Before the Appellate Tribunal for Electricity
(Appellate Jurisdiction)

Appeal No. 90 of 2007

Dated: December 11, 2007.

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

Reliance Energy Ltd.
Reliance Energy Centre
Santacruz (East)
Mumbai

Versus

1. The Maharashtra Electricity Regulatory Commission
   World Trade Centre No. 1
   13th floor, Cuffe Parade, Colaba
   Mumbai-400001 ....Appellant

2. Mumbai Grahak Panchayat
   Sant Dnyaneshwar Marg,Vile Parle(W)
   Mumbai-400056

3. Prayas C/o Amrita Clinic, Athawale Corner
   Karve Road
   Pune-411004

4. Thane Belapur Industries
   Post Ghansoli
   Navi Mumbai-400071

5. Vidarbha Industries Association
Civil Lines,
Nagpur-4400041 ....Respondents

For the appellant(s) : Mr. J.J. Bhatt,Advocate
Ms Anjali Chandurkar,Advocate
Mr. Syed Naqvi, Advocate
Ms Smieetaa Inna, Advocate

For the respondent(s): Mr. Jayant Bhushan, Senior Advocate
Mr. Arijit Maitra & Mr. Buddy Ranganadhan, Advocates
Mr. Suresh Gehani & Mr. Sunil Kumar, Consultants

Judgment

This appeal, preferred by Reliance Energy Ltd. (REL in short), challenges order dated April 23, 2007 in case No. 2 of 2007 and tariff order dated April 24, 2007 passed in case No. 75 of 2006 by the Maharashtra Electricity Regulatory Commission (MERC or the Commission in short).

2. The brief facts leading to the appeal are given hereunder:

3. REL was required to submit its Multi Year Tariff (MYT) petition to MERC by November 30, 2006 for the FY 2007-08 as per Regulations 9 of the MERC (Terms and Conditions) Tariff

Regulations notified by MERC under provisions of The Electricity Act, 2003 (the Act). MERC was determining tariff for the year 2007-08 which was a part of the first MYT period for FY 2007-08 to FY 2009-10. Submission of the petition was delayed by REL due to several reasons and the same was eventually submitted in January, 2007 for generation, transmission and distribution businesses for the first control period FY 2007-08 to FY 2009-10. In the meantime, by an order dated April 23, 2007, MERC ordered REL to charge tariff to its consumers as per the then existing tariff order. MERC thereby extended the applicability thereof till the revised tariff was determined for FY 2007- 08. Vide this order MERC also held that the brunt of the underrecovery, if any, or financial implications, caused due to late submission of the MYT applications by licensee should not be passed on to the consumers and the licensee should internalize and bear the consequential losses thereon. MERC held that no adjustment shall be allowed to be made in the bills for the underrecovery by licensee on account of continuation of the existing tariff for

the period till the revised tariff was determined for the remaining period under FY 2007-08. Hence this appeal.

4. The appellant has the following grievances in tariff order dated April 24, 2007 issued by the Commission insofar as REL is concerned:

(A) applicability Revised Tariff prospectively from April 24, 2007 and not from April 1,2007;

(B) the Energy Input requirement assumed by MERC for FY 2008, 2009 and 2010;

(C) the determination of distribution losses at 11.50%, 11% and 10.50% for FY 2008, 2009 and 2010 respectively;

(D) the underrecovery of Fuel Adjustment Cost (FAC) up to September, 2006

(E) the approval of short term power purchase at Rs. 4.41 per unit;

(F) the Capital Expenditure not approved by the MERC on the ground that the Detailed Project Report (DPR) schemes were not approved by MERC;

(G) Income-tax

(H) Standby charges;

(I) Employee Expenses.

Since several issues are involved, we proceed to take up each issue one by one:

(A) Applicability of Revised Tariff prospectively from April 24, 2007 and not from April 1, 2007:

5. Ms Anjali Chandurkar, learned Advocate appearing for the appellant submitted that the REL, hithertofore, was an integrated utility engaged in generation, transmission and distribution of electricity and it was for the first time that it had to submit its tariff petitions separately for generation, transmission and distribution. Therefore, it was contended by the appellant, REL sought for formats for submission of its MYT application and that MERC confirmed the formats for submission of ARR applicable for FY 2006-07 as late as on December 13, 2006. It was further submitted by her that REL had collected and compiled the required data on a standalone computer whose hard disk got corrupted and, therefore, REL

was required to collect the data from various sources once again. This fact was duly informed to MERC by REL vide its letter dated January 9, 2007 and despite the letter of intimation MERC vide its letter dated January 10, 2007 issued a show cause notice to REL under the provisions of Section 142 of the Act.

