

MAHARASHTRA ELECTRICITY REGULATORY COMMISSION

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Case No. 5 of 2011

In the matter of

Application of Indiabulls Power Limited for grant of Distribution Licence in the area of supply served by R-Infra-D in the Suburbs of Mumbai

Shri V.P. Raja, Chairman
Shri Vijay L. Sonavane, Member

Indiabulls Power Limited
“Indiabulls House”, 448-451,
Udyog Vihar, Phase V,
Gurgaon - 122001

....Applicant

ORDER

Dated: August 11, 2011

Background

The Commission published an ‘Invitation for Expression of Interest for Distribution of Electricity in the Suburbs of Mumbai’, on October 6, 2010. This was in the backdrop of the date of expiry on August 15, 2011 of the licence of Reliance Infrastructure Limited (RInfra) to distribute electricity in the suburbs of Mumbai.

2. In response, by November 4, 2010, the Commission received Expressions of Interest (EoI) from the following eight applicants, namely, Maharashtra State Electricity Distribution Company Limited; Torrent Power Limited; DPSC Limited; Lanco Infratech Limited; GMR Energy Limited; Indiabulls Power Limited; Tata Power Company Limited; and Enzen Global Solution Pvt. Limited. Subsequently, the Commission advised all these applicants through separate letters to submit applications for grant of Distribution Licence before the Commission in accordance with the applicable Regulations of the Commission and the provisions contained in the Electricity Act 2003 (hereinafter referred to as the “2003 Act”).

3. Four out of the above eight applicants, namely, Lanco Infratech Limited (LITL), Indiabulls Power Limited (IPL), Torrent Power Limited (TPL) and Maharashtra State Electricity Distribution Company Limited (MSEDCL) applied for the Distribution Licence.
4. IPL filed an application on January 17, 2011, registered as Case 5 of 2011, as per the provisions of Section 14 read with Section 15 of the 2003 Act and in accordance with the provisions of the MERC (General Conditions of Distribution Licence) Regulations, 2006. In its application, IPL did not mention specific prayer. However as part of Form II of application format, it has mentioned,

IN THE MATTER OF: The Public Notice dated 6th October 2010 issued by the Honourable Commission for "Invitation for Expression of Interest for distribution of electricity in the suburbs of Mumbai."

AND

IN THE MATTER OF: The application for "Electric Distribution " under Section 14 of the Electricity Act 2003 by Indiabulls Power Limited in the suburbs of Mumbai"

5. The Technical Validation Session (TVS) for IPL's application was held in the presence of authorised consumer representatives on February 23, 2011 at the Commission's office. IPL was asked to clarify and satisfy the Commission as to how it proposed to meet the requirement of economical power along with power procurement plan for meeting 24 x 7 power demand (existing and projected) in the Mumbai Suburban area; and whether there are any inter-state/intra-state transmission bottlenecks in bringing power from its proposed source. The application submitted by IPL was analysed for data gaps. The details of IPL's application were hosted on the website of IPL on May 10, 2011.

Admission of IPL's application and Public Notice

6. After having examined the data gaps, and holding of Technical Validation Session (TVS), the Commission admitted IPL's application for Grant of Distribution Licence on May 5, 2011 and directed IPL to issue a Public Notice on or before May 10, 2011 in compliance with Section 15(2) of the 2003 Act read with Regulation 5.3 of MERC (General Conditions of Distribution Licence) Regulations, 2006.
7. IPL informed the Commission that it published a notice on May 10, 2011, of its application for grant of Distribution Licence in two (2) daily English newspapers (Financial Express & Indian Express) and in two (2) daily Marathi newspapers (Lokmat and Loksatta) in the proposed area of supply. A copy of the same was made

available on the Commission's as well as the IPL's websites. IPL invited suggestions and/ or objections on its application within thirty (30) days from the date of publication of notice.

8. Subsequently on June 20, 2011, IPL revised the proposed area of supply in its application. An addendum to the aforesaid public notice was published by IPL on June 24, 2011 in two (2) daily English newspapers (Financial Express and Indian Express) and in two (2) daily Marathi newspapers (Lokmat and Loksatta) to notify this amendment in its application. A copy of the same was made available on IPL's websites. According to the addendum, IPL invited suggestions/ objections on its application within thirty (30) days from the date of publication of that addendum. The objections received in response to both the first notice and the addendum have been analysed in the subsequent portions of this Order.
9. In accordance with Section 15 (2) (ii) of the 2003 Act, and in order to ascertain whether the Central Government could have any objection to the grant of licence, in the event the proposed area of supply included the whole or any part of any cantonment, aerodrome, fortress, arsenal, dockyard or camp or of any building or place in the occupation of the Central Government for defence purposes, the Commission issued letters to the concerned Ministries of the Central Government (Ministry of Defence, Ministry of Civil Aviation, and Ministry of Shipping) inviting objection(s), if any, with reference to the application of IPL for grant of Distribution Licence. The Commission did not receive any objection in this respect within 30 days from the date of the issuance of the said letters.

Objections raised against the application of IPL

10. In response to the Public Notice published by IPL of its application for grant of Distribution Licence, the Commission received several objections from various stakeholders and members of the public against the application submitted by IPL. These objections have been classified broadly under the following heads depending on the reason for which such objections have been raised.

Objection 1: Lack of previous experience in distribution of electricity

Some of the consumers have objected that IPL does not have enough experience in distribution of electric power. They mentioned that IPL does not have enough skilled manpower to take over the distribution area of existing licensee. It will be difficult for IPL to handle "bulk VIP customers" having high power consumption and to give them full service to their satisfaction. Some consumers also suggested that prior experience in distribution of electricity should be assigned a weight while selecting a distribution licensee.

IPL's response

IPL has submitted that it has adhered to all the requirements of the regulatory procedure in its application for award of distribution licence for the said area. Owing to the limited opportunities available for private sector participation in the business of power distribution in the country, the applicant does not have prior experience in the business of power distribution. Additionally, the spirit of the 2003 Act is to promote private investments and efficiencies in the power sector in all the business functions – generation, transmission and distribution. It is in this spirit and acceptance of new players with no prior experience, that the country today enjoys a comfortable position in the projected demand supply scenario in the 12th Plan. Almost two-third of the investment planned in generation projects is from the private sector. IPL appealed that given a chance, it shall strive to emerge as the preferred supplier of electricity in the suburbs of Mumbai as it has achieved in every other business segment where it operates.

The IPL group has repeatedly demonstrated its skills at building businesses and execution of projects. The success of the group is recognized all over the country and is often used as a benchmark. With substantial experience and highly successful retail customer service record in the Financial Services domain, real estate and power generation the Group is appropriately positioned to meet the challenge of improving the procurement efficiency of Mumbai's licensed area, while also being capable of taking up necessary capital investments and meeting customer service obligations in electricity distribution.

Commission's view

Although, the 2003 Act does not mandate having prior experience in distribution of electricity as a pre-condition for grant of distribution licence, the objections raised have to be seen in the context of the vast experience of over several decades of the present incumbent Licensee (i.e., Bombay Suburban Electricity Supply Company Limited renamed as BSES Ltd., renamed as Reliance Energy Limited and thereafter renamed as Reliance Infrastructure Limited). Thus, IPL's lack of experience in the business of electricity distribution has been raised as a concern by members of the public because they feel that it is critical to ascertain the ability of the applicant in terms of well-trained staff and the requisite systems to distribute electricity to about 28 lakh consumers, given the importance of electricity to the common public and its commercial importance in a city like Mumbai. The Commission is of the view that one will have to view the experience shown by IPL in its documents in the context of the vast experience of over several decades of the present incumbent Licensee and whether IPL's experience favourably compares with that of the present incumbent Licensee. The Commission will take the decision, of granting of licence, keeping in view the interest of the consumers.

Objection 2: IPL has not met the requirement of minimum area of supply

Some of the consumers have objected that the proposed area of supply in the application IPL does not cover the minimum area requirement as specified in Rule 3 with sixth proviso to section 14 of the 2003 Act as done by RInfra by including villages Chene & Varsova.

IPL's response

No response has been received from the applicant in this regard.

Commission's view

The Commission notes that IPL has not responded to this objection. However, the Commission observed that IPL has published an addendum to its public notice mentioning the addition of the areas of Chene and Varsova of Mira Bhayandar Municipal Corporation to its proposed area of supply that is the area of supply served by the existing licensee (viz., RInfra) in order to comply with the minimum area of supply criteria prescribed in the Distribution of Electricity Licence (additional requirements of Capital Adequacy, Creditworthiness and Code of Conduct) Rules, 2005, and informed the Commission accordingly.

Objection 3: Proposed power procurement plan indicates supply arrangement of existing licensee. There is no clarity regarding the sources for procuring power. IPL's power procurement plan does not consider competitive bidding.

Existing licensee RInfra and some of the consumers have objected that IPL in its business plan has considered power from Dahanu power plant of existing licensee, which is an unlikely scenario. One objector also highlighted that IPL's business plan shows that the power sought for the proposed area of supply would be procured from its own generation and not through competitive bidding. Such proposition would be against the Commission's direction regarding procurement of electricity through competitive bidding.

