Submission related to Order(s) issued by the Commission regarding the petition No.159/MP/2012 (Tata / CGPL Mundra UMPP)and the committee report in this regard

By
Prayas (Energy Group), Pune
Consumer Representative u/s E. Act 2003

1 November 2013

Outline

- Background and context
- Process shortcomings
- Committee Recommendations: Winners & losers
- Methodological and Analytical Shortcomings in the Committee Report
- Way forward

Background & Context

Main contentions raised by the petitioner

- Petitioner has sought relief under:
  - Article 13 of the PPA dealing with ‘Change of Law’
  - Article 12 of the PPA dealing with ‘Force Majeure’ events
  - Section 79 of the Electricity Act 2003 urging commission to intervene and help the petitioner to achieve a tariff that will be financially viable

Gist of the majority order

- Para 69: "*We have considered the submissions of the parties. For the reasons already recorded, the case of the petitioner **does not fall under either Change in Law or Force Majeure**."*

- Para 86, the commission notes as follows: *"The Electricity Act, 2003 vests in the Commission the responsibility to balance the interest of the consumers with the interest of the project developers while regulating the tariff of the generating companies and transmission licensees....In our view, under the peculiarity of the facts of the present case and also **keeping in view the interest of both project developer and consumers**, we consider it appropriate to direct the parties to set down to a **consultative process to find out an acceptable solution** in the form of compensatory tariff over and above the tariff decided under the PPA to **mitigate the hardship arising out of the need to import coal at benchmark price on account of Indonesian Regulations**." (emphasis added)*

Committee Recommendations: Winners & losers

Recommended formula for gross compensatory tariff

- *Gross Compensatory Tariff (GCT) = Normative Fuel Energy charges - Tariff recovered from Fuel Energy components of PPA*
  - Adjustments for Profits accruing to the Promoters from the Indonesian mines
  - Adjustment for profit from third party sale of power beyond Normative Availability

Committee's calculation of compensatory tariff for FY 2014 (page no 37)

The compensatory tariff calculation for FY 2014 is shown below:

Item	Ref	Unit	Value
Units sold	(18)[22]	mil kWh	26630
Fuel charges (only FOB) as per tariff	(19)[23]	USD/kWh	0.01856
Fuel charges recovered	(20)[24]	mil USD	494.27
FOB cost of imported coal	(21)[25]	USD/ton	63.78
FOB cost of imported coal – adjusted for taxes	(22)[26]	USD/ton	67.82
Normative Quantity of coal imported	(23)[27]	mil ton	11.15
Normative Cost of coal imported	(24)[28]	mil USD	756.25
Gross Compensation	(25)[29]	mil USD	261.99
Gross Compensation	(26)[30]	mil INR	15640.53
Gross Compensation per unit	(27)[31]	INR/kWh	0.59

Implications of committee recommendation: Impact on different stakeholders

- Increase in tariff beyond PPA tariff : **Rs. 1,564 Cr** per year
  - Loss in profitability of developer / equity holder: Rs. 0.00 Cr. (as compared to coal prices at the time of bidding)
  - Loss to lenders : Rs. 0.00 Cr.
  - Loss to procurer : Rs. 0.00 Cr. (As the entire cost can be passed through to consumers, based on regulatory approval)
  - Loss to consumers : **Rs. 1,564 Cr**

➔ *Takes away all the commercial risk on account of fuel price variation, which the developer had taken willingly at the time of bidding.*

➔ *Committee recommendations imply CGPL as well as mining operations not sharing any burden on account coal price increase*

Methodological Shortcomings
Issue 1:
Profits from shareholding in the Indonesian mines

Possible approaches

- Approach 1: Based on audited financial statements, calculate Generator's proportionate share in mining profits and deduct the same

- Approach 2: Calculate increased revenue based on incremental rise in price of coal over and above the price CGPL could have contracted in absence of the Indonesian Regulation, after accounting for taxes and duties. Use this revenue to offset the impact on tariff

Committee recommended Approach for calculating impact on tariff for FY 13 (page 44)

Particular	Reference	Unit	Value
Tata Power share of net PAT from KPC	(1)	mil USD	1.022
Tata Power share of net PAT from Arutmin	(2)	mil USD	0.964
Total Tata Power share of Profit from KPC & Arutmin	(3)=(1)+(2)	mil USD	1.986
Exchange Rate	(4)	INR/USD	59.7
Total Tata Power share of Profit from KPC & Arutmin	(5)=(3)*(4)	Mil INR	118.564
Units supplied by CGPL to procurers in FY 2013	(6)	mil units	11565
Impact on Compensatory tariff	(7)=(5)/(6)	INR/kWh	0.01

Alternate approach (not recommended by committee)

Particular	Reference	Unit	FY 13
FOB selling price of the Indonesian mining company as per invoice	[A]	$/ton	
Contracted Price as per FSA	[B]	$/ton	
Incremental revenue to Indonesian mining company per ton	[C] = [A] – [B]	$/ton	
Less: Royalty @ 13.5%	[D]= [C*13.5%]	$/ton	
Revenue net of Royalty per ton	[E] = [C] – [D]	$/ton	
Less: Income tax at marginal rate @ 45%	[F] = [E * 45%]	$/ton	
Incremental Profit to Indonesian mining company per ton	[G] = [E] – [F]	$/ton	
Quantity supplied to CGPL by the mining company	[H]	Mil Ton	
Net incremental PAT to Indonesian mining company	[I] = [G] * [H]	Mil $	
Tata Power share of net incremental PAT of mining company	[J] = [I * 30%]	Mil $	1.053
Dollar-rupee conversion rate	[K]	Rs	59.7
Tata Power share of net incremental PAT of mining company	[L]= [J]* K] /10	Rs Cr	6.28641
Units sold		Mil kWh	11565
Relief on this account		Rs/unit	0.005