6. Learned counsel submitted that the REL duly replied show cause notice of MERC and had submitted categorically that there was no intentional delay in filing MYT petition and that delay was beyond its control and that in the meantime it had compiled data in respect of REL-D which was being filed separately. She stated that the proceedings under Section 142 of the Act are pending before MERC.

7. Learned counsel for the appellant tried to justify the delay in submission of their tariff petition and said that during the Technical Validation Session on February 13, 2007 by MERC, REL was directed to submit certain additional data also. She further submitted that vide letters dated

February 07, 2007 and February 13, 2007, MERC sought certain queries from REL which were duly replied by it vide its letters dated February 9, 2007, February 10, 2007 and February 12,2007 and that this shows that REL had acted fast in giving requisite information and details to MERC.

8. Ms Anjali Chandurkar submitted that whereas REL was permitted to charge the existing tariff by MERC, MERC vide its letter dated April 23, 2007 extended the applicability of the existing tariff till the revised tariff was determined for FY 2007-08. MERC held that the brunt of underrecovery, if any, financial implication caused due to late submission of MYT application should not be passed on to the consumer and the licensee should internalize and bear the same. She said that valid reasons beyond the control of appellant existed due to the crashing of hard disk as the business of REL was run on an integrated SAP Platform. She pleaded that REL should not be made to bear the financial burden of approximately Rs. 50 crores for the period April 01, 2007, April 23, 2007 due to non-application of the revised tariff.

Analysis and decision:

9. In a similar case in appeal No. 70 of 2007, Maharashtra State Electricity Distribution Co. Ltd. vs Maharashtra Electricity Regulatory Commission, this Tribunal has held as under:

> *"8. In the present case the gap between the beginning of the FY and the date when the new MYT becomes effective is nearly a month. The loss of revenue in this given situation is Rs. 88 crores. This loss could be much higher if the delay in tariff fixation had been longer. In a given situation, if the licensee is unable to file the ARR petition due to some reasons will it be proper to say that tariff policy requires such difference to be denied to the licensee forever? The answer clearly is 'No'. All that can be denied to a licensee in this situation is the carrying cost and not the legitimate claim towards revenue."*

> *" 9. It has to be understood that the consumer has to pay for the electricity supplied to him. As per Section 61 of The Electricity Act, 2003 the Appropriate Commission fixes the tariff safeguarding, inter alia, interest of consumers and at the same time, recovery of cost of electricity in a reasonable manner. Therefore, there is nothing unjust in*

recovering the sheer cost of supply of electricity from the consumers. It is not an additional burden on the consumer. The consumer in the present example would have paid the same tariff had the ARR and tariff petition been filed in time. Only, the tariff order comes into effect a month later. The expression used by the Commission namely 'financial implications caused solely due to late submission of MYT applications by the licensees should not be passed on to the hapless consumers" indicates misplaced sympathy. In case consumer is made to pay more than the cost of supply he can be described as hapless. Secondly the financial implication caused solely due to late submission is only the delay in recovery and not the increase in tariff. It is not the case of the MERC that the tariff has gone up because of late filing. Only the determination of tariff is delayed because of late filing. The financial implication of the delay is nothing but the carrying cost. The consumer cannot be burdened with this resulting carrying cost because the delay has not been caused on account of their default."

" 10. In view of the above, we allow the appeal and set aside the impugned order of 22nd April, 2007. The MERC will now pass appropriate orders, making it possible for the appellant to recover the amount denied to it by the

impugned order, either through the process of truing up or by the process of revision in tariff."

10. The above judgment of this Tribunal squarely applies to the facts of the present appeal. In view of the above judgment we decide that the appellant should be allowed to recover the difference between the revised tariff and the tariff which was applied during April 1, 2007 to April 23, 2007. We order accordingly.

(B) Energy input requirement assumed by MERC for FY 2008, 2009 and 2010.

11. Learned counsel for the appellant submitted that the Commission has inadvertently considered different sale figures in Table 8 and Table 10 of the tariff order dated April 24, 2007 which had led to incorrect energy input requirements in different computation as mentioned in table 10 of the tariff order, which has, in turn, resulted in reducing estimation of power purchase requirements and, consequently, the estimation of power purchase cost.

12. MERC vide its affidavit dated August 14, 2007 has fairly conceded that there has been an inadvertent error in the consideration for the purposes of estimation of power purchase quantum and hence power purchase cost. It is

conceded by the Commission that an additional quantum of 144 MU of power purchase is required thereby increasing the power purchase cost by Rs. 64 crores considering the power purchase rate of Rs. 4.41 PU as per the tariff order dated April 24, 2007. The Commission conceded that the reasonable and prudent quantum and cost of power purchase based on actual sales and allowed distribution loss level will be considered at the time of Annual Performance Review for FY 2007-08.

13. In view of the above we direct MERC to allow expenditure while truing up the accounts. We order accordingly.

(C) Determination of distribution losses at 11.50%, 11% and 10.50% for FY 2008,2009 and 2010 respectively.

14. Learned counsel for the appellant contended that the order of the Commission directing REL to reduce the commercial loss at the rate of 0.5% every year throughout the control period is without any basis or reasons whatsoever and even without considering the technical losses or giving any finding thereon and that MERC has merely directed REL to conduct a detailed study of technical losses in the system at

feeder level and distribution and transmission level and submit a report within six months from the date of impugned order. She asserted that MERC has itself held that in absence of any technical substantiation MERC was constrained to draw its own conclusion. She further submitted that MERC has neither relied upon any material nor given any reason for the purpose of arriving at the said loss reduction or the approved distribution loss and that the order is based merely on conjectures and surmises.

15. Learned counsel for the appellant submitted that REL is in the process of providing the data with regard to technical losses for which MERC has given six months time and that insofar as the commercial losses are concerned, REL has given details that the same shall be about 1.6%. Learned counsel contended that REL has given various reasons for commercial losses in the distribution system such as slow and sticky meters, theft of electricity etc. She emphasized that meters installed by REL are of Class-II accuracy having a tolerance of

2%, around six lakhs meters are electro-mechanical. She pleaded that MERC has not permitted REL to replace old meters which are less than 15 years old vide its letter dated November 10, 2005. She said that MERC itself, recognizing the fact that replacement of meters would result in reduction of commercial losses, has directed BEST undertaking to replace all Electro mechanical Meters by Electro static Meters. She said that MERC ought to have considered that theft of electricity which cannot be eliminated entirely in view of electrification of large unorganized development (slums) in REL's area of supply. She said that MERC reliance on this Tribunal order dated August 29, 2006 in appeal No. 80 of 2006, KPTCL vs KERC, is misplaced. Learned counsel submitted that MERC order in regard to determination of distribution losses at 11.5%, 11% and 10.05% for FY 2007-08, FY 2008-09 and FY 2009-10 respectively may be set aside and the distribution loss at 12.1% for the MYT period as claimed by it in the MYT petition before the Commission may be allowed.

16. Per contra learned counsel for MERC contended that as stated in its order dated April 24, 2007 the target set is not an impossible target and the utility has to work towards achieving the same. In this view of the matter they drew our attention to the following paras of their order:

> *"However, REL-D in its petition has stated that, there are commercial losses in the REL-D's distribution system and that the commercial losses in the Distribution system are due to slow & sticky meter, theft of electricity etc. REL-D has submitted that for managing the commercial losses, it has segregated its consumers into Non-Slum (Residential, Commercial and Industrial) and Slums based on commercial losses. REL-D has further stated that the Commercial loss for the non-slum consumers is less than 1%. Also it has stated the details about the commercial losses in the slum areas. The relevant extract from the licensee's petition is given below:*
>
> *"There are approximately 35% of REL consumers who live in unorganized developments commonly known as slums. The levels of losses in these Slums vary between 15% and 70% with average losses of around 22% in these areas during the drive. These areas are densely populated and*

have limited access with the network being laid in very rigid conditions including limited space available for cable laying. In view of this the network is highly susceptible to pilferage and unauthorized drawl of energy. In view of constraints stated above it becomes difficult to locate such unauthorized drawls and it is observed that the pilferage reoccurs in a short period of time. This indicates that the process of reducing pilferage in these areas is time consuming and results are slow and get offset by new unauthorized mushrooming."

Considering the above submissions of the licensee, the Commission has observed that REL-D has significant commercial losses in its slum as well as non-slum areas and that the licensee's efforts in reduction of commercial losses have been limited. In the technical validation session, the Commission & the consumer representatives have suggested REL-D, various measures such as giving out franchisee of slums, reduction of theft through special drives and other effective measures for reduction of commercial losses.