IPL's response

IPL submitted that as per Honourable Commission's directives, various scenarios/business models have been analyzed and the financial impact on the cost to serve has been worked out and submitted to the Commission for evaluation. The various scenarios and business models submitted in the business plan include:

- a) Base case with long term power procurement not available from Dahanu Power

- b) Distribution Licence for partial distribution area of South Zone + East Zone with/ without Dahanu Power
- c) Distribution Licence for partial distribution area of South Central Zone + Central Zone + North Zone with/ without Dahanu Power
- d) Retail supply segregated from wires business for entire licence area
- e) Third parallel licensee

There is a major difference in the cost of supply of each licensee operating in Mumbai region, owing primarily to the varying power purchase cost incurred by the licensees. The existing licensee has experienced a declining portfolio of long term sources and a corresponding increase in short term power at very high cost, resulting in an increasing trend of retail tariffs in its area of supply. MERC intended to generate various options, which would primarily address the issue of lowering cost of supply to benefit the consumers in the area of supply of existing licensee. Considering this, IPL has submitted a business plan which is most suitable to the present scenario. Based on the appropriate clarification and justifications received from the bidders on the comments raised by the stakeholders, the Commission may decide on the next steps.

There is a possibility that the cost of power purchase reduces significantly from its present level and accordingly, the consumers of Mumbai suburban area may get better tariffs. The process for entering into definitive contractual arrangements for purchase of the proposed power shall be subject to the provisions of the Electricity Act, 2003, National Tariff Policy, Competitive Bidding Guidelines and the relevant Regulations put in place by the Hon'ble Commission, which are applicable to distribution licensees.

IPL submitted that it is in the process of developing 5,400 MW of thermal power plants in the State of Maharashtra at Nasik and Amravati. However, as per the MERC (General Conditions of Distribution Licence) Regulations, 2006, a Distribution Licensee shall purchase electricity from other sources through agreements for purchase of power for distribution and supply within the area of supply and for meeting the obligations under the Licence and under the provisions of the Act only after seeking due approval of the Commission. Also, such procurement shall be made in an economical manner under a transparent power purchase and procurement process which shall be required to be in accordance with the regulations, guidelines, directions made by the Commission from time to time. Thus, the firm price shall be discovered through a transparent bid process under the Case-1 route after getting Distribution Licence. IPL can't commit any power from its upcoming power plants for the Mumbai suburb area as the same has to be decided through a competitive bidding process with due approval of MERC. IPL's generating plants may participate in such a competitive bidding process and will decide as and when such process is declared.

The reduction in power purchase cost in 2013-14 is envisaged primarily on the basis of availability of cheaper sources of power through competitive bidding. The power

purchase costs for the base year case as presented in the business plan are as shown below;

| Particulars | 2011-12 (Part year) | 2012- 13 | 2013- 14 | 2014- 15 | 2015- 16 | 2016- 17 |
|--|--------------------------------|---------------------|---------------------|---------------------|---------------------|---------------------|
| Average power purchase cost (Rs./ kWh) | 4.08 | 4.17 | 3.35 | 3.52 | 3.7 | 3.89 |

The average power purchase cost per unit as indicated above is the basis on which the increase in price should be calculated. As can be seen from the table above, the applicant intends to reduce the average power purchase cost by replacing the high cost short term power with cheaper long term sources.

Commission's view

In Case No. 13 of 2010, in the matter of Supply of Electricity from the generating stations of the Tata Power Company Ltd. to Reliance Infrastructure Ltd. for distribution to its consumers, the Commission has stated,

"The Commission clarified that as per the Electricity Act 2003 and the MERC (Terms and Conditions of Tariff) Regulation, 2005 the Commission has no power to interfere regarding the quantum of power for which each licensee needs to enter into a PPA. Hence, the Commission cannot advise the licensee on any issue on which the licensees has to enter into a PPA... .."

... .. Further the Commission agrees with TPC that it is the responsibility of the licensee to procure its energy requirement and thus directs REL-D to make arrangements for procurement of its short term power purchase requirement."

A PPA is a commercial contract between two entities. The scheme of 2003 Act does not empower the Commission to assign current PPA of the existing licensee to a new licensee(s). In addition, IPL has not produced a firm substantiation indicating its arrangement to bring power from Dahanu plant. Therefore, the Commission does not find IPL's assumption on this matter tenable.

Moreover, in a notification issued on December 9, 2010 by the Ministry of Power, Government of India, it was stated that the issue of competitive bidding route for PSUs/CPSUs beyond five years after the implementation of the paragraphs 5.1 and 7.1 of the Tariff Policy was discussed in the meeting of Group of Ministers on Power Sector Issues held on October 29, 2010 and the following decisions were taken:

"States should fully migrate to procurement of power by Discoms through tariff based competitive bidding both for public and private sector generation and transmission projects. For the sake of abundant clarity, MoP would issue a clarification regarding

the permitted exemptions in the Tariff Policy for the expansion/upgradation of projects, excluding the hydro sector.”

Pursuant to the above, the notification stated that generation projects of PSUs/CPSUs and transmission projects of STUs/CTU, for which PPA(s)/ TSA(s) have been signed on or before January 5, 2011 are exempted from the tariff based competitive bidding. Therefore, power procurement by the distribution licensee, in the interests of consumers, would have to be done through competitive bidding.

Objection 4: IPL lacks generation capabilities

Some of the objectors have objected that M/s IPL does not have its own power generation capability.

IPL's response

IPL responded that it is in the process of developing 5,400 MW of thermal power plants in Maharashtra at Nasik and Amravati. Amravati Power Transmission Company Ltd. (APTCL), a subsidiary of IPL is developing a 400 KV transmission line from Amravati TPP to 400 KV Akola substation of MSETCL. Another subsidiary, Sinner Power Transmission Company Ltd. (SPTCL) is developing 400 KV transmission lines from Nasik TPP to 400 KV Bableshwar of MSETCL. The BPTA for the same have been executed.

Commission's view

The Commission has noted the response of IPL. However, for the reasons stated in the preceding objection, power procurement by a distribution licensee, in the interests of consumers, would have to be done through competitive bidding.

Objection 5: IPL is facing resistance in developing Power plants

Some of the consumers have objected that IPL, in its business plan, has stated that it is developing 5,400 MW power projects at Nasik & Amravati. These are facing stiff resistance from the locals who have alleged that the Govt is diverting water to these power plants. In such a scenario it will be impossible for these two power projects to see the light of the day.

IPL's response

IPL is in the process of developing 5,400 MW of thermal power plants in Maharashtra at Nasik and Amravati. As per the MERC (General Conditions of Distribution

Licence) Regulations 2006, IPL proposes to discover the lowest prices of long term supply contracts through running a transparent bid process for procurement of long term power post the award of licence for the said area. IPL can not commit any power from its upcoming power plants for the Mumbai suburb area as the same has to be decided through a competitive bidding process with due approval from MERC. IPL's generating plants may participate in such competitive bidding process and will decide as and when such process is declared.

Commission's view

The Commission notes that IPL has not appropriately responded to the concerns raised by the objectors.

Objection 6: IPL's tariffs are higher as compared to the existing licensee. There is a sudden increase in Average Billing Rate (ABR) and Capital Expenditure. Its Return on Equity is increasing at nearly 15%

Some consumers have objected that M/s IPL's takeover of the area of supply of existing licensee may lead to higher tariffs.

- Some consumers have also argued that IPL will require minimum 4 years to generate its own power. In such a case, consumers will get lower tariffs no earlier than 2017.
- One objector highlighted that in IPL's business plan, in the 3rd parallel licence scenario, the ABR in FY 2011-12 is Rs. 8.21 per unit which is 16% higher than the existing licensee's ABR of Rs. 7.06 per unit.
- IPL's Capital expenditure as per the business plan is increasing on an average of about 9% in first 3 years. In FY 2013-14 there is a significant increase of 38% in capital expenditure.
- One objector also highlighted that in IPL's business plan, Return on Equity is increasing at an average rate of nearly 15%.

IPL's response

Power procurement would be done in an economical manner under a transparent power procurement process in accordance with the Regulations, guidelines, directions made by the Commission from time to time. After getting a distribution licence, the firm price would be discovered through a transparent bid process under the Case-1 route. The reduction in power purchase cost in 2013-14 is envisaged primarily on the basis of availability of cheaper sources of power through competitive bidding. The power purchase costs for the base year case as presented in the business plan are as under;

| Particulars | 2011-12 (Part year) | 2012- 13 | 2013- 14 | 2014- 15 | 2015- 16 | 2016- 17 |
|--|--------------------------------|---------------------|---------------------|---------------------|---------------------|---------------------|
| Average power purchase cost (Rs./ kWh) | 4.08 | 4.17 | 3.35 | 3.52 | 3.7 | 3.89 |

The average power purchase cost per unit as indicated above is the basis on which the increase in price should be calculated. As can be seen from the table above, the applicant intends to reduce the average power purchase cost by replacing the high cost short term power with cheaper long term sources.

