

Comments on the discussion paper – Auction of mines for sale of coal

Prayas (Energy Group), January 2020

The following are comments and suggestions from Prayas (Energy Group) on the discussion paper on ‘Auction of Mines for Sale of Coal’ published by the Ministry of Coal in January 2020. We request you to take them into consideration while finalising the methodology for auction of mines for sale of coal.

Comments on the discussion paper

1. **Promoting competition:** The Mineral Laws (Amendment) Ordinance, 2020 lowers the entry barrier for firms to participate in the bidding process for coal mines in India in an attempt to promote competition. While this is a laudable move, we would like to bring attention to related two points in this regard:
 - a. The eligibility criteria, bid security, performance security and other such conditions in the final offer document should ensure that only serious players participate in bidding and win mines. The experience of block allocations for captive use before the promulgation of the CMSPA 2015, when many non-serious players acquired coal blocks which were never developed, should be a useful reminder in this regard.
 - b. Given that Coal India Ltd. (and other public sector miners) will continue to be allotted mines with no revenue share requirements, and given the global reduction of interest in investing in coal¹, it is quite likely that investor and bidder interest, particularly from reputed international players, would be muted.
2. **National Coal Index:** The National Coal Index (NCI) is a very important element in the entire scheme as revenue sharing (and related payments such as the upfront payment) would be based on it. However, the NCI is not yet finalized and hence unknown, thus making it difficult to comment about the revenue sharing mechanism. Therefore, we suggest that
 - a. the NCI should be finalized only after comments are sought from the public and all stakeholders and incorporated and
 - b. the methodology for auction of mines for sale of coal should be finalized only after the NCI is finalized to ensure that they are in harmony.
3. **Revenue sharing:**
 - a. The quantity of coal produced each month is a crucial parameter to determine the revenue share. However, it is not clear how this quantity would be determined on a monthly basis in a fair and transparent manner. The methodology for this should be clearly defined and it should include some measure of independent verification. Relying on sale invoices will not be appropriate for two reasons. One, the revenue sharing in the proposed scheme is based on *production* rather than sales. Two, since the proposed scheme allows for self-consumption, sale to affiliates and export of coal, sales invoices may not provide independent validation of actual sales.

¹ The most recent announcement to exit from coal was by the world’s largest fund manager, BlackRock.

- b. It is not clear from the discussion paper whether the revenue that would be generated from coal production (based on the bids) would be payable to the respective state government or the central government. This should be clarified.
4. **Allowing export of coal:** The proposed scheme allows export of coal by the winning bidder. Allowing export of coal when the stated aims of the government include reducing of imports and promote competition within the domestic coal industry does not seem appropriate. Moreover, the NCI would be based on Indian coal prices implying that government revenue would be calculated based on Indian prices. However, the miner's revenue would be based on international prices when the coal is exported, leading to the possibility of super-normal profits. This would also incentivise bid winners to export coal rather than sell in the domestic market, thus defeating both the objectives of addressing domestic coal shortage and promoting competition in the domestic coal sector. Hence, we strongly suggest that export of coal by the successful bidder should not be allowed, until such time as India becomes self-sufficient in (at least) thermal coal.
5. **Pricing of coal:** The provision allowing sale of coal to affiliated parties and for self-consumption may make it administratively easier to manage the sector. However, it risks potential foul-play or gaming, wherein miners could offer coal selectively to affiliates or themselves at preferred prices and others at expensive prices, thus defeating the purpose of fair competition in the sector². Moreover, as indicated earlier, in such cases it would also be difficult to ascertain the actual quantity of coal production or sale independently. Given these weaknesses, we suggest that all coal sale from auctioned mines happens on a transparent, double-blind exchange platform where sellers and buyers interact and prices are discovered truly competitively. Such a platform can also be very useful as the basis for the proposed NCI. Ideally, even CIL (and other public sector miners) should sell their coal through the same platform, making it India's single coal transaction platform. This platform could be similar to the platform envisaged for SHAKTI B(iii) auctions, but with additional features of better transparency, double-blindness and allowing multiple sellers and buyers. An example of such a functioning exchange in the energy space in India today is the IEX for electricity.
6. **Coal sale contracts:** The current discussion paper does not state anything about the duration of coal sale contracts. Given the uncertainties around demand for coal going forward, we suggest that coal sale contracts should not be for long-term durations such as 25 years as is currently the practice. Instead, they should be for shorter terms (say, 3 to 5 years), with more frequent coal sale auctions being conducted. Once again, this point is also relevant to SHAKTI B(iii) auctions, since materially SHAKTI B(iii) auctions and coal sale contracts under this dispensation are similar in nature. The acceptable duration of these contracts should be finalized based on discussions with the Ministry of Power, since they should roughly correspond to Power Purchase Agreement (PPA) contracts. We firmly believe that new PPAs for coal-based generation should also not be of 25-year duration but much shorter.
7. **Other points**
- The details of the electronic auction process are not clear from the discussion paper. For example, it is not clear whether it would be a single-step auction where all qualified bidders get just one chance to submit a bid, or would it be a multiple step auction where bidders

² The pricing controversy around domestic natural gas from the KG D6 basin would be instructive in this regard.

- may bid multiple times – and if so, how the winner would be chosen. The final offer document should lay out this process in detail.
- b. The fixed amount to be paid includes the cost incurred by CMPDIL for preparation of the mine dossier. It should be made clear how these costs would be estimated and validated. Moreover, the cost for preparation of the mine dossier should be published along with other details of each mine being offered during the auction process, so that there are no disputes or confusion later.
 - c. Some of the provisions in the discussion paper – for example, the need to produce at least 50% of the approved mine plan and the need for the miner to produce a mine plan whose year-on-year production profile would be higher than the tentative production profile – may be too restrictive, given the uncertainty of future coal demand, particularly considering that mine life is likely to be upwards of 25 or 30 years.

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