The Commission is of the strong view that there is a huge scope of reduction in commercial losses that is directly related to managerial effectiveness, with least or no capital expenditure requirement in the area of the licensee

and that the licensee needs to take all necessary and immediate steps to reduce the commercial losses in the system. The argument of commercial loss due to sticky and slow mete and impossibility to reduce the same without commensurate capital expenditure is not sound since it is only fair for the Commission to ensure that the licensee extracts useful technical life of the investments already made in metering. The Commission directs the licensee to submit a commercial loss reduction plan to the Commission within forty five days of the issue of this Order; this plan should include the different types of commercial loss prevailing in the system and the amount of loss attributable to the each of the loss types.

The Commission has also noted that REL-D has not provided the breakup of distribution loss into technical & commercial losses for the control period, in spite of having invested significant sums in SCADA that is supposed to facilitate such technical loss evaluation."

Hence, the Commission directs the licensee to conduct a detailed study of the technical losses in the system at feeder level and DTR level and submit a report on the same within six months of the issue of this order. In absence of any technical substantiation, the Commission

would be constrained to draw its own conclusion in such matters of technical nature."

17. Learned counsel for the Commission stated that the Commission has also provided for correction of the loss target based on the technical loss study to be submitted by the licensee. The relevant extract from the tariff order is as follows:

> *"The Commission observed that in the public hearing held on February 13, 2007, responding to the queries on distribution loss levels, REL-D has replied that the technical loss of the system is of the order 10.50% and the commercial loss is of the order 1.60% which amounts to a total system loss of 12.10%. The Commission is of the opinion that commercial loss for REL-D would be more than 1.60%, as REL-D's claim is not supported by any technical study. The Commission after considering the analysis on the commercial losses, mentioned in the above paragraphs, directs the licensee to reduce the commercial losses at the rate of 0.5% every year through out the control period.* ***The loss levels would be corrected based on the technical loss study to be submitted by the licensee." (emphasis added).***

18. Learned counsel for MERC informed that the appellant has not yet submitted report on technical studies as had been directed by the Commission and that the commercial loss of 1.60% has been estimated as the difference between the total losses and the technical losses is also not tenable in the absence of any study to estimate the actual technical losses which is in the process of being undertaken by the appellant. Learned counsel cited this Tribunal's order dated August 29, 2006 in appeal No. 84 of 2006, KPTCL vs KERC, relevant para of which is extracted below:

> *"….we are of the considered view that with respect to the direction issued by Commission to reduce the transmission losses, no interference is called for. The Commission has issued directions to reduce transmission losses to the level of 4.06% and this is not an impossibility. It is for the utility to improve its performance and reduce the transmission loss. The Commission is well founded in issuing direction in this respect."*

19. Learned counsel pleaded that the commercial losses can be reduced if theft of electricity is curtailed and that the appellant should conduct the required technical studies and undertake measures for loss reduction as directed by the Commission.

Analysis and decision:

20. Admittedly loss reduction in distribution system is vital and in the interest of both the licensee and the consumers and, therefore, all efforts need to be made to reduce these losses. We recognize that the Commission is making all sincere efforts to ensure reduction of losses. We find that though specific numbers have been given while setting the target for the losses in three years of the control period, no study has been done either by the Commission or by the licensee while fixing these loss targets. The licensee has two major problems in the reduction of losses namely theft of electricity and meters with accuracy Class-II having tolerance of 2%. The Commission is targeting the reduced losses to the extent of 0.5% every year There is no reason and rationale for not changing the mechanical meters which entail the error of 2%. When losses are to be reduced to the extent of 5 to 10%, as in some of the states where prevailing loss level is more than 30%, perhaps it is not so urgent to replace the mechanical meters but when attempted reduction of losses is as low as 0.5% then there is no reason for continued use of meters with 2% tolerance level. We direct the Commission to allow the appellant to change all the meters within a specified period of about six months, depending upon the procurement and installation time. We are also inclined to agree that the theft cannot be curbed over night.

21. The Commission has cited our Karnataka judgment in case of transmission losses where there is no question of theft or wrong metering and therefore, this argument is misplaced in case of distribution losses.

22. We direct the appellant to immediately submit report on technical studies as directed by the Commission in the next three months.

23. Considering that the losses must be reduced further and keeping in mind the practical difficulties regarding the mechanical meters and theft of electricity in unorganized areas, till such time the technical studies are carried out, the target of losses during the year 2007-08 be retained at the level of 12.1% as proposed by the appellant in its petition. We also direct the Commission that after installation of electrostatic meters in place of mechanical meters and availability of technical study report, it should review the loss level target for the year 2008-09 and 2009-2010.

(D) Underrecovery of Fuel adjustment Cost (FAC) upto September, 2006.

