

Before the
MAHARASHTRA ELECTRICITY REGULATORY COMMISSION
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Case No. 21 of 2006

In the matter of
Review of Determination of Annual Revenue Requirement (ARR) for FY 2006-07 for
Maharashtra State Electricity Transmission Company Ltd. (MSETCL).

Dr. Pramod Deo, Chairman
Shri A. Velayutham, Member
Shri S. B. Kulkarni, Member

ORDER

Dated: 19th October, 2006

Upon directions from the Maharashtra Electricity Regulatory Commission (MERC), Maharashtra State Electricity Transmission Company Limited (MSETCL) submitted its application for approval of Annual Revenue Requirement and Tariff Petition for 2006-07, under affidavit. The Commission, in exercise of the powers vested in it under Section 61 and Section 62 of the Electricity Act, 2003 (EA 2003) and all other powers enabling it on this behalf, and after an elaborate process, determined the ARR for transmission of electricity by the Maharashtra State Electricity Transmission Company Limited for FY 2006-07 vide its detailed order dated 28th June 2006.

Subsequently, MSETCL filed a Petition under Affidavit (listing specific grounds on which it sought review against specific aspects of the detailed order) with the Commission vide its letter Ref. No. MSETCL/CO/CR-RC/ARR/Review Petition/8108 dated 10th August 2006 under the provisions of regulation 85 of the MERC (Conduct of Business) Regulation 2004 as under:

“85. (a) Any person aggrieved by a direction, decision or order of the Commission, from which (i) no appeal has been preferred or (ii) from which no appeal is allowed, may, upon the discovery of new and important matter or evidence which, after the exercise of due diligence, was not within his knowledge or could not be produced by him at the time when the direction, decision or order was passed or on account of some mistake or error apparent from the face of the record, or for any other sufficient reasons, may apply for a review of such order, within forty-five (45) days of the date of the direction, decision or order, as the case may be, to the Commission.”

The MSETCL's Review Petition was heard for admission in presence of authorised consumer representatives on 5th September 2006 at 12.00 Hrs in the Office of the Commission. In the admissibility hearing MSETCL was also permitted to make a presentation on various issues including merits.



Through this Order the Commission provides its views and / or rulings on various issues as set hereunder:

1. TRANSMISSION LOSSES

1.1 MSETCL's Submission

Subsequent to the issue of the detailed Order, MSETCL requested the Commission (vide letter dated 12th July 2006) for a copy of CPRI's Report to enable them to study and take a view. The copy of CPRI's Report was stated to be received by MSETCL on August 3, 2006. MSETCL submitted that since the Commission had relied mainly on the CPRI Load Flow Study Report to decide on the allowable level of transmission loss, they would like to comment on the said report as follows:

- 1) *“CPRI has considered duration of peak, intermediate and light load, based on load duration curves for 52 sample days during FY 2004-05 to undertake load flow studies for all seasons. CPRI has assumed that the full capacity of Koyna hydel generation is used for the entire peak duration. The Hon'ble Commission will appreciate that due to flow of power from Eastern to Western region, losses in MSETCL system largely depend on utilization of Koyna generation capacity in MW. Due to restrictions on the utilization of water, Koyna generation capacity (1700-1850 MW) is used to the full extent to meet peak demand only for an hour or two, while during rest of the peak hours, Koyna generation is restricted to 700 to 1000 MW only. Hence, the losses will be higher during the remaining duration of peak demand.*
- 2) *For all 52 sample days during FY 2004-05 considered by CPRI, the HVDC bipole operation has been assumed at the constant level of 1200 MW. This, however, does not reflect the actual HVDC operation during FY 2004-05. The Hon'ble Commission will appreciate that HVDC operations have direct impact on transmission losses in MSETCL network”.*
- 3) Further, during presentation MSETCL contended that CPRI had considered gross generation (including auxiliary losses) of the MSPGCL power station instead of net generation at bus level, in arriving at the transmission loss levels through the load flow studies. Hence the transmission loss levels would be higher.

MSETCL also submitted that the Commission had mentioned about comparison of MSETCL network with that of the states like Andhra Pradesh, Karnataka, Gujarat and Madhya Pradesh while arriving at its conclusion of allowable transmission loss. On this issue MSETCL submitted that the numbers of voltage levels in MSETCL's transmission system are 7 (seven), i.e., 500 kV, 400 kV, 220 kV, 132 kV, 110 kV, 100 kV and 66 kV. MSETCL produced a comparison of transmission losses allowed by the respective SERC to various State Transmission Utilities (STU) as given in Table below along with the number of transmission voltage levels.



Table: Comparison of Losses allowed to other STUs in FY07

Parameter	Maharashtra	M.P.	A.P.	Karnataka	Gujarat
Transmission Losses (%)	6%	5%	4.55%	4.06%	4.27%
No. of Voltage Levels	7	3	3	4	4

MSETCL advocated that the number of voltage levels in case of MSETCL is significantly higher as compared to other STU's and that with each additional voltage of transmission, the transformation losses and the transmission losses will increase.

As per the provisional Transfer Scheme, the Transmission network of 66 kV and above, and existing EHV sub-stations feeding the distribution system having secondary output at 33-22-11kV levels forms part of the Transmission System and are to be maintained by MSETCL. At present, out of 1148 Nos of transformers with 46327.2 MVA capacity, 949 No of Transformers with 23231.81 MVA capacity are having step down level of 33-22-11 kV feeding Distribution System. Also, number of 33-22-11 kV bays is 3422 out of total 6514 bays. The transmission losses of MSETCL include transformation losses in step down up to 33-22-11kV.

MSETCL has highlighted that the geographical spread between the generation stations in the State and the load centres is far greater in Maharashtra as compared to other States, which contributes to higher losses. The load centres in the Western Region comprise nearly 56% of total Energy handled by MSETCL in the State while 63% of the generating capacity is located in Eastern Maharashtