge – Energy Charge)

Provided further that the Energy Charges shall not exceed the Annual Fixed Charge under these Regulations"

"35.2 Energy Charges

(a) Energy charges shall be worked out on the basis of paise per kWh rate on exbus energy scheduled to be sent out from the hydro power generating station.

(b) The energy rate of a hydro power generating station shall be such rate as may be notified by the Commission from time to time, based on the price variable cost of the least-cost available alternative source of power if such hydro power generating station was not to be dispatched in accordance with the final dispatch schedule of the State Load Despatch Centre.

(c) The energy charge shall be computed in accordance with the following formula

Energy Charge = Saleable Energy x Energy Rate"

The MERC Tariff Regulations do not differentiate between primary energy and secondary energy, and energy charges are to be computed based on entire saleable energy. Thus, the entire revenue recovered from Energy Charges should be deducted from Annual Fixed Charges for determining Annual Capacity Charges."

18) It is clear from the above quotation that Regulation 28.2 and 35.2 applied strictly will eliminate the secondary energy charge altogether. The Regulation 28.2 specifically provides that annual capacity charge will be equal to annual fixed charge (-) energy charge and further that energy charge shall not exceed the annual fixed charge. The Commission has opined that entire revenue recovered from energy charges should be deducted from annual fixed charge for determining annual capacity charge. The price for any secondary energy generated will have to be covered within the same formula as there is no distinction between primary energy charge or secondary energy charge. The plain reading of the Regulations leads one to the same conclusion to which the Commission has arrived at. The appellant does not dispute this position. However, the appellant contends that the CERC Regulations need to be applied because : (i) the State Commission has to be guided by the CERC Regulations while framing its own regulations and (ii) the MERC Regulations need to be read down following the principle laid down by this Tribunal in *Damodar Valley*

Corporation Vs. Central Electricity Regulatory Commission & Others 2007 ELR (APTEL) 1677 (at page 1687-1688). In the DVC case (supra) we ignored certain Regulations which were contrary to DVC Act although those provisions were not held to be ultra vires of the DVC Act. We are of the opinion that the principle of reading down does not apply to the present case as we are not invited to ignore any part of the Regulations as being ultra vires. It is actually being submitted that the Regulations are either inadequate or are contrary to CERC Regulations. The prayer of the appellant in fact is to read more than what is available in the Regulations relied upon by the Commission. This is not possible within the principle of reading down. So far as CERC Regulations are concerned, they may have some guiding value but once the State Commission frames its own Regulations the State Commission's Regulations and not the CERC Regulations can apply. Therefore, the appellant cannot get what it wants for secondary energy generation by application of CERC Regulations or by reading down the MERC Regulations.

19) Although we uphold the Commission's decision to disregard secondary energy charge, we cannot but express our concern for encouraging energy generation on the one hand and rewarding efficiency on the other. Section 61 of the Act, inter alia, requires the Commission to be guided by some factors while framing terms & conditions for determination of tariff. Clause (c) of section 61

mentions encouragement to efficiency, economic use of the resources, good performance and optimum investment. Clause (e) mentions rewarding efficiency in performance. Clause (h) directs promotion of energy from renewable sources of energy. Thus rewarding secondary energy generation is in the spirit of the provisions of section 61 of the Act. The Central Commission has accordingly made provision for rewarding secondary energy generation. We are not able to appreciate the Commission's approach of ignoring the need to encourage generation of secondary energy by making adequate provision in its Regulations. We hope the Commission will take remedial measures in this regard and bring appropriate amendment in the Regulations.

Auxiliary Consumption:

20) The Commission has limited the auxiliary consumption to 1.2% whereas the appellant has asked for 1.44%. The brief order of the Commission in this respect is as under:

> ***"XII. Auxiliary Consumption***
>
> *77. As regards the Auxiliary Consumption, the commission has not considered DLHPPL's submissions to consider at 1.44% and has considered the normative auxiliary energy consumption and transformation losses as 0.7% and 0.5%, respectively, in accordance with the MERC Tariff Regulations."*

21) In the counter affidavit the Commission says that the Commission has followed the norms prescribed in the Tariff Regulations. The norms prescribed in the Tariff Regulations are at Paragraph 33.2.2 and 33.3 of the Regulations which is as under:

"*33.2.2 Auxiliary Energy Consumption*

(a) Surface hydro electric power generating stations with rotating exciters mounted on the generator shaft – 0.2% of energy generated

(b) Surface hydro electric power generating stations with static excitation system – 0.5% of energy generated

(c) Underground hydro electric power generating stations with rotating exciters mounted on the generator shaft – 0.4% of energy generated

(d) Underground hydro electric power generating stations with static excitation system – 0.7% of energy generated

33.3 Transformation losses (hydro power generating stations)

From generation voltage to transmission voltage – 0.5% of energy generated."

22) It is contended by the appellant that the appellant's power plant does not fall into any of the categories mentioned above. The appellant contends that the appellant's project is a typical well type underground power station and that the power station requires continuous running of drainage and de-watering pump due to presence of upstream and downstream reservoirs. On account of its location there is water seepage inside the power house and auxiliary consumption is required to pump out water on a constant basis. It is further contended that the power station runs at a very low plant load factor of about 12% and therefore, the auxiliary consumption is high as compared to normal hydro project. It appears from the portion of the order extracted above that the Commission has not considered the peculiarity associated with the station of the appellant while determining the auxiliary consumption. The Commission, therefore, has to re-visit its decision in this regard and has to come to a fresh decision after considering the peculiarity of the power station with very low plant load factor in question.

Unscheduled inter change charge:

23) It is alleged by the appellant that the unscheduled inter change charge has been applied by the Commission to the

appellant's power station in the same manner as the other generating stations are subjected to. It is contended by the appellant that the Tariff Regulations of the State Commission do not deal with an irrigation based hydro power plant where scheduling based on power requirements of the State is not possible. In an irrigation based project power generation can only be at the time when the water is to be dis-charged as per the requirements of the Water Resources Department. Such projects operate as Must-Run-Type Power Plant. The Commission in its counter affidavit, however, has denied that unscheduled inter change charge have been made applicable to the appellant. The Commission in the impugned order said:

> "T*he other issues raised such as Charges for Unscheduled Interchange, Billing and Payment Mechanism, Rebate/Late Payment Surcharge, Demonstration of Declared Capacity and Deemed Generation shall be governed by the respective Regulations of the Commission"*.

24) The Commission's Regulations in this regard has been extracted by the Commission in its counter affidavit which is as under:

“The generating station may be entitled to receive or shall be required to bear, as the case may be, the charges for deviations between energy sent-out corresponding to scheduled generation and actual energy sent-out, in accordance with the Balancing and Settlement Code, as may be published by the State Load Despatch Centre and approved by the Commission:

Provided that the rate for determination of such charges shall be as notified by the Commission from time to time.”

25) The Commission says that in accordance with the above provisions of the Regulations it has issued the Order in case No. 42 of 2006 in the matter of introduction of Availability Based Tariff regime at State level within Maharashtra and other related issues wherein the Commission has not considered generators as part of imbalance pooled settlements and hence unscheduled inter change charges are not applicable to generators.

26) In view of this counter affidavit the issue regarding imposition of unscheduled inter change has become infructuous.

<u>Demonstration of declared capacity index:</u>

27) The appellant contends that the Commission has erred in its direction regarding demonstration of declared capacity index. In

view of Commission's stand in respect of the UI charges this issue has also become infructuous.

<u>Incentive based on capacity index:</u>

28) The Commission's directive on this issue is as under:

> "*XV Incentive*
>
> *82. DLHPPL shall be eligible for an incentive payable in accordance with Regulation 37.2 of MERC Tariff Regulations, DHPPL shall compute the incentive on the basis of the actual performance and shall bill the same as an additional charge, payable at the end of the year. There shall be pro-rata reduction in recovery of Annual Fixed Charges in case the generating station achieves capacity index below the prescribed normative levels."*

29) The appellant contends that the appellant cannot be subjected to this incentive based on the capacity index as its performance is highly dependent on the water level at Nilwande Dam. The Commission's contention in this regard is that it has gone by the Tariff Regulations which is as under:

> *"33.2 <u>Hydro power generating stations</u>*
>
> *33.2.1 Normative capacity index for recovery of annual fixed charges*

(a) During first year after commissioning of the generating station

(i) Purely Run-of-river power stations - 85%

(ii) Storage type and Run-of-river power stations with pondage - 80%

(b) After first year after commissioning of the generating station

(i) Purely Run-of-river power stations - 90%

(ii) Storage type and Run-of-river power Stations with pondage - 85%

Note:

There shall be pro rata recovery of annual fixed charges in case the generating station achieves capacity index below the prescribed normative levels. At Zero capacity index, no fixed charges shall be payable to the generating station."

