Statement of Reasons

Odisha Electricity Regulatory Commission (Terms and Conditions for Determination of Wheeling Tariff and Retail Supply Tariff) Regulations, 2022

ODISHA ELECTRICITY REGULATORY COMMISSION

December, 2022

Background

1. In exercise of the powers vested under Sections 61 and 181 (2) of the Electricity Act, 2003 (hereinafter referred to as "Act") and all other enabling powers and in compliance of the requirement under Section 181 (3) of the Act, the Commission had uploaded the draft of OERC (Terms and Conditions for Determination of Wheeling Tariff and Retail Supply Tariff) Regulations, 2022 on its website https://www.orierc.org/.
2. The Commission had invited Comments from stakeholders through Public Notices published in leading newspapers, which was also uploaded on the Commission's website https://www.orierc.org/. The last date for submission of comments from stakeholders on the said draft Regulations was 14.11.2022.
3. Stakeholders namely TPCODL, TPSODL, TPWODL, TPNODL, GRIDCO, Mr. Soumya Ranjan Pattnaik, Mr. Anand Kumar Mohapatra, Mr. Rabindranath Behera and Mr. Ashok Kumar Nanda have submitted their comments / suggestions / objections / recommendations etc. on the draft Regulations to the Commission.
4. After considering the comments of all stakeholders, the Commission has notified OERC (Terms and Conditions for Determination of Wheeling Tariff and Retail Supply Tariff) Regulations, 2022 on 20/12/2022.
5. This Statement of Reasons (SOR) is being issued with the intent of explaining the rationale and objective behind finalization of OERC (Terms and Conditions for Determination of Wheeling Tariff and Retail Supply Tariff) Regulations, 2022. However, in case of any deviation/discrepancy in the SOR with respect to OERC (Terms and Conditions for Determination of Wheeling Tariff and Retail Supply Tariff) Regulations, 2022, the provisions of OERC (Terms and Conditions for Determination of Wheeling Tariff and Retail Supply Tariff) Regulations, 2022 shall be applicable.
6. It is to mention for the sake of clarity, that the term "Commission" in most of the cases refers to the Officers of the Commission for carrying out the research/due diligence on the available information for preparation of SOR pertaining to OERC (Terms and Conditions for Determination of Wheeling Tariff and Retail Supply Tariff) Regulations, 2022.
7. The Stakeholders' comments along-with the Commission's views on various Regulations of the OERC (Terms and Conditions for Determination of Wheeling Tariff and Retail Supply Tariff) Regulations, 2022 are discussed further in this

document. Provision of some of the important Regulations relating to Multi Year Tariff (MYT) principle, Return on Equity (RoE), Depreciation, O&M Expenses and Fuel & Power Purchase Adjustment Surcharge (FPPAS) have been discussed in the SoR.

Vesting Orders

8. The Distribution system of Odisha has reached a unique stage of development. The responsibility of distribution of power has been vested to four (4) DISCOMs (TPCODL, TPNODL, TPWODL, and TPSODL) through four Vesting Orders issued under Section 21 of the Electricity Act, 2003 after acquisition of 51% of the equity by TPCL and 49% of the equity by GRIDCO on behalf of the Government of Odisha in each the four DISCOMs. The Vesting Orders have imposed certain conditionalities, trajectories etc. on the new DISCOMs in respect of AT&C loss, infusion of CAPEX and collection of outstanding dues of erstwhile Distribution Utilities etc. The Commission had notified Odisha Electricity Regulatory Commission (Terms and Conditions for Determination of Wheeling Tariff and Retail Supply Tariff) Regulations, 2014. The first control period provided in the Regulations has expired on 31.03.2019 though the Regulations are still in force as the said Regulations are not repealed.

9. Electricity Act, 2003 is a comprehensive piece of legislation. One provision cannot be read in isolation of other. The provisions of Regulations framed under Section 61 of the Act, which applies to any distribution licensee and the conditionalities on the Vesting Orders issued under Section 21 are to be read harmoniously and followed. However, when licensee comes through a Vesting Order then, Vesting Order shall have precedence over the Regulations which is general in nature. This is because Vesting Orders are specific to each licenced area of operation whereas Regulations are general in nature and applicable to the whole State. The second phase of privatization in Odisha is in nascent state. The Commission reframed the Regulations accommodating the provisions of the Vesting Orders and has now notified the new / instant Regulations named “Odisha Electricity Regulatory Commission (Terms and Conditions for Determination of Wheeling Tariff and Retail Supply Tariff) Regulations, 2022” which is aligned with the Vesting Orders.