IPL submitted that the scenario of 3rd parallel licensee is based on following assumptions:

- a) It is assumed that the applicant as a third licensee will be able to add the entire projected growth in number of consumers and sales (in MUs) in the base case scenario during the period of the business plan;
- b) The entire new capital expenditure projected for the existing licence area in the Base Case Scenario is considered to be made by the Applicant for creating infrastructure for the load required;

The applicant will make entire capital expenditure, whereas the number of consumers would be limited to the new consumers coming because of growth. Hence, this higher capital expenditure cost per consumer is being reflected in the higher tariff in this scenario. However, this is only one scenario amongst many that has been developed based on directives from the Honourable Commission. Further, parallel licensing may not always lead to increased tariff burden to consumers. Competitive pricing by the existing second licensee in the said licence area has already benefited several consumers. The average cost of supply figures for the base case as presented in the business plan are as follows:

| Particulars | 2011-12 (Part year) | 2012- 13 | 2013- 14 | 2014- 15 | 2015- 16 | 2016- 17 |
|--------------------|--------------------------------|---------------------|---------------------|---------------------|---------------------|---------------------|
| Cost of Supply | 6.03 | 6.2 | 5.35 | 5.62 | 5.93 | 6.19 |

The capital expenditure has been projected on the basis of the increase in the projected number of units sold in the particular year. In FY 2013-14, the per unit power purchase cost has been assumed to decrease to Rs. 3.5 owing to the power being available on long term basis from sources to be determined through competitive bidding process, which would reflect in lower tariffs. This advantage of lower tariff has been assumed to translate into higher sales in each of the consumer category, resulting in a significant increase in total sales and hence, in total capital expenditure.

The return on equity is constant at 16% (except for FY 2011-12, which has lower RoE as it is a part year). The absolute figures of RoE are increasing in tandem with the

increase in capital expenditure, which as explained earlier, is directly linked to the increase of units sold.

Commission's view

The business plan submitted along with the application for grant of licence is an important part of the application, which provides a bird's eye view of the proposed licensed business. However, in accordance with the Commission view expressed in the matter of objection 3, power procurement by a distribution licensee would have to be done through competitive bidding.

The Commission deals with Retail tariff related matters through a separate process, under the provisions of its Tariff Regulations. The Commission allows a Distribution Licensee to recover all prudent costs with the approval; it is also allowed to recover a return on its equity at a regulated rate. This is done in a transparent manner. Therefore, the Commission believes that tariff related assumptions by IPL, in relation to its business plan submitted for the purpose of grant of licence; do not adversely affect its eligibility for the grant of the licence.

Objection 7: IPL has assumed acquisition of distribution assets of existing licensee without any supporting document

IPL's application proceeds on the grounds that the existing licensee's (RInfra's) assets would be partly or fully transferred. RInfra and some respondents have objected to IPL's assumption on this matter, as below:

- IPL has not planned properly to give uninterrupted supply to the consumers in the proposed licence area.
- The assumptions made by IPL in its business plan with respect to transfer of RInfra's existing assets by being carved out of RInfra's existing area of supply, treatment of regulatory assets, treatment of employees are based on the assumption that the entire undertaking of the existing licensee would be purchased by IPL. This is contrary to the provisions of the 2003 Act.
- Such assumption is against the spirit of Section 14 and 15 of the Electricity Act 2003, under which IPL has filed an application for grant of distribution licence. These sections provide only for the procedure for the grant of distribution licence and not the sale or transfer of assets.
- There is no provision in the Electricity Act, 2003 which provides for transfer of assets of an existing licensee to a new licensee where an application for grant of licence has been made under the provisions of Section 14 and Section 86 (1) (d).
- On a combined reading, inter alia, of the provisions of Section 2(17) and (19) and the Sixth Proviso to Section 14, there is no doubt that any prospective applicant is

required to apply for a licence on the basis that he shall have his own distribution system within an area in which there exists other licensee(s).

- There can be no separation of retail supply and wires licence under the Electricity Act 2003. Therefore, IPL's application that the existing licensee's assets be transferred to IPL is against Section 14 of the Electricity Act, 2003.

IPL's response

IPL submitted that as per Honourable Commission's directives, various scenarios/business models have been analyzed and the financial impact on the cost to serve has been worked out and submitted to the Commission for evaluation. The various scenarios and business models submitted in the business plan include:

- a) Base case with long term power procurement not available from Dahanu Power
- b) Distribution Licence for partial distribution area of South Zone + East Zone with/ without Dahanu Power
- c) Distribution Licence for partial distribution area of South Central Zone + Central Zone + North Zone with/ without Dahanu Power
- d) Retail supply segregated from wires business for entire licence area
- e) Third parallel licensee

In the base case scenario, IPL has assumed that it will take over the entire distribution business of existing licensee, including the wires and retail supply business on expiry of the said licence on August 15, 2011 and the distribution assets shall be transferred to IPL by being carved out of the existing licensee. Associated outstanding liabilities, which have been duly approved by MERC in its last Tariff Order, are also assumed be transferred to Indiabulls Power Limited in the base case. It is further submitted that the final modalities for award of licence and transfer of assets, if any, shall be in accordance with the scheme/terms and conditions which are yet to be approved by the Commission.

Further, it mentioned that MERC intended to generate various options, which would primarily address the issue of lowering cost of supply to benefit the consumers in the area of supply of existing licensee. Considering this, IPL has submitted a business plan which is most suitable to the present scenario. Based on the appropriate clarification and justifications received from the bidders on the comments raised by the stakeholders, the Commission may decide on the next steps.

The applicant has further submitted that the MERC has appointed consultants to undertake a study on the feasibility of application of alternative options of issuing distribution licence and based on the report and recommendations of the same, the interested bidders have been asked to develop the business plans for various alternative scenarios for award of licence.

IPL also submitted that it would adhere to all laws and regulations applicable to it as a distribution licensee post award of the licence by the Commission. The applicability of the said clause of the Electricity Act, 2003 shall be determined by the scheme/ terms and conditions of the licence to be approved by the Commission.

Commission's view

The Commission has had the occasion to examine the opinion dated May 14, 2011 rendered by Shri. Gopal Subramaniam, the Learned Former Solicitor General of India, to the Forum of Regulators. A copy of this opinion as available on the website of the Forum of Regulators was made available to all applicants for grant of licence pursuant to the aforesaid EOI, and uploaded on the website of the Commission. In the opinion, Learned Former Solicitor General of India examined the issue of economic viability of duplicating existing network due to sunk cost associated with it and economies of scale derived from network operation while examining the queries raised as follows:-

- (i) Can a licence be granted to a new entrant/applicant to distribute electricity within the area of an existing distribution licensee without requiring/mandating such an entrant/applicant to lay down its own distribution system within the same area?
- (ii) If so, could the Appropriate Commission decide that there is no requirement of capital investment for distribution network in terms of Rule 3(1) of the Rules, 2005?
- (iii) Could there be wheeling de hors open access so as to enable the new entrant to use the distribution system of the existing incumbent distribution licence to wheel power but without seeking open access? In other words, does the 2003 Act envisage any means other than open access for separation of carriage and content in distribution business?
- (iv) To enable choice of supplier and competitive tariffs to the consumer/any person, could it be inferred that such a consumer/any person could seek supply from a licensee or a generating company other than the distribution licensee within whose area of supply such a consumers'/any persons' premises are situated, on a basis other than open access for avoiding payment of cross subsidy surcharge mandated under the first and second provisos to sub-section (2) of Section 42 of the 2003 Act?
- (v) If distribution & supply are separated should the existing consumers be made to pay full cross subsidy to cover the existing level of cross subsidy or allow them to pay cross subsidy at reduced rates and eliminate the cross subsidy over a given time frame?
- (vi) Is it mandatory for a distribution licensee to own the network as well as supply electricity to its consumers?

- (vii) Can distribution and retail supply business be separated under the existing provisions of the 2003 Act?
- (viii) Could two different types of distribution licenses be issued under the 2003 Act, one requiring the distribution licensee to be the network operator and the other requiring another entity to effect supply to its consumers?
- (ix) If retail supply is segregated from wires business, what should be the minimum area?
- (x) Does separation of supply from wire business to make retail supply competitive, necessarily require an amendment to the 2003 Act?
- (xi) Would the ratio quoted above in the aforesaid judgment of Hon'ble Supreme Court in the case of Tata Power Co v. Reliance Energy Ltd be confined to the said case or apply to similar situations in the electricity sector?