24. Learned counsel for the appellant submitted that REL-D has incurred FAC for the period April 1, 2006 to September 30, 2006 aggregating to Rs. 49 crores which is payable to REL-

G and that tariff determination by MERC vide order dated October 3, 2006 was made applicable prospectively and therefore, the said amount of Rs. 49 crores could not be recovered by REL-D.

25. In reply learned counsel for the Commission fairly stated that in its communication of April 4, 2007 to REL on approval of REL's FAC for July, 2006 to September, 2006, the Commission has approved the FAC of Rs. 49 crores payable to REL-G by REL-D based on the details submitted by REL-D and the Commission has also stated that: *"the Commission will consider the truing up of FAC for the entire year 2006-07 based on audited accounts for FY 2006-07 subject to prudence".* Learned counsel stated that the Commission has already committed for truing up of unrecovered FAC to be taken at the time of Annual Performance Review (APR) for FY 2007-08 when the audited accounts for FY 2006-07 will be available and the expenses and revenue of 2006-07 will be trued up.

26. In view of the position explained by the Commission we direct the Commission that the amount of Rs. 49 crores be allowed during truing up after verification of the same.

(E) Approval of Short Term Power Purchase at Rs. 4.41 per unit:

27. Learned counsel for the appellant submitted that REL in its MYT petition has considered the procurement of power from TPC-D at Rs. 4.41 per unit, being the rate as stated in MERC's earlier tariff order dated October 3, 2006 and that it intends to continue procuring additional power through TPC-D and that by an order dated April 30, 2007 in case No. 70 of 2006, passed in TPC-D's MYT petition, MERC has considered the rate of Rs. 5.50 per unit for estimating the cost of power purchase from external sources. She submitted that the power being procured from TPC-D as submitted by REL-D in its MYT petition at the same rate of Rs. 5.50 per unit ought to have been permitted and the same may be permitted to REL-D at the time of performance review as on November 30, 2007 as provided in the Tariff Regulations.

28. Learned counsel for the Commission fairly stated that MERC Regulations, 2005 have a provision under Regulation 82 for any variation in the fuel cost or power purchase cost which will be analyzed by the Commission every quarter and the reasonable variation will be passed on to the consumers through Fuel Adjustment Cost (FAC) and that in view of this there is no cause of concern for appellant as the difference between the projected power purchase cost and the actual

power purchase cost, if any, will be adjusted through FAC mechanism.

29. In view of the position explained by the Commission, we consider that no interference is required from this Tribunal in this regard as concedingly the Commission is obligated to allow recovery of incremental power purchase cost through FAC as per its Regulations 82. We direct the Commission accordingly.

(F) Capital expenditure not approved by the MERC on the ground that the Detailed Project Report (DPR) Schemes were not approved by MERC.

30. Learned counsel for the appellant stated hat REL-D proposed capital expenditure of Rs.530.13 crores, Rs.499.58 crores and Rs. 554.40 crores respectively for FY 2007-08, FY 2008-09 and FY 2009-10 and capitalization during the said period as Rs. 476.67 crores, Rs.506.79 crores and Rs.554.40 crores respectively and that REL-D's capital expenditure incurred in the past 4 years is as follow:

Year	Capex (Rs. Crore)
FY 03	119.43
FY 04	118.48
FY 05	174.55
FY 06	331.43

31. She stated that it was necessary to meet the new demand and to maintain the system and that these figures have not been disputed by MERC in the said affidavit. She submitted that along with DPRs for FY 05, FY 06 and FY 07, REL has submitted various schemes which were to be executed during FY 08 whose details and required information has been given as sought for by MERC but the same are pending approval with MERC. She stated that MERC in para 2.10 of its impugned order (Pg.478) has held, inter alia, as follows:

> *"The Commission considered only non-DPR schemes for approval towards capital expenditure for the control period in the ARR, as no DPR schemes have been approved 'in principle' for the control period due to lack of submission of DPRs by the licensee and lack of data. The Commission observed that despite*

the requirement of the licensee as per regulation 71 of MERC tariff regulations to submit detailed project reports (DPP's) for proposed schemes who total outlay is above Rs. 10 crore, REL-D has not submitted only DPRs for approval to the Commission."

32. She contended that the MERC on the aforesaid alleged ground permitted capitalization to the extent of Rs. 15.99 crores, Rs. 40.42 crores and Rs. 40.47 crores for FY 2007-08, FY 2008-09 and FY 2009-10 respectively which it erred in granting.

33. She submitted that MERC failed to appreciate that REL ought to have been given capital expenditure based on the DPRs pending for FY 2006 and FY 2007 which are awaiting clearance and all necessary details whereof have been duly submitted to MERC or at the least increment over the last years expenditure and that part of expenditure in relation to these DPRs have already been incurred by REL-D, and the balance would be carried out in the control period.

34. She contended that MERC erred in holding that REL lacked in submitting DPRs or data for the current year and that in any event, REL is in the process of supplying information data sought for by MERC in this regard and that REL-D is entitled to such expending as per the DPRs pending approval in FY 06 and FY 07.

35. Learned counsel contended that MERC erred in not approving capitalization as aforesaid especially in view of the expenditure already incurred by REL. She submitted that MERC, in its reply, has admitted that the approved DPRs for FY 2006-06 and FY 2006-07 and the actual investments against these schemes would be considered during the Annual Performance Review and that this Tribunal may be pleased to order accordingly.

36. Learned counsel for the Commission drew our attention to the decision of this Tribunal in its order dated August 29, 2006 in case of KPTCL Vs. KERC (Appeal No. 84 of 2006), wherein it was inter alia held as under:

"14.......Mere proposal to invest will not involve the liability either interest or finance charges eo instanti, but such charges may have to be incurred only when the amount is actually invested as planned. Till the investment is complete the utility is not entitled to claim either finance or interest or return on the investment."

"16......The regulator is not going to approve the expenditure or approve the financial charges just for asking and the regulator has to satisfy itself by a prudent check with respect to capital investment and in case they contribute for the quality or development or providing better service, the regulator may include and pass on the consequences of such investment to the consumers......."

37. He submitted that Regulations 71 and 72 of the MERC (Terms and Condition of Tariff) Regulations, 2005, requires the distribution licensee to submit annual rolling plan and the investment plan to the Commission for the approval and that the said Regulation requires approval of all the investment plans in excess of Rs. 10 crore by the Commission. The Regulations also require the Commission to approve

depreciation, interest and return on equity on the basis of approved investment only.

38. Learned counsel submitted that in accordance with its regulation, the Commission in para 2.10 of the Order has stated that:

> *" The Commission has considered only non-DPR schemes for approval towards capital expenditure for the control period in the ARR, as no DPR schemes have been approved 'in principle' for the control period due to lack of submission of DPRs by the licensee and lack of data. The Commission observed that despite the requirement of the licensee as per regulation 71 of MERC tariff regulations to submit detailed project reports (DPR's) for approval schemes whose total outlay is above Rs. 10 crores, REL-D has not submitted any DPRs for approval to the Commission.*
>
> *REL-D in its petition has submitted list of schemes which do not require DPR's (outlay less than or equal to Rs. 10 crore). As per the licensee submission the amount of*

capital expenditure for the non DPR schemes for the control period is Rs. 39.98 crore, Rs. 41.08 crore and Rs. 39.81 crores for FY 2007-08. FY 2008-09 and FY 2009-10 respectively. Based on past trends the Commission has considered the amount of capitalization on the total amount of capex on account of non-DPR schemes to be invested in the control period to be spread across two years in the ratio of 40% and 60%. While Commission has considered the capital expenditure on non-DPR schemes, it does not mean approval of capital expenditure of the schemes and that further analysis of non-DPR schemes would be undertaken by the Commission"

39. Learned counsel further submitted that the Commission would consider the approved DPRs for FY 2005-06 and FY 2006-07 and the actual investment against these schemes during the Annual Performance Review. We order accordingly.

(G) Income Tax.

40. Learned counsel for the appellant submitted that MERC in paragraph 13.3 of Chapter 3 (Pg. 457) of the impugned order has, in view of the order dated 4th April, 2007 passed by this Tribunal in Appeal No. 251 of 2006, held that the actual Income-tax payable by REL for its distribution business will be considered on a standalone basis and will be allowed and that MERC further held that accordingly, for the control period MERC has computed Income-tax as per the provisions of the Indian Income- Tax Act, 1961 and has ruled that the same will be trued up once the actual income tax figures are furnished.

41. She submitted that in the impugned order in para 2.15, Chapter 4 thereof (Pg.484), while referring to the said order of this Tribunal and following the same, the MERC has arrived at the tax amount of Rs. 65.90 crore but has held that *"This amount would be trued up in subsequent review by Commission when the information on actual tax paid by REL-D would be available."* She further submitted that MERC in the said

affidavit has merely reproduced the extracts of para 3.13 of Chapter 3 and para 2.15 of Chapter 4 whilst stating that the Commission has implemented the Ruling of this Tribunal dated 4th April, 2007 in Appeal No. 251 of 2006. The finding of the Commission that the amount of Income-Tax would be trued up in subsequent review by MERC when the information on 'actual tax paid' by REL would be available, is contrary to the finding of this Tribunal. She asserted that MERC has wrongly reiterated in the said reply that the income-tax based on actual tax paid as against the actual tax payable by REL for its distribution business would be trued up. She emphasized that as per decision of this Tribunal, the Commission ought to consider the tax payable by REL (D).