30) It is contended by the appellant that it is not covered by any of the two classes of hydro generating stations mentioned in the Regulations namely run-of-river power station or storage type and run-of-river power station with pondage. The Commission is required to apply its mind as to which category and why the appellant's power station will fall. The Commission needs to pass a speaking order on the appellant's contention that the Regulations do not apply to its power station in view of the fact that it is dependent on the level of water at Nilwande Dam and also because

it is an irrigation related project, the demands of irrigation takes precedence over the demand of the generating station.

<u>Non-consideration of Interest during construction for calculation of O&M cost:</u>

31) The mode of calculation of operation and maintenance cost has been provided in clause 34.6.2 of Tariff Regulation which is applied to the appellant. The same is as under:

> *"(b)* ***Hydro power generating stations***
>
> *The base operation and maintenance expenses shall be fixed at 1.5 percent of the approved original cost of the project, in the year of commissioning and shall be escalated at a rate of 4 per cent per annum for the subsequent years."*

32) The Commission has fixed O&M expenses on the capital cost of Rs.93.29 Crores from the date of COD as can be seen from the following part of the order :

> "***O&M Expenses***
>
> *69. The Commission has considered the base O&M expenses as 1.5% of the capital cost of Rs.93.29 Crore from the date of COD of the project and has escalated the*

same @ 4% in accordance with Regulation 34.6.2 (b) of the MERC Tariff Regulations for future years."

33) The appellant had contended that the capital cost of Rs.93.28 Crores did not include interest during construction as the power station was constructed by the Government of Maharashtra which does not have to borrow. Since the capital cost normally includes interest during construction the operation and maintenance cost which is related to the capital cost should include interest during construction. It is not disputed that the capital cost of Rs.93.28 Crores does not include interest during construction. In order to give a realistic assessment of O&M expenses it is only reasonable and fair that interest during construction is added to the declared capital cost of the station in order to derive the O&M expenses. The Commission has not considered this aspect of the case and has not even given any reason for not considering the component of interest during construction as a part of capital cost for deriving the O&M expenses. We, therefore, have to require the Commission to re-visit its opinion on the operation and maintenance expense and calculate the same on the basis of capital cost including interest during construction.

Non-inclusion of minimum alternate tax:

34) The appellant has expressed a grievance that the Commission has calculated the Minimum Alternate Tax or MAT at 11.99%

although the rate for MAT as revised for the year 2000-10 was 16.995%. This issue has been considered by the Commission in its counter affidavit. The Commission has expressed its willingness to include in its calculation an enhanced MAT. As per Regulations income tax is considered as part of annual fixed charges on estimated basis which is subject to adjustments each year on account of the assessment. It is stated in the counter affidavit that in accordance with the Regulations the appellant always has the opportunity to approach the Commission for suitable adjustments in the annual fixed charges on account of change in income tax rate. The omission to apply the enhanced rate of 16.995% was on account of the fact that the revision in the rate came almost simultaneously with the passage of the impugned order. We, therefore, have to direct the Commission to apply the enhanced rate of MAT while calculating annual fixed charge.

Means of finance and debt equity ratio:

35) The appellant bid for the project at the estimated value of Rs.93.28 Crores but made an upfront payment of Rs.60 Crores. The appellant disclosed that of the Rs.60 Crores upfront payment Rs.54 Crores had been obtained by way of loan from financial institutions. The commission has applied the debt equity ratio of 54:6 for calculating return to equity. The appellant claims return to equity on the normative debt equity ratio of 70:30.