In a nutshell, Learned Former Solicitor General of India took the view that multiple distributors must come with the condition that each of the distributors supply electricity through their own distribution system in accordance with the sixth proviso to Section 14 of the 2003 Act, and therefore in accordance with Rule 3 of the Distribution of Electricity Licence (Additional requirements of Capital Adequacy, Creditworthiness and Code of Conduct) Rules, 2005 it is mandatory for the Commissions to decide the capital investment for distribution network. The definition of "distribution licensee" under Section 2 (17) of the 2003 Act does not leave a scope for two different types of licensees i.e., one who operates the distribution system/ network and the other who supplies electricity. Hence, retail supply and wires business cannot be segregated. However, as regards, the Hon'ble Supreme Court judgment in the case of Tata Power Co. Ltd vs. Reliance Energy Ltd., reported in (2008) 10 SCC 321, on a specific query as to whether the ratio in this case would be confined to the said case or apply to the similar situations in the electricity sector, Learned Former Solicitor General of India took the view that in the said case TPC was supplying electricity in an area for which the distribution licensee was BSES Ltd. This is not a case where TPC is a subsequent applicant to procure a distribution licence for an area for which the existing licensee was BSES Ltd. TPC's licenses came to be granted long before BSES's licenses were granted. Since, Hon'ble Supreme Court held that "*There is sufficient material on record to establish that Tata Power had been supplying energy to domestic consumers on retail basis within areas which subsequently came to be included in BSES' (and subsequently REL's) area of supply and no objection was raised in that regard..*" the requirement of supplying electricity through one's own distribution system laid down in the sixth proviso to Section 14 of the 2003 Act need not be adhered to. These observations were made by Hon'ble Supreme Court in the light of the facts of the case in hand, and not while deciding an issue whether a subsequent licensee for an area or multiple licensees for an area can use the distribution system of the distribution licensee for retail without owning a distribution system as expressly required under the sixth proviso to Section 14 of the 2003 Act.

Hence, the ratio of the Hon'ble Supreme Court judgment in the case of Tata Power Co. Ltd vs. Reliance Energy Ltd., *Supra* is specific to the facts of the case.

The Commission has independently applied its mind on the aforesaid opinion dated May 14, 2011. The Commission is in agreement with the views of the Learned Former Solicitor General of India. A copy of this opinion as available on the website of the Forum of Regulators was made available to all applicants for grant of licence pursuant to the aforesaid EoI, and uploaded on the website of the Commission, for their views.

IPL's submission about the requirement of its own network rollout plan have been analysed in subsequent portions of this Order (Para 44 to Para 51).

The Commission also notes that IPL's interpretation about the Commission's direction to develop alternative scenarios is not fully correct. The Commission strives to take decisions, which are in the interest of the consumers. The Commission has conducted various studies and obtained expert opinions to address the concerns regarding interest of the consumers and has been transparent throughout the process. It has disseminated information to all applicants and urged them to be innovative in generating more alternatives. The Commission, therefore, has been flexible in allowing scenarios in the business plans, if the applicant would so like to propose. However, it was not mandatory for the applicants to develop their business plans based on the recommendations of the internal studies of the Commission.

Objection 8: Data gaps in IPL's application

An authorised consumer representative and existing licensee objected that the preliminary data gaps have not been submitted.

- IPL's application is lacking in details relating to roll-out of distribution network and funding of the same, which will determine whether IPL meets the capital adequacy requirement.
- Additional requirement prescribed by Central Government as may be applicable (Item 12 of Part B of the application form)
- Data on top 5 projects in the preceding 5 years

IPL's response

The IPL submitted that all necessary particulars relating to its capital adequacy, creditworthiness etc. in accordance with the requirements specified in the Ministry of Power, Government of India notification no. G.S.R. 188(E) dated March 23, 2005 issued pursuant to sixth proviso of Section 14 of the EA 2003 and also meets the various Code of Conduct requirements specified therein.

Commission's view

According to the Central Govt Rules, 2005, the capital adequacy is to be assessed based on the applicant's ability to make available the equity to the extent of 30% of the investment requirement in the proposed area. The Commission has assessed the capital investment required in such area based on the size of area and the universal service obligation. As clarified by IPL, it submitted the above-mentioned data gaps to the Commission vide its original application submitted on January 17, 2011.

Salient features of IPL's application

11. The salient features of IPL's application are highlighted below (identified against each section of the data format of the application specified in the MERC General Conditions of Distribution Licence Regulations, 2006):

| Part/Section | Description | Details provided |
|--|---|---|
| Part A: General Information | General Information | IPL has provided all the basic details as specified in this section. Primary contact details, registered office details, registration number, date of incorporation and registration are provided. |
| Part A: 7 (c) | Name and addresses of the Board of Directors | IPL has provided details of the Board of Directors and promoters in Part A1 of its application. |
| Part A: 7 (c) | Ownership/Shareholding pattern | IPL has provided the shareholding pattern in Annexure 1 of its application. According to this, the promoter group holds 58.61% of the total shares; institutional investors hold 24.58% of the shares and 16.81% is held by non-institutional investors. 68.23% of the promoters' shares have been pledged as on September 30, 2010. The largest shareholder is Indiabulls Real Estate Ltd, which holds 39.99% of the shares. |
| Part B: 1 | Memorandum and Articles of Association (in case of a company) as in force on the date of application | IPL has provided a copy of the Memorandum of Association & Articles of Association in Annexure II of its application form. |
| Part B: 2a | An organization chart detailing the management structure of the Applicant, which shall include information (in respect of operations, projects, commercial, finance, regulatory IT and HR | The Organization chart is attached in Annexure III of the application. IPL has submitted all the necessary information with respect to the management details in Annexure III of the application. |

| Part/Section | Description | Details provided |
|---------------------|---|---|
| | functions) a) Senior Executive Management (along with curriculum vitae); | |
| Part B: 2b | b) Board of Directors (along with curriculum vitae); | IPL has submitted that it has 6 Directors on the Board. The details of the Board of Directors are provided in Part A2 of its application, and in the pre TVS data gaps submitted by IPL on February 14, 2011. |
| Part B: 2c | Number of middle/lower management personnel | No of middle/lower management personnel – 350 |
| Part B: 2d | Relationship (including intending relationship, where applicable between the Applicant and key to the application for grant of Licence. | Not applicable |
| Part B: 3, 4 | Details of Income tax PAN/TAN; Details of import licence, if any | The details of the Income tax PAN and TAN are attached in Annexure IV of the application. The copy of import licence has been attached in Annexure V of the application of IPL. |
| Part B: 5 | Bank references asserting that the Applicant is financially solvent | Canara Bank has provided a Certificate (DEL PCB II IBPL OPL 813 2010) declaring that IPL has a Networth of Rs 3,920.20 crore as per audit accounts as on March 31, 2010. |
| Part B: 6 | Annual Audited Reports for the past 3 years for the Applicant and for any Holding Company, Subsidiary or affiliated company (if any). | IPL submitted its audited Annual Accounts for last three years in Annexure VII of its application. It has also submitted the Annual audited Reports for IPL for FY 2009-10 (since the company listed in October 2009) and for Indiabulls Real Estate Limited (holding company) for FY 2007-08, FY 2008-09 and FY 2009-10 as part of Annexure II of the Pre TVS data gaps submitted by IPL on February 14, 2011. IPL has further stated that Indiabulls Power Ltd and its holding company have over 100 and 200 subsidiaries respectively, and details for these have been captured in the Annual audited Reports submitted. |
| Part B: 7 | Any other documentary evidence to substantiate the financial capabilities, technical competence and others. | IPL has also provided Chartered Accountants' Networth certificate from Sanjeev Suyash & Associates in Annexure VIII of the application. |

| Part/Section | Description | Details provided |
|---------------------|--|---|
| Part B: 8 | Details of the actual or proposed location of the system of electric lines and electrical plant by means of which the applicant intends to enable distribution of electricity, indicating which plant and lines are to be constructed and which are existing plant and liens, and the area to which the application for Licence relates. | IPL did not submit the details of actual or proposed location of the system of electric lines and electrical plant as part of the original application on January 17, 2011. The data gap was highlighted to the IPL. IPL has submitted vide letter dated May 30, 2011, to the Commission that the application for Licence by Indiabulls Power Ltd relates to the entire distribution area currently served by the existing licensee and is not limited to any partial area. IPL has also submitted that it proposes to use the existing network infrastructure to serve the existing consumers and add new lines and networks to meet the increased load growth projected as per the Business Plan. |
| Part B: 9 | Detailed electrical distribution map or maps of the proposed geographical area of supply, on a scale of not less than 10 centimetres to a kilometre, The map shall clearly distinguish between the existing system and new facilities. | IPL did not submit the detailed electrical distribution map as part of the original application on January 17, 2011. The data gap was highlighted to the applicant. IPL vide letter dated May 30, 2011, to the Commission, has submitted that this requirement be condoned at the present stage. IPL was of the view that the requisite information cannot be submitted on the basis of the secondary data made available. As per the IPL, the same will be provided along with the detailed technical feasibility study, which will be finalized in consultation with the Commission. |
| Part B: 10 | Business plan details | IPL submitted its revised Business Plan on April 1, 2011, after taking into consideration the scenarios discussed during the TVS. IPL was asked to submit a revised Business Plan subsequent to change in the proposed area of supply. However, IPL has not responded to the same. |
| Part B: 12 | Supporting information on compliance with the additional requirements prescribed by the Central Government, as may be applicable. | IPL has provided an affidavit signed by its Company Secretary for Compliance with the provisions of Distribution of Electricity Licence (Additional requirements of Capital Adequacy, Creditworthiness and Code of conduct) Rules, 2005. |
| Part C | Format for assessing competence of applicant | IPL submitted its previous experience (past 5 years for Related Business), Details of Proposed Business, Revenue Potential, Information on Appropriate Expertise |

| Part/Section | Description | Details provided |
|--------------|-------------|--|
| | | (Personnel), Details of Financial Soundness of Subsidiaries, Baseline Information vide part A3 of its original application and the pre TVS data gaps submitted on February 14, 2011. |