42. Learned counsel submitted that MERC has placed reliance on Regulation 63.2.2 in the said affidavit of the Regulations, which is extracted herein below:

> *"63.2.2 The Distribution Licensee shall include an estimate of the income-tax liability of his Distribution business*

along with the application for determination of tariff, based on the provisions of the Income-Tax Act, 1961:

> *"Provided that any change in such income-tax liability on account of assessment under the Income-Tax Act, 1961 shall be dealt with as being on account of uncontrollable factors:*
>
> *Provided further that any change in such income-tax liability on account of changes in the provisions of the Income-Tax Act, 1961 shall be dealt with as being on account of uncontrollable factors;*
>
> *Provided further that any change in such income-tax liability on account of change in income of the Distribution Licensee from the approved forecast shall be attributed to the same controllable or uncontrollable factors as have resulted in the change in income and shall be dealt with accordingly."*

43. She contended that the said Regulation in fact permits a distribution licensee to include an estimate of the income-tax

liability of his distribution business in determination of tariff and submitted that the said finding in para 2.15 (Pg.484) of the impugned order is contrary to and inconsistent with the order of this Tribunal dated 4th April 2007 as well as MERC's ruling in para 13.3 of the impugned order and that MERC erred in holding that the amount of Rs. 65.19 crores would be trued up when information on actual tax paid by REL-D would be available.

44. She pleaded that this Tribunal may be pleased to set aside the finding of MERC in so far as it holds that the amount of Rs. 65.19 crores (allowed to REL-D as Income-Tax payable by REL-D's business as stand alone) would be trued upon when information on actual tax paid by REL would be available.

45. Learned counsel for the Commission stated that this Tribunal in para no. 32 of its order dated April 4, 2007 for appeal No. 251 of 2006, held with regard to the computation of income tax as given below:

" the consumers in the licensees area must be kept in a water tight compartment from the risks of other business of the licensee and the Income Tax payable thereon. Under no circumstance, consumers of the licensee should be made to bear the Income Tax accrued in other businesses of the licensee. Income Tax assessment has to be made on stand alone basis for the licensed business so that consumers are fully insulted and protected from the Income Tax payable from other businesses."

46. He contended that the Commission has implemented the above ruling while allowing the Income Tax for the control period. The Commission in para 3.13 of Chapter 3 of the impugned order has stated that:

" The Commission opined that the computation of tax by grossing up of Return on Equity (RoE) is not a correct approach. The ATE, in its order dated April 4, 2007 for appeal No. 251 of 2006, agrees with this opinion of the Commission. The Commission in line with the ATE order dated April 4, 2007, rules that the actual income tax payable by the licensee for the distribution business considered on a stand alone basis, will be allowed. Further, for the control period the Commission has computed the income tax as per the provision of Income

Tax, 1961 and has ruled that the same will be trued up once the actual audited tax figures are furnished".

47. It was contended by the learned counsel that the Commission has further elaborated in the para 2.15 of Chapter 4 of the order, as follows:

" After considering the ATE's order, the Commission has adopted the Profit Before Tax (PBT) approach for projecting the tax for the control period. As per this approach, the Commission has assumed the approved ARR as the projected revenue from the business and has computed the profit before tax by deducting the various expense head like fuel cost, O&M expense, depreciation, interest on long term loan and interest on working capital. Then the applicable tax rate is applied to this PBT to arrive at the tax that might be due in FY 2007-08. The tax rate of 30% is applied with surcharge of 10% and education cess of 3%. Taking this into consideration the Commission arrives at a tax amount of Rs. 65.19 crore. This amount would be trued up in the subsequent review by the Commission, when the information on actual tax paid by the REL-D would be available".

48. He emphasized that the Commission is thus consistent in para 3.13 of Chapter 3 and para 2.15 of the Chapter 4 and

that the Commission would also like to state that the truing up of income tax based on the actual tax paid as per the audited annual accounts is consistent with the Regulation 63.2.2 of MERC (Terms and Conditions of tariff) Regulation, 2005 and hence there is no cause to modify the Commission's order in this regard.