Regulation 2.3.1: Multi Year Tariff (MYT) Principle

10. In MYT principle, the operational norms & trajectories of performance parameters are specified, which gives certainty to the principle to be adopted for determining different

components of tariff, such as employee cost, repair and maintenance expenses, administrative and general expenses and return on equity etc. along with a specified trajectory for AT&C loss. The Commission in this Regulation has segregated various components of ARR into controllable and uncontrollable cost. For example, distribution loss and employee cost are controllable whereas power purchase expenses and taxes on income are uncontrollable. Accordingly, the Business plan for each year of the entire control period i.e. FY 2023-24 to FY 2027-28 shall be submitted by the Applicant based on the above principle and forecast of ARR & expected revenue from tariff for each year of control period shall be approved by the Commission.

11. Apart from the Business Plan Petition, the Distribution Licensee shall file combined application every year for approval of Truing up of previous year; Annual Performance Review (APR) (considering actual performance of first 6 months and projection for next / subsequent 6 months of the year) for current year, Annual Revenue Requirement (ARR) for determination of tariff for ensuing Financial Year, as per timelines specified in **Annexure-I** of these Regulations. The Commission shall determine the wheeling tariff and Retail Supply Tariff every year under Section 62 of the Electricity Act, 2003. In addition to the instant Regulations, four Vesting Orders have been issued under Section 21 of the Act and have force of law. Accordingly, while adopting the MYT principle, the Commission shall also take into account the principles enumerated in these Regulations and the Vesting Orders.

Regulation-3.6: Return on Equity (RoE)

12. The Stakeholders have submitted that considering the rising interest rates and risk premium the RoE maybe allowed at 16% per annum post tax basis for the Control Period.

13. The base rate of RoE being allowed by various Electricity Regulatory Commissions (ERCs) in India have been studied before finalizing the base rate of RoE for the Distribution licensees. The Commission has observed that the base rate of Return on Equity specified by other State Electricity Regulatory Commissions (SERCs) like Haryana, Bihar, Gujarat, Telangana is allowed at 14% on equity investment, whereas in States like Madhya Pradesh, Rajasthan, Delhi, Telengana RoE is allowed at 16% for retail supply business.

14. The Commission is of the opinion that the RoE currently being allowed under Odisha Electricity Regulatory Commission (Terms and Conditions for Determination of

Wheeling Tariff and Retail Supply Tariff) Regulations, 2014 to the Distribution Licensee is reasonable and competitive, considering the current financial market condition, operating scenario and the performance of such Distribution Licensee with respect to similar Distribution Licensees of other States.

15. The Commission has, therefore, decided to continue with the existing rate of 16% on post tax-basis applicable for RoE under the OERC (Terms and Conditions for Determination of Wheeling Tariff and Retail Supply Tariff) Regulations, 2014.

Regulation- 3.8: Depreciation

16. The Stakeholders have submitted that longer term loans (in excess of 12 years) are difficult to secure and depreciation rates as per the Vesting Order may be continued.

17. The Commission has transferred the utilities to the TP DISCOMs with clean balance sheet apart from certain additional serviceable liabilities. Also, the gains accruing on account of better performance in reducing AT&C loss and incentive on past arrear recovery shall be allowed to be retained in full upto FY 2030 for the TP DISCOMs as per Vesting Orders. This would be over and above the return on its equity allowed by the Commission as a part of Annual Revenue Requirement and shall not be adjusted as other income or in any way appropriated through any Truing Up process or future Aggregate Revenue Requirement process.

18. In the Vesting Orders for the respective DISCOMs it has been provided that the capital investments shall be allowed. The recovery of depreciation in line with the rates prescribed in the Vesting Orders shall be made till the time of notification of new Regulations by the Commission. The depreciation rates specified in the new Regulations shall prevail over the rates specified in the Vesting Order as and when such Regulations are notified by the Commission. Therefore, the depreciation rates as specified in these instant Regulations shall prevail over the depreciation rates provided in the Vesting Orders.

19. Further, the DISCOMs are expected to avail long term loans while operating in a conducive environment with long repayment period. The lower depreciation rate shall also help the DISCOMs to be eligible for availing interest on loan for a longer period.. Therefore, the Commission has considered the depreciation rates as per the notified draft OERC (Terms and Conditions for Determination of Wheeling Tariff and Retail Supply Tariff) Regulations, 2022.

Regulation-3.9: O&M Expense

Employee Expense

20. The Stakeholders have submitted that the expense for employees joining after Effective date may be allowed to be recovered at CPI escalation over previous year plus a margin of 2% or 3%. One of the Stakeholder has suggested to allow employee expense as per actuals.

21. The Commission has allowed the expense against employees transferred from erstwhile DISCOM Utilities to be governed by the terms of their appointment and the same shall be allowed as per actual. Regarding the employees recruited after Effective date the expense shall be allowed considering average yearly inflation of Consumer Price Index (Industrial workers) over the previous year. However, the DISCOMs shall have the option to meet their additional employee expense (if any) from its share of the efficiency gain defined under the sharing of gains on account of controllable factors as listed under Regulation 2.14.