Evaluation of IPL's eligibility for grant of Distribution Licence

12. On the date of expiry of the present licence of RInfra, another Licensee viz., Tata Power Company Limited (TPC), would exist in the same area. Hence, the issue of grant of licence to more than one person in the same area will arise when grant of a distribution licence in the area of supply of an existing licensee is considered. In such a situation, the sixth proviso to Section 14 of the 2003 Act, contemplates that an applicant where "there already exists a Licensee in the same area for the same purpose" must "comply with the additional requirements relating to the Capital Adequacy, Creditworthiness, and Code of Conduct as may be prescribed by the Central Government." This would be without prejudice to the other conditions or requirement, if any, under the 2003 Act. The sixth proviso to Section 14 of the 2003 Act is extracted as follows:-

"Provided also that the Appropriate Commission may grant a Licence to two or more persons for distribution of electricity through their own distribution system within the same area, subject to the conditions that the applicant for grant of Licence within the same area shall, without prejudice to the other conditions or requirement under this Act, comply with the additional requirements relating to the Capital Adequacy, Creditworthiness, and Code of Conduct as may be prescribed by the Central Government, and no such applicant, who complies with all the requirements for grant of Licence, shall be refused grant of Licence on the ground that there already exists a Licensee in the same area for the same purpose:"

13. Accordingly, the provisions of the Distribution of Electricity Licence (additional requirements of Capital Adequacy, Creditworthiness and Code of Conduct) Rules, 2005 notified by the Central Government as per the provisions of Section 14 of the 2003 Act, have been applied in the present case. The extracts thereof are as follows:-

"... 3. Requirements of capital adequacy and creditworthiness.-

(1) The Appropriate Commission shall, upon receipt of an application for grant of licence for distribution of electricity under sub-section (1) of section 15 of the Electricity Act, 2003, decide the requirement of capital investment for distribution network after hearing the applicant and keeping in view the size of the area of supply and the service obligation within that area in terms of section 43.

(2) *The applicant for grant of licence shall be required to satisfy the Appropriate Commission that on a norm of 30% equity on cost of investment as determined under sub-rule (1), he including the promoters, in case the applicant is a company, would be in a position to make available resources for such equity of the project on the basis of networth and generation of internal resources of his business including of promoters in the preceding three years after excluding his other committed investments.*

Explanation: - For the grant of a licence for distribution of electricity within the same area in terms of sixth proviso to section 14 of the Act, the area falling within a Municipal Council or a Municipal Corporation as defined in the article 243(Q) of the Constitution of India or a revenue district shall be the minimum area of supply.

4. Requirement of Code of Conduct.- The applicant for grant of licence shall satisfy the Appropriate Commission that he has not been found guilty or has not been disqualified under any of the following provisions within the last three years from the date of the application for the grant of licence:

(a) section 203, section 274, section 388B or section 397 of the Companies Act, 1956;

(b) section 276, section 276B, section 276BB, section 276C, section 277 or section 278 of the Income tax Act, 1961;

(c) section 15C, section 15G, section 15H or section 15HA of the Securities and Exchange Board of India Act 1992;

(d) clause (b), (bb), (bbb), (bbbb), (c) or (d) of sub-section (1) of section 9 of the Excise Act 1944;

(e) section 132 or section 135 of the Customs Act 1962,

and that the applicant is not a person in whose case licence was suspended under section 24 or revoked under section 19 of the Act, within the last three years from the date of application:

Provided that where the applicant is a company, it shall satisfy the Appropriate Commission in addition to provisions of this rule that no petition for winding up of the company or any other company of the same promoter has been admitted under section 443 (e) of the Companies Act, 1956 on the ground of its being unable to pay its debts.”

14. Apart from the above requirements, according to the sixth proviso to Section 14 of the 2003 Act, licence can be granted only to those applicants, who would distribute electricity through their own distribution system.

15. The Commission assessed IPL's eligibility for grant of the distribution licence on the basis of the framework described above, and various information provided in IPL's

application and other submissions made by IPL from time to time. Accordingly, the Commission used the following criteria to determine IPL's eligibility for grant of distribution licence:

- Minimum area of supply requirement (E1)
- Capital Adequacy requirement (E2)
- Creditworthiness requirement (E3)
- Code of Conduct requirement (E4)
- Requirement of own network rollout plan (E5)

Minimum area of supply requirement (E1)

16. Till 1985, BSES Ltd.'s licensed area included the area of Municipal Council of Mira Bhayandar (as it was known then). Thereafter, the Government of Maharashtra (GoM), by a notification dated January 10, 1990, revised the area of Mira Bhayandar Municipal Council to include the areas to the East covered by the revenue villages of Chene and Varsova (additional area).
17. By notification in Gazette Extra Ordinary dated December 1, 2001, the Govt of Maharashtra ("GoM") declared that the whole of the local area comprising the Mira Bhayandar Smaller Urban Area should cease to be a Municipal Area from February 28, 2002. In the same Extra Ordinary Gazette, the said area was further notified as larger urban area as a municipal corporation by the name of Mira Bhayandar Municipal Corporation with effect from the same date.
18. Initially, IPL sought a licence to distribute electricity in and around suburbs of Mumbai. However, subsequently, IPL revised the proposed area of supply in the application and sought a licence to distribute electricity in and around suburbs of Mumbai plus the area covered under Chene and Varsova, which are contiguous with the area applied for earlier. IPL stated that it proposed to include the additional areas of Chene and Varsova to fulfil the criteria of minimum area of supply as specified in the Distribution of Electricity Licence (Additional requirements of Capital Adequacy, Creditworthiness and Code of Conduct) Rules, 2005. Therefore, IPL has applied for an area, which covers Mira Bhayandar Municipal Corporation completely.
19. The Commission is of the view that the area of supply as proposed by IPL in its application for grant of Distribution Licence conforms to the minimum area of supply in terms of the Explanation to Rule 3 of the Distribution of Electricity Licence (Additional requirements of Capital Adequacy, Creditworthiness and Code of Conduct) Rules, 2005. The proposal entails supplying to the entire area covered by the Mira Bhayandar Municipal Corporation. Therefore, the prescription that "*the area falling within aMunicipal Corporationshall be the minimum area of supply,*" is fulfilled. Therefore, the Commission is of the view that in totality the minimum area of supply requirement in terms of the Explanation to Rule 3 of the Distribution of

Electricity Licence (Additional requirements of Capital Adequacy, Creditworthiness and Code of Conduct) Rules, 2005 stands complied with.

Capital Adequacy requirement (E2)

20. To comply with the Capital Adequacy requirement laid down in the said Rules 2005 of the Central Government, IPL was required to satisfy the Commission that it has the ability to make available equity to the extent of 30% of the capital investment requirement for distribution in the proposed area of supply. It is also specified in the said Rules that such ability is to be assessed based on the Networth and Internal Resource Generation of the business and promoters in the preceding three years after excluding other committed investment.
21. The applicant was asked to submit a certificate providing computation details about its financial parameters namely Internal Resource Generation and Networth. For the purpose of computation of these parameters, only audited annual accounts were to be considered. Such accounts include all the assets and liabilities owned by the applicant entity. In other words, if the applicant owns distribution assets existing in the proposed area of supply, the value of those assets would anyway get captured in such computations. In such case, even if the capital investment requirement may be incremental, the Capital Adequacy cannot be assessed in incremental manner. Because, it is not possible to obtain the audited Annual Accounts, which exclude the value of distribution assets existing in the proposed area of supply. Therefore, the Commission found it appropriate to consider the applicant's audited annual accounts, which include all assets and liabilities. And accordingly, it proceeded to determine the capital investment required for rolling out a new distribution system in the proposed area of supply.
22. It is specified in the Rules that the Commission needs to determine requisite capital investment based on the size of area and the universal service obligation. The Commission felt that accurate estimation of capital investment requirement is not a necessary exercise for the purpose of grant of licence. The central idea is to have a fair estimate of such capital investment requirement. After hearing the applicant and considering the area for which licence is sought for, the Commission arrived at an estimate of capital investment requirement based on publicly available information and other material in the possession of the Commission. According to such estimate, capital investment requirement shall be to the tune of Rs. 4,640 crore.
23. Therefore, on a norm of 30% equity, the total equity investment required is about Rs. 1,392 crore. The Commission feels that under the dynamics of capital markets, a company may choose not to invest all the equity/ share capital from its own resources. It is reasonable to expect that the company shall invest at least 26% of the total equity requirement from its own resources to have sufficient control in terms of controlling

stake and voting rights in the said licensed business. Therefore, IPL needs to invest a minimum equity capital of Rs. 362 crore.