36) During arguments the appellant contended that had the Commission granted a pre-operative expense of Rs.9.75 Crores which had been spent out of equity the appellant would not have had any grievance. The appellant has not only spent Rs.60 Crores which was the bid price but also other capital expenses particularly the pre-operative expense of Rs.9.75 Crores. We have already held that the Commission needs to take into account the pre-operative expenses which were incurred by the appellant after the bid but before actually operating the plant for production of electricity. Further the R&M expenditure also needs to be taken into account. Once the Commission takes into account these items of capital expenditure the Commission will have to calculate afresh the debt equity ratio.

Date of applicability of tariff:

37) The tariff as determined by the commission vide the impugned order is applicable for 30 years. It is stated in the impugned order that the revised/determined tariff shall be made applicable from 01.04.09. As against the appellant's claim for tariff of 5.60 kWh the Commission has determined a tariff of 3.73 per kWh. The Commission says the following in respect of effective date of tariff revision and treatment of under-recovery and over-recovery.

"***XIII. Effective Date of Tariff Revision and Treatment of Under-Recovery/Over-Recovery***

78. *The Commission has computed the year-wise Annual Fixed charges for BHEP-II from the date of taking over of the project by DLHPPL. The Commission has considered the details of the revenue received as submitted by it for the period from FY 2006-07 to FY 2008-09. As the Commission has approved the AFC from FY 2009-10 onwards, the Commission has considered the under-recovery or over-recovery of AFC from the year of taking over till the end of FY 2008-09 as shown in Table below and has amortised the same in equal instalments along with carrying cost of 6% per annum from FY 2009-10 onwards over the remaining period of lease of BHEP-II. The Commission clarifies that the revision in AFC as approved by the commission will be effective only prospectively i.e., with effect from July 1, 2009, and any difference between the approved AFC for FY 2009-10 and total revenue recovered during FY 2009-10, should be adjusted at the end of FY 2009-10.*

Particular	***FY 2006-07***	***FY 2007-08***	***FY 2008-09***
Computed AFC	*2.67*	*10.93*	*11.12*
Revenue Received from MSEDCL	*3.40*	*20.19*	*14.78*
Under/(Over) Recovery	*(0.73)*	*(9.26)*	*(3.66)*
Carrying cost on			

Under/(Over) Recovery	*(0.04)*	*(0.56)*	*(0.22)*
Total Carrying Cost till FY 2009			*(0.82)*
Under/(Over) Recovery with carrying cost to be amortised			*(14.47)*

38) The extracted portion above shows that the intention of the Commission was to apply the tariff prospectively w.e.f. 01.07.09 and any difference between approved AFC for the FY 2009-10 and total revenue recovery during 2009-10 would be adjusted at the end of 2009-10. Nonetheless, in the table extracted above, some adjustment is suggested w.e.f. the year 2006-07. The Commission contends that in the tariff petition, which is 27 of 2007, the appellant itself had prayed for the revised tariff to be applied from 01.01.07. The Commission contends that in view of this prayer the Commission in the table showed truing up assuming revision in tariff w.e.f. 01.01.07.

39) This is an obvious mistake. The Commission, having said in so many words that the tariff will be applicable w.e.f. 01.07.09, cannot ask for truing up from 2007 onwards. The prayer of the appellant in its tariff petition was in view of the appellant's prayer for enhancement in tariff. Since the tariff determined has not been enhanced it will be unfair to ask the appellant to return the tariff recovered till the impugned order was passed. In this regard we have to uphold the appellant's contention that the tariff will be

effective only from 01.07.09 and adjustments of under-recovery or over-recovery will be made only for 2009-10.

40) The respondent No.2, MSEDCL, has expressed apprehension that a revision in tariff following the present judgment may adversely affect its financial position. The apprehension is appreciated.

41) In view of our above decision, the appeal is allowed in part, as indicated in paragraphs 09, 15, 22, 30, 33, 34, 36 and 39 above. We set aside the impugned order. The Commission is directed to re-determine the tariff petition No. 27 of 2007 in the light of the observations made above.

42) The impact of the tariff revision following this judgment be distributed over twelve monthly bills of the respondent No.2.

43) With this the interlocutory application No. 265 of 2009 also stands disposed of.

44) Pronounced in open court on this *23rd day of December, 2009.*

(H. L. Bajaj)
Technical Member

(Justice Manju Goel)
Judicial Member

Reportable✓ / Non-reportable