Impact as per the Alternate approach

Particular	Reference	Unit	FY 13	CGPL Petition	Prayas suggestion
				FY 14	FY 14
FOB selling price of the Indonesia mining company as per invoice	[A]	$/Ton		63.67	63.67
Landed cost of coal as per PPA quoted tariff at which the petitioner is revenue neutral	[B]	$/Ton		50.92	41.68
Incremental revenue to the mining company per ton	[C] = [A] - [B]	$/Ton		12.75	21.99
Less: Royalty @ 13.5%	[D] = [C*13.5%]	$/Ton		1.72	2.97
Revenue net of Royality per ton	[E] = [C] - [D]	$/Ton		11.03	19.02
Less: Income tax at marginal rate @ 45%	[F] = [E*45%]	$/Ton		4.96	8.56
Incremental Profit to Indonesia mining company per ton	[G] = [E] - [F]	$/Ton		6.07	10.46
Quantity supplied to CGPL by the mining company	[H]	Million Ton		11.15	11.15
Net incremental PAT to Indonesia mining company	[I] = [G] * [H]	Million $		67.63	116.65
Tata Power share of net incremental PAT of mining company	[J] = [I * 30%]	Million $	1.053	20.29	34.99
Less: Indian Tax (on dividend received)@15% for FY-14	*[K] = [J * 15%]*	*Million $*		*3.04*	*5.25*
Dollar-rupee conversion rate	[L]	Rs	59.7	59.7	59.7
TPC share of net incremental PAT of mining company	[M] = [L]*[J-K]/10	Rs Cr	6.286	102.96	177.58
Total Units to be sold	[N]	Mil kWh	11565	26630	26630
Relief on this account factor	[O]=[M]*[N]	Rs/unit	0.005	0.04	0.07

Methodological Shortcomings

Issue 2: Sell of generation beyond normative availability to third parties

Committee approach (page 46)

		Scenario 1	Scenario 2	Scenario 3	
Normative Availability	%	80%	80%	80%	As per PPA
Third party Sale	%	5%	10%	20%	If allowed sale to third party
Third party sale Price	INR/kWh	4	4	4	
Energy Charges	INR/kWh	2.24	2.24	2.24	
Per Unit Surplus	INR/kWh	1.76	1.76	1.76	Sale price – Energy charges
Incentive to generator	INR/kWh	0	0.13	0.19	Incentive beyond 85% apportioned on entire quantum of 3rd party sale
Share of Procurers @50% of balance surplus	INR/kWh	0.88	0.82	0.79	50% share
Reduction in Gross Compensatory tariff	INR/kWh	0.055	0.1022	0.1965	Procurer share apportioned on 80%

→ *Seller can keep the share of incentives over and above the compensation*

Actual sharing of revenue from sale of power beyond the target availability

		Scenario 1	Scenario 2	Scenario 3
Normative Availability	%	80%	80%	80%
Third party Sale	%	5%	10%	20%
Third party sale Price	INR/kWh	4	4	4
Energy Charges	INR/kWh	2.24	2.24	2.24
Per Unit Surplus	INR/kWh	1.76	1.76	1.76
Surplus Mus	MU	1664	3329	6658
Additional revenue	Rs Cr	293	586	1172
Impact on compensatory tariff	Rs/unit	*0.11*	*0.22*	*0.44*

Similar approach has also been proposed by one of the procurers

Salient observations…1

- Combination of following options will significantly offset impact on tariff due to Indonesian Regulations
  - Plough back of incremental revenue (net of tax and royalty) from coal mines
  - Sale of generation beyond normative availability and entire surplus used to offset impact on tariff
  - Reduction in costs due to measures such as low GCV coal, low transportation costs, other sources of coal etc.

Salient observations…2

- Analysis highlights serious lacunae in both methodology and analysis of the committee
- Hence commission cannot rely on committee recommendations for deciding either methodology or impact on tariff
- Need for independent evaluation on part of commission in this regard

Prayas Submission…1

- Independently establish the need and extent of compensation:
  - CERC must establish beyond doubt the need for compensatory tariff
  - All analysis, documents and assumptions used by the Commission in this regard should be made public

- Define principles for awarding any compensation
  - CERC should ensure that its order does not set any wrong precedent for revising competitively discovered tariffs.
    - Specially crucial considering number of such cases before CERC and other state commissions.
  - Therefore, if need for compensation is established, then any proposed solution must adhere to following criteria:
    - Not fundamentally alter risk allocation in the bidding process and PPA
    - Procurers maximum entitlement should be protected (i.e. normative generation at PPA tariff)
    - Equitable sharing of incremental burden by all stakeholders (developer, lenders and consumers)

Prayas Submission…2

– Undertake due public process, including public hearing, which is an established practice for any tariff revision and also mandatory as per law

Prayas Submission…3

- Return the generation assets at the end of PPA:
  - Allowing compensation would imply pass through of the commercial risks, voluntarily assumed by the project developer to win the contract, to consumers.
  - Asset supported and sustained in this manner should ultimately belong to the consumers.
  - Hence, entire generation asset supported by such mechanism should be returned to the consumers at the end of term, at an appropriate transfer price.
  - Actual mechanism to be adopted for transferring these assets should be decided based on public consultation.

Thank you

Prayas (Energy Group)

www.prayaspune.org/peg