24. The Central Govt. Rules, 2005 states, “..... *satisfy the Appropriate Commission that.... a company, would be in a position to make available resources for such equity of the project...*” Accordingly, the applicant may opt to raise the equity for the required capital investment through multiple avenues along with its own resources. It may dilute its ownership in this distribution business to raise equity from outside sources to fund capital investment. Therefore, it is assumed that the applicant will form a Special Purpose Vehicle (SPV) for the proposed distribution business. Even if the applicant may decide not to form such SPV, the Commission, for the purpose of evaluation of eligibility of the applicant and to give effect of the provisions of the said Rules, 2005, has assumed such SPV while assessing Capital Adequacy and Creditworthiness requirements.
25. If other investors infuse significant equity in the proposed distribution business, they may get representation in the Board of Directors. For the decisions regarding capital investment in the proposed distribution business, the applicant has to obtain approval from its Board of Directors. If the investments are in the interest of the business, the Board would support decisions for such investments. Therefore, major hurdles in getting Board’s approval for such investments are not anticipated.
26. However, it is possible that the applicant’s share in equity reduces substantially due to external infusion of equity. It would still be fair to assume that the applicant continues to hold its primary interest in the distribution business and therefore in holding the Distribution Licence. Hence, it will ensure its control over the critical decisions regarding this business. Therefore, it shall hold minimum 26% of total equity in proposed distribution business, so that, independently, it can block special resolutions, which are not in the interest of the company. Therefore, the minimum equity requirement from the applicant at any point in time shall not be less than 26% of total equity.
27. According to the Distribution of Electricity Licence (Additional requirements of Capital Adequacy, Creditworthiness and Code of Conduct) Rules, 2005 the Capital Adequacy has to be assessed based on Networth and Internal Resource Generation of preceding three years. As the 2003 Act or the Rules of the Central Government do not specify any method of computing Networth and Internal Resource Generation, the Commission adopted the method specified by the Central Government in the Standard Bidding Documents for procurement of power through tariff based Competitive Bidding under Case 2.

The formula for Networth computation adopted by the Commission is as below:

Networth = Equity Share Capital + Reserves and Surplus - Revaluation Reserves - Intangible assets - Miscellaneous Expenditure to extent not written off and carry forward losses

The formula for Internal Resource Generation computation adopted by the Commission is as below:

Internal Resource Generation = Profit after Tax + Depreciation and Amortization + Decrease in Net current Assets (Excluding cash) + Any other non-cash expenditure (including deferred tax) – Scheduled loan repayments and increase in net current assets (excluding cash)

The following two tests were considered, while assessing capital adequacy of the applicant. It is important to note that both the below-mentioned tests had to be separately passed.

Test 1: Is the maximum of (NW1, NW2, NW3) – CE \geq CIC

AND

Test 2: Is five (5) times the maximum of (IRG1, IRG2, IRG3) – CE \geq CIC

Where:

IRG1: Internal Resource Generation for the last audited financial year

IRG2: Internal Resource Generation for the year before the last audited financial year

IRG3: Internal Resource Generation for two years before the last audited financial year

CE: 26% of the Committed Equity investments elsewhere

CIC: 26% of (30% of Capital Investment Criteria) as estimated from capital expenditure requirement

NW1: Networth for the last audited financial year

NW2: Networth for the year before the last audited financial year

NW3: Networth for two years before the last audited financial year

The multiplying factor for Internal Resource Generation (IRG) is taken as 'five (5)', which reflects the number of years needed to setup the distribution system in the applied licence area.

28. IPL was asked to submit the computation of Networth and Internal Resource Generation (IRG) certified by the Managing Director/ Chief Executive Officer/ Manager (authorized through a board resolution), being a full time director on the Board of the Company and the statutory auditor as per the formula specified above,

through MERC letter dated June 17, 2011. IPL vide its letter dated June 27, 2011, submitted the computation of Networth and IRG for the company as per audited financial statements, which is shown below.

Table 1 : IPL - Networth and IRG

| (Rs. crore) | FY 2007-08 | FY 2008-09 | FY 2009-10 |
|--------------------|-------------------|-------------------|-------------------|
| Networth | 1,986.91 | 2,306.14 | 3,920.32 |
| IRG | -1,429.68 | 463.06 | -794.24 |

29. The Networth as on March 31, 2010 is Rs. 3,920.32 crore, which is the maximum in the preceding 3 years. Its maximum IRG over the last 3 years was Rs. 463.06 crore in FY 2008-09. IPL had a negative IRG in FY 2007-08 and 2009-10.
30. To assess whether the applicant has committed investments tied up in other projects, IPL was asked to submit this information through letter dated May 25, 2011. As per the Distribution of Electricity Licence (Additional requirements of Capital Adequacy, Creditworthiness and Code of Conduct) Rules, 2005, such commitments need to be excluded while deriving capital adequacy. IPL vide its letter dated May 30, 2011 informed the Commission that it has a commitment of investments in projects other than the proposed area of supply, worth around Rs 26,838 crore. Out of which, Rs 20,128 crore represents sanctioned debt. Therefore, the committed investments to be financed through equity amounts to Rs 6,710 crore. For adjustment of such commitments while deriving capital adequacy, only equity component of the other committed investments will be relevant. However, with increasing avenues to raise equity, the applicant may choose not to bring the entire equity for other committed investments from its own resources. It can be fairly assumed that minimum equity contribution from an applicant may be 26% of the total equity, which is sufficient for stopping any special resolution and maintaining a control in the said committed investments. Therefore, for the adjustment related to other commitments, 26% of committed equity in other committed investments has been considered which amounts to Rs. 1,745 crore.
31. Therefore, according to the test determined by the Commission, the Networth, adjusted for the committed equity investments elsewhere, was computed to be Rs. 2,176 crore. However, IPL is required to satisfy the Commission that the minimum of Rs. 362 crore for this licensed business is potentially available as explained in Para 23. Its adjusted Networth (Rs. 2,176 crore) is greater than the equity requirement (Rs. 362 crore). Therefore, the Commission is of the opinion that IPL satisfies the Networth criteria.
32. Additionally, according to the test determined by the Commission, the IRG, adjusted for the equity investments committed elsewhere, was computed to be Rs.571 crore. IPL needs to satisfy the Commission that minimum of Rs. 362 crore for this licensed business is potentially available as explained in Para 23. The adjusted IRG (Rs. 571

crore) is greater than the equity requirement (Rs. 362 crore). Hence, IPL satisfies the IRG criteria.

33. Therefore, IPL has met the eligibility requirement for Capital Adequacy as it passed the tests for both Networth and Internal Resource Generation.

Creditworthiness requirement (E3)

34. The Distribution of Electricity Licence (Additional requirements of Capital Adequacy, Creditworthiness and Code of Conduct) Rules, 2005, do not elaborate on the method of Creditworthiness assessment. However, in the Judgment of the Hon'ble Appellate Tribunal for Electricity in Appeal No. 7 of 2010 is being referred to for the purpose of evaluation of creditworthiness requirement. In this judgement, the Hon'ble Tribunal observed as follows:-.

“The Capital Adequacy is determined on the above basis; and on the basis of the Capital Adequacy so determined the ability of the Applicant to raise finances and funds has to be determined. The creditworthiness of the Applicant will have to be tested by considering whether external borrowings from Banks or Financial institutions will be available to the Applicant based on the fulfilment of the Capital Adequacy norms”

35. The MERC (General Conditions of Distribution Licence) Regulations, 2006 (in Point 5 of Part B of Annexure 1 of the Application format) require the applicant to submit “Bank references asserting that the Applicant is financially solvent”. The solvency assesses the ability of an organisation to meet its long-term fixed expenses and to accomplish long-term expansion and growth. Moreover, as part of additional information, IPL was asked to submit the latest available Credit Rating report. The Credit Rating report provides a rating, which represents the rating agency's opinion on the general creditworthiness of the rated entity. A simple alphanumeric symbol is normally used to convey a credit rating. In contrast to a credit bureau, which provides information on past debt repayments by borrowers, a credit rating agency provides an opinion relating to ability of the borrower to repay a debt in future. Since a credit rating report takes into consideration past repayment records and future likelihood of repayment of a debt, the Commission, in the absence of any other tool, found it appropriate to consider latest available credit rating report for assessing Creditworthiness of IPL. Thus, based on the solvency certificate and credit rating report submitted, the Creditworthiness of IPL was assessed.
36. IPL in its application dated January 17, 2011 provided a solvency certificate from Canara Bank. Canara Bank, in the solvency certificate has declared Indiabulls Power Limited to be solvent to the extent of Rs. 3,920.20 crore. Canara Bank was contacted to verify the authenticity of the certificate. Canara Bank confirmed the validity of the solvency certificate issued by it to IPL on June 16, 2011.

37. In response to the Commission's letter dated May 25, 2011, IPL submitted its credit rating report on May 30, 2011. According to the report submitted, ICRA Limited has assigned an Issuer Rating of "BBB" to IPL. The rating has been assigned "Stable" outlook. As per ICRA, an Issuer Rating of 'BBB' indicates moderate credit quality. The rated entity carries a higher than average credit risk. This rating is only an opinion on the general creditworthiness of the rated entity and not specific to any particular debt instrument.
38. The debt requirement of IPL in the proposed business is 70% of the total capital investment requirement, which is about Rs. 3,248 crore. The applicant should be in a position to raise this debt. Based on the solvency certificate provided by Canara Bank, IPL can be treated as solvent to the extent of Rs. 3,920 crore. Based on solvency certificate and the credit rating report, the Commission is satisfied that IPL meets the requirement of Creditworthiness.

Code of Conduct requirement (E4)

39. As provided in Rule 4 of the Distribution of Electricity Licence (additional requirements of Capital Adequacy, Creditworthiness and Code of Conduct) Rules, 2005, IPL was required to meet the Code of Conduct requirements as per the provisions of the following Acts:

- Companies Act, 1956
- Income Tax Act, 1961
- Securities and Exchange Board of India Act, 1992
- Excise Act, 1944
- Customs Act, 1962

The relevant sections of the Central Government Rules are highlighted below:

"4. Requirement of Code of Conduct.- The applicant for grant of licence shall satisfy the Appropriate Commission that he has not been found guilty or has not been disqualified under any of the following provisions within the last three years from the date of the application for the grant of licence:

(a) section 203, section 274, section 388B or section 397 of the Companies Act, 1956;

(b) section 276, section 276B, section 276BB, section 276C, section 277 or section 278 of the Income tax Act, 1961;

(c) section 15C, section 15G, section 15H or section 15HA of the Securities and Exchange Board of India Act 1992;

(d) clause (b), (bb), (bbb), (bbbb), (c) or (d) of sub-section (1) of section 9 of the Excise Act 1944;

(e) section 132 or section 135 of the Customs Act 1962,

and that the applicant is not a person in whose case licence was suspended under section 24 or revoked under section 19 of the Act, within the last three years from the date of application:

Provided that where the applicant is a company, it shall satisfy the Appropriate Commission in addition to provisions of this rule that no petition for winding up of the company or any other company of the same promoter has been admitted under section 443 (e) of the Companies Act, 1956 on the ground of its being unable to pay its debts.”

40. IPL, in its original application dated January 17, 2011, had submitted an affidavit signed by the authorized Company Secretary under the requirement of Code of Conduct (Rule 4) of the Distribution of Electricity Licence (additional requirements of Capital Adequacy, Creditworthiness and Code of Conduct) Rules, 2005 issued by the Central Government.
41. Based on the information submitted by IPL under affidavit, the Commission is satisfied that IPL is not in violation of the Code of Conduct and meets the requirement of the Rule 4 of the Distribution of Electricity Licence (additional requirements of Capital Adequacy, Creditworthiness and Code of Conduct) Rules, 2005.

Requirement of own network rollout plan (E5)

42. The sixth Proviso to Section 14 of the 2003 Act provides that two or more licensees can distribute electricity within the same area, but through their own distribution system. Accordingly, the applicant for distribution licence will have to supply electricity through its own distribution system. Therefore, Network Rollout Plan is a mandatory requirement for grant of distribution licence in the proposed area of supply. The plan should give an overview of timelines required to set up the network and the way the applicant proposes to meet the Universal Service Obligation of a Distribution Licensee.

IPL's Network Rollout Plan

43. IPL does not have any action plan in terms of geographical coverage and time frame for rolling out its own distribution network in the area of supply for which the licence is sought for. IPL submitted that the approach to the business plan is predicated on the assumption that the distribution assets would be carved out of the existing licensee and then transferred to IPL by paying an amount equal to equity base of the existing licensee, as approved by the Commission during determination of tariffs. Further, it has proposed to accept associated outstanding liabilities of existing licensee, as approved by the Commission in the last tariff Order. Accordingly, in the base case scenario of its business plan, IPL has projected capital investment and network roll out

on the basis of capital expenditures approved by the Commission over the last three years and linked it to growth in energy sales. IPL has also submitted an alternative scenario in which it would be the third parallel licensee in the area of supply. However, even in this scenario, it has envisaged capital expenditure and network roll out only to the extent of meeting growth in the number of consumers and the corresponding load growth. The Commission asked IPL to submit a network roll-out plan and a geographical roll-out plan via a letter dated May 25, 2011. In response, it again submitted the estimated additions in the electrical plant and machinery for meeting load growth in the area of supply of the existing licensee.

44. It is clear from IPL's submission that it does not propose to build its own network to distribute electricity in the proposed area of supply. Although, the Electricity Act, 1910 has been repealed in terms of Section 185(1) of the 2003 Act, it may be relevant to note that Section 3(2)(e) of the 1910 Act provides that "*the grant of a license under this Part for any purpose shall not in anyway hinder or restrict the grant of license to another person within the same area of supply for a like purpose*". The requirement that the applicant for distribution licence should have its own distribution system in order to distribute electricity is an express provision added in the sixth proviso to Section 14 of the 2003 Act. It would also be relevant to take a note of the comments of the Standing Committee on Energy (2002) that the area of supply for a new entrant should necessarily include a mix of urban and rural or any composite remunerative and unremunerative clusters having mixed load, so that it is ensured that both the rural and urban areas get equal opportunities in the development of infrastructure, including power [Para 6.37 of the Report of the Standing Committee on Energy (2002)]. This provision also clarifies the intention of the Parliament that new incumbent applicants/distribution licensees are supposed to make capital investment and lay down distribution system/network in the area of supply with regard to which they would seek a licence under the sixth proviso to Section 14 of Electricity Act, 2003.
45. The new licensee in the area of an incumbent licensee has to establish its own distribution system. The sixth proviso to Section 14 of Electricity Act, 2003 is unambiguously clear on this matter. It gives power to the Commission to grant licences to two or more persons to distribute electricity within the same area, but only through their own distribution systems. Accordingly, the applicant for distribution licence will have to supply electricity through its own distribution system.
46. Sub-section (1) of Section 42 of the 2003 Act mandates the duty of a distribution licensee to develop and maintain an efficient, coordinated and economical distribution system in his area of supply. There is no exception contained in this provision from the duty of a distribution licensee, be it a new entrant or an existing incumbent distribution licensee, to develop distribution system in his area of supply.
47. A distribution licensee (irrespective of whether he is a new entrant or an existing incumbent distribution licensee) is required to operate and maintain a distribution

system comprising of wires and associated facilities. The term “distribution licensee” defined in Section 2(17) of the 2003 Act is extracted below:

“(17) “distribution licensee” means a licensee authorised to operate and maintain a distribution system for supplying electricity to the consumers in his area of supply;”

48. The term “operate” is defined as follows in the Law Lexicon by P Ramanatha Iyer [2006 edn.]:

“To put in action and supervise the working of; to perform a work of labour; to effect any result; to bring about a specified result; to produce the proper or intended effect. The word ‘operate’ means to put into or to continue in operation or activity, to work as to operate a machine and is distinct from maintaining or keeping in repair. 1. To take effect; 2. to be in activity; 3. to work.”

49. The term “maintain” is defined as follows in the Law Lexicon by P Ramanatha Iyer [2006 edn.]:

“Webster’s International Dictionary defines “maintain” to mean to hold or keep in any particular state or condition; to support; to sustain; to uphold; to keep up; to keep possession of; not to surrender; to continue; not to suffer to cease or fail; to bear the expense of.

The word “maintain” does not mean to provide or construct, but means to keep up; to keep from change; to preserve.

“maintain” also means to bear the expense of; to support; to keep up; to supply with what is needed.”

50. Although, a distribution licensee is required to operate and maintain a distribution system in terms of the definition contained in Section 2(17), the 2003 Act in sub-section (1) Section 42 thereof has expressly specified the mandatory duty of a distribution licensee to develop and maintain distribution system in his area of supply.

51. IPL does not have any action plan in terms of geographical coverage and time frame for rolling out its own distribution network in the area of supply for which the licence is sought for. IPL has admittedly not submitted a separate network rollout plan since its business plan assumes partial or complete takeover of the existing licensee’s assets. IPL has planned for capital expenditure that primarily caters only to the ‘demand growth’ envisaged in the proposed area and investment requirement towards application of advanced technologies. The Commission is of the view that IPL has assumed a situation where there would be three licensees viz. Tata Power Co. Ltd; RInfra; and IPL, and that IPL would only choose to supply power to those newly

added consumers from time to time and hence states that its capital expenditure primarily caters only to the 'demand growth' envisaged in the proposed area. This situation presupposes that new consumers would only belong to IPL and not to either of the other two licensees. In other words, IPL has assumed an exclusive licence to supply electricity only when there is 'demand growth' in the area. Moreover, from such submissions by IPL, it also appears that it does not propose to serve existing consumers in the proposed area of supply. The Commission is of the view that such a stipulation on the part of IPL is contrary to Section 43 of the 2003 Act that emphasises and statutorily lays down universal obligation on distribution licensees. For these reasons, contentions of IPL are not sustained in law. Therefore, the Commission found that IPL's application does not conform to the provisions of the 2003 Act as well as the aspects relevant to grant of licence.