22. The Stakeholders have submitted that the number of employees as per CEA benchmarking may be increased to 1.7 per 1000 consumers against 1.40 employees per 1000 consumers mentioned in the draft Regulations. It is to be understood that the CEA reports are general in nature and are not State specific. The Commission has observed that the DISOMs have proposed to make huge investment amounting to around Rs. 5,640 Crore in a period of 5 years from their respective Effective dates. Major investments have been proposed to be made towards building robust IT infrastructure and Network Strengthening which shall reduce human intervention, improve system reliability and centralised control room shall require less manpower to monitor the distribution system. Further, the Commission has also observed that certain activities are also outsourced to Third party resulting in less manpower requirement. In view of the same, the Commission has preferred to retain its stand of 1.40 employees per 1000 consumers for normative calculation of employee expense.

Administrative and General (A&G) Expense

23. The Stakeholders have submitted that the actual A&G cost for FY 2022-23 may be escalated for subsequent years for determining normative A&G expenditure.

24. The Commission has already approved substantial A&G expenses for FY 2022-23 in the ARR Orders of the respective DISCOMs. Consideration of actual A&G expense for calculation of normative A&G expense for subsequent years shall impose huge

burden on the consumers. It is to be understood that the A&G expenses for the initial years after vesting of utilities would have increased over previous year due to regularization of various expenses which were not properly accounted for in earlier years and shall stabilize within a year. All the new DISCOMs have already completed their first year of operation and henceforth their A&G expenses are expected to remain at same level or go down. Therefore, only normative escalation of 7% over A&G expense approved for previous years has been considered which is also in line with OERC (Terms and Conditions for Determination of Wheeling Tariff and Retail Supply Tariff) Regulations, 2014.

Repair & Maintenance (R&M) Expense

25. The Stakeholders have submitted that

 a. the existing allowance of R&M expense @ 5.4% of opening GFA [as per OERC (Terms and Conditions for Determination of Wheeling Tariff and Retail Supply Tariff) Regulations, 2014] has been grossly insufficient and therefore, the actual R&M expenditure, subject to prudence check, to be trued-up for the first five years after Effective date and norms for balance period to be revised based on past years Actual Expenditure, through a Mid Term Review of the Norms.

 b. R&M norms may be determined considering normalised actual (post Effective Data).

However, one of the Stakeholders has submitted a comparative analysis of R&M expense of DISCOMs of other States which are less than or around 3% of opening GFA.

26. The Commission has observed the norms and actual R&M expense of DISCOMs of other States and has found that the R&M expense is well below 3% of opening GFA level. Since majority of the distribution assets are commissioned only few years ago, they shall require less maintenance and huge capital investment for creating of new assets, network strengthening etc. shall help in bringing down the R&M expense. However, considering that the DISCOM utilities have been vested recently, the new DISCOMs shall take some transition time to bring down their R&M expense to the level of 3% in view of very negligible R&M expense done in period prior to Effective dates. Therefore, the Commission has provided specific trajectories of R&M expense

for individual DISCOMs to reach the normative level of 3% of opening GFA by end of this control period in a phased manner.

Regulation- 3.10: Interest on Working Capital

27. The Stakeholders have submitted that the Maintenance Spares may be considered as 40% of R&M expense for one month in place of 20% of R&M expense for one month and receivable of one month may be considered in place of one-month power purchase cost while calculating Working Capital requirement.

28. The Commission is of the opinion that the Maintenance Spares shall be limited to 20% of R&M cost for one month however, the DISCOMs have the flexibility to opt for additional R&M under special circumstances which may be allowed by the Commission after prudence check. Power Purchase expense is one of the major expenses incurred by the DISCOMs, which has to be paid on monthly basis. Therefore, the same has been considered as a part of Working Capital requirement. Considering the receivable for one month, shall end up in double accounting of the other costs forming a part of Working Capital Requirement. Therefore, same has not been considered as a part of Working Capital Requirement.

Regulation- 5.7: Fuel and Power Purchase Adjustment Surcharge (FPPAS)

29. Rule 14 of the Electricity (Amendment) Rules, 2022 specifies that the Commission shall specify a price adjustment formula for recovery of the costs, arising on account of variation in price of fuel or power purchase costs. The impact in the cost due to such variation shall be automatically pass through to the consumers subject to True-up on annual basis.

30. Accordingly, the Commission has introduced the provision for levy of Fuel and Power Purchase Adjustment Surcharge (FPPAS) by GRIDCO on the DISCOMs on monthly basis with prior permission of the Commission. The Distribution Licensee(s) shall subsequently recover, such FPPAS from the consumers on monthly basis in the form of Power Purchase Surcharge (PPS) in proportion to their energy consumption with prior permission of the Commission. The PPS recoverable from the consumers for any month shall not be more than Rs. 0.20/kWh (20 paise/unit) for avoiding tariff shock to the consumers. However, the unrecovered PPS for any month shall be considered at the time of truing up. This back-to-back recovery of power purchase cost arrangement shall help in reducing the burden of carrying cost on the consumers.