Analysis and decision:

49. The Commission, in line with this Tribunal order dated April 04, 2007, has ruled that the actual income tax payable by the licensee for the distribution business considered on a standalone basis will be allowed. The Commission has also ruled that the income tax will be trued up once the actual audited tax figures are furnished. We hold the view that the Commission has to ensure that the consumers in the licensee's area are always protected from the burden of the income tax on account of other businesses of the licensee. It may happen, during any year, that the distribution company entails losses whereas there are enormous profits for other businesses of the REL. If the Commission was to apply the

criteria of *actual tax paid* even the consumers of the distribution licensee will have to bear the brunt of income tax whereas they would not have to pay any tax as the licensee's distribution business has suffered losses. On the other hand it may happen that the distribution business of the licensee has earned profits but other businesses suffer losses. In this case the overall income tax payable by the umbrella company may be Nil due to the losses of other business. It has to be borne in mind that as per the Income Tax Act the losses occurred during a year can be set off against the profits during the following years. In this context the relevant section 72 of the Income Tax Act is extracted below:

*"**Carry forward and set off of business losses**.*

72. (1) Where for any assessment year, the net result of the computation under the head "Profits and gains of business or profession" is a loss to the assessee , not being a loss sustained in a speculation business, and such loss cannot be or is not wholly set off against income under any head of income in accordance with the provisions of section 71, so much of the loss as has not

been so set off or, where he has no income under any other head, the whole loss shall, subject to the other provisions of this chapter, be carried forward to the following assessment year, and-

(i) it shall be set off against the profits and gains, if any, of any business or profession carried on by him and assessable for that assessment year;

(ii) if the loss cannot be wholly so set off, the amount of loss not so set off shall be carried forward to the following assessment year and so on.

Provided that where the whole or any part of such loss is sustained in any such business as is referred to in section 33B which is discontinued in the circumstances specified in that section, and, thereafter, at any time before the expiry of the period of three years referred to in that section, such business is re-established, reconstructed or revived by the assessee, so much of the loss as is attributable to such business shall be carried forward to the assessment year relevant to the previous year in

which the business is so re-established, reconstructed or revived, and-

(a) it shall be set off against the profits and gains, if any, of that business or any other business carried on by him and assessable for that assessment year; and

(b) if the loss cannot be wholly so set off, the amount of loss not so set off shall, in case the business so re-established, reconstructed or revived continues to be carried on by the assessee, be carried forward to the following assessment year and so on for seven assessment years immediately succeeding.

(2) Where any allowance or part thereof is, under sub-section (2) of section 32 or sub-section (4) of section 35, to be carried forward, effect shall first be given to the provisions of this section.

(3) No loss (other than the loss referred to in the proviso to sub-section (1) of this section) shall be carried forward under this section for more than eight assessment years

immediately succeeding the assessment year for which the loss was first computed.

50. The criteria is that in spite of the enabling provision of the Income Tax Act the liability of the income tax out of other businesses cannot be allowed to be passed on to the consumers of the distribution licensee. It is equally just, fair and equitable that the reverse also does not happen i.e. the liability of income tax pertaining to the distribution business is not passed on to the other businesses.

51. In view of the foregoing discussions we decide that the income tax to be allowed must be worked out on the basis of *the income tax payable solely on account of the distribution business of the licensee.* We, therefore, decide accordingly and allow the appeal in this view of the matter.

(H) Standby charges:

52. Though the issue of standby charges has been raised in the Memorandum of Appeal and the Written Submission, the

appellant has prayed that this issue may be deferred and heard along with AFR No. 944/07 filed by it before this Tribunal. We order accordingly.

Employee Expenses:

53. Learned counsel for the appellant contended that MERC ought to have allowed additional employee expenses towards wage revision. She submitted that MERC, in its affidavit has fairly stated that it would examine the reasonableness and prudence of costs incurred once the audited expenses are submitted.

54. Learned counsel for the respondent Commission submitted that the Commission had not considered the impact of wage revision as during the MYT process the appellant had not entered into any agreement with the employees union and had neither apprised the Commission after having entered into an agreement on April 19, 2007. He fairly stated that the Commission, according to the MERC (Terms and Conditions of Tariff) Regulations, 2005 would true up various costs of the utility based on the reasonableness and prudence of the costs

incurred, once the audited expenses are submitted to the Commission.

55. In view of the aforesaid submissions of the appellant and the respondent Commission, we direct that while truing up the Commission may allow the actual incremental expenditure due to wage revision subject to prudence check.

56. In the result, the appeal is allowed to the extent indicated herein above.

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

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No. of corrections