52. Considering all the material on record, the Commission is of the view that IPL's application for grant of a Distribution Licence has complied with additional requirements as specified by the Central Government in the Distribution of Electricity Licence (Additional requirements of Capital Adequacy, Creditworthiness and Code of Conduct) Rules, 2005. However, IPL's application did not fulfil a mandatory requirement specified under the 2003 Act, which is to lay out its own distribution system in the proposed area of supply.
53. The Commission decided to assess IPL's application in terms of the benefits it may bring to the consumers in and around Mumbai suburban areas. Based on various information provided in the application and other submissions by IPL from time to time, the Commission assessed IPL's application for its

- Power Procurement Plan (S1); and
- Management and Technical Expertise (S2)

Power Procurement Plan (S1)

As part of the original application submitted on January 17, 2011, IPL had submitted a power procurement plan which considered the procurement of power from Dahanu Power Plant of existing licensee. However, post the Technical Validation Session, IPL submitted a power procurement plan incorporating various scenarios as part of the revised business plan.

IPL has submitted that its approach to the business plan is predicated on lowering the power procurement cost by securing long term supplies from sources to be determined through the competitive bidding process. IPL has also stated that it is developing 5400 MW of thermal power plants at Nasik and Amravati in the State of Maharashtra, out of which, 2700 MW is under advanced stages of construction and the remaining 2700 MW is under development.

In the base case of the business plan, the power procurement plan is based on the following assumptions

- Long term power would be available from the power plant of the existing licensee, namely Dahanu Power Plant
- Renewable sources of power of the existing licensee shall continue uninterrupted over the new licence period
- Past average cost and annual escalation has been assumed at CERC approved rate for escalation of domestic coal which is 6.01% p.a.

For the balance power to be procured, IPL has assumed an appropriate mix of medium and long term power sources, with minimal short term power procurement, in order to arrive at a blended procurement cost as outlined in the table below:

| Particulars | 2011-12 (Part year) | 2012-13 | 2013-14 | 2014-15 | 2015-16 | 2016-17 |
|---------------------|--------------------------------|----------------|----------------|----------------|----------------|----------------|
| Medium-term Sources | 4.80 | 4.80 | | | | |
| Long-term Sources | | | 3.50 | 3.67 | 3.84 | 4.03 |

For FY 2011-12 and FY 2012-13, the procurement is assumed to be largely on medium term basis, while from FY 2013-14 onwards, power is envisaged to be available on long-term basis from sources to be determined through competitive bidding process.

The demand of energy estimated by IPL in the proposed area of supply was estimated as below:

| Particulars | 2011-12 (Part year) | 2012-13 | 2013-14 | 2014-15 | 2015-16 | 2016-17 |
|--|--------------------------------|----------------|----------------|----------------|----------------|----------------|
| Sales (MU) | 6,139 | 10,514 | 11,422 | 12,451 | 13,531 | 14,748 |
| T&D Loss (%) | 14.00% | 13.50% | 13.50% | 13.00% | 13.00% | 12.50% |
| Energy Input into Distribution System (MU) | 7,139 | 12,155 | 13,204 | 14,311 | 15,553 | 16,854 |

Average power purchase cost proposed by IPL in the base case scenario is summarized as below:

| Particulars | 2011-12 (Part year) | 2012-13 | 2013-14 | 2014-15 | 2015-16 | 2016-17 |
|-----------------------------|--------------------------------|----------------|----------------|----------------|----------------|----------------|
| Power Purchase Cost (Rs cr) | 2,915 | 5,067 | 4,417 | 5,035 | 5,755 | 6,556 |
| Power Purchase Quantum (MU) | 7,139 | 12,155 | 13,204 | 14,311 | 15,553 | 16,854 |
| Power Purchase | 4.08 | 4.17 | 3.35 | 3.52 | 3.70 | 3.89 |

cost per unit
(Rs/unit)

In addition to the base case, IPL has also submitted the following scenarios with respect to power procurement:

- **Scenario 1 (Base Case with Dahanu Power not available):** In this scenario, IPL has assumed that power from Dahanu Power Plant would not be available to the applicant post award of the distribution licence. Other assumptions are same as those in the base case.
- **Scenario 2A (Base Case with 7% CERC escalation rate for energy charges):** This scenario takes into account the impact of variations in power purchase cost due to variation in factors like fuel (coal and natural gas), demand supply dynamics and market conditions. It is assumed that energy charges for the power from the new source, which is to be determined through a Case-1 bidding mechanism, will increase at a rate of 7% annually during the business plan period. Other assumptions are same as those in the base case.
- **Scenario 2B (Base Case with 8% CERC escalation rate for energy charges):** It is assumed that energy charges for the power from the new source, which is to be determined through a Case-1 bidding mechanism, will increase at a rate of 8% annually during the business plan period. Other assumptions are same as those in the base case.

Management and Technical Expertise (S2)

Expertise of key personnel

IPL's senior management possesses relevant expertise in the areas of people management, and strategy and planning. The key personnel has experience across the power sector value chain in areas such as construction, design and O&M of electrical apparatus and systems, commercial aspects, financial management, regulatory affairs, customer handling, project execution, stores and material handling, rolling out of advanced technologies.

Experience of management in handling businesses with large number of consumers and employees

Currently, IPL has strength of 701 technical and non-technical workforces. Details of average number of employees in IPL in past three years are summarized below:

| Year | Average number of employees |
|-------------|------------------------------------|
| FY 2008-09 | 73 |
| FY 2009-10 | 172 |
| FY 2010-11 | 613 |

Experience in the last 3 years in the value chain of electricity

IPL submitted that it has presence across generation and transmission projects.

Generation: IPL is developing power projects aggregating 9,207 MW. These include:

- 1350 MW Amravati (Phase – I) Thermal Power Project in Maharashtra
- 1350 MW Amravati (Phase – II) Thermal Power Project in Maharashtra
- 1350 MW Nasik (Phase – I) Thermal Power Project in Maharashtra
- 1350 MW Nasik (Phase – II) Thermal Power Project in Maharashtra

As per IPL, debt and equity for the projects has already been tied up. The projects are in advanced stage of construction.

Transmission: Subsidiary of IPL, Amravati Power Transmission Company Ltd (APTCL) is developing 400 KV transmission line from Amravati Thermal Power Project (TPP) to 400 KV substation of MSETCL and LILO of 400 KV Koradi – Akola line at Amravati TPP. Another subsidiary, Sinnar Power Transmission Company Ltd (SPTCL) is developing 400 KV transmission lines from Nasik TPP to 400 KV Bableshtar substation of MSETCL. The Bulk Power Transmission Agreement (BPTA) for the same has been executed.

Experience in rolling-out advanced technologies in utility-like business

IPL has submitted that IPL Group established one of the first online platforms in India for offering internet brokerage services. This was followed by establishment of Financial Services and Real Estate Services by the Group. The power business of IPL Group was established subsequently in 2007.

IPL has further submitted that the Group has full-fledged Enterprise Resource Planning (ERP) system across the organization embracing finance/accounting, sales and service, etc. with an integrated software application. The entire setup is equipped with the latest software and hardware.

IPL has also stated that it is implementing advanced and upgraded techniques in its power plants under construction.

54. Since, the Commission found that IPL's application does not conform to the provisions of the 2003 Act as well as the aspects relevant to grant of licence, the proviso to clause (b) of Section 15(6) of the 2003 Act was required to be complied with.

55. In terms of the proviso to clause (b) of Section 15(6) of the 2003 Act, an opportunity of being heard was granted by the Commission to IPL on August 2, 2011 before rejection of its application. During the course of the hearing, the Commission communicated its intention to reject the application of IPL for grant of licence after explaining the grounds, as described in the preceding Para 44 to Para 52.

56. During the hearing, IPL submitted that in the third parallel licensee scenario, it has assumed that the load growth in the area of supply of the existing licensee would be met by IPL as the third parallel licensee and that the projected capital expenditure would cater to this load growth. The applicant stated that this scenario is independent of the distribution network of the existing licensee.
57. Consumer Representatives, authorized under Section 94(3) of the 2003 Act, to represent the interest of the consumers in the proceedings before the Commission, expressed that the application of IPL should be rejected. Shri Ashok Pendse, of Thane Belapur Industrial Association (TBIA), Consumer Representative, submitted that the applicants' proposed power procurement cost is not in line with the prevailing competitive bidding rates. Shri Rakshpal Abrol and Shri Ponrathnam expressed their satisfaction about the conclusions reached by the Commission.
58. After assessing the application of IPL, the Commission is of the view that IPL's Application does not conform to aspects relevant to grant of distribution licence, on account of lack of action plan for geographical coverage and time frame for rolling out its own distribution network in the area of supply for which the licence is sought for.
59. Therefore, the application filed by IPL is rejected as it does not conform to the provisions of the 2003 Act required for grant of distribution licence as discussed above. However, the statute enables the making of application for grant of distribution licence at any time and enables the Commission to consider at any time the grant of two or more licenses in the same area.
60. In view of the above, the application of Indiabulls Power Limited for grant of Distribution Licence in and around suburbs of Mumbai in Case No. 5 of 2011 stands dismissed. Liberty is granted to apply afresh for grant of distribution licence keeping in view the statutory requirements of eligibility.

Sd/-
Vijay L. Sonavane
(Member)

Sd/-
V. P. Raja
(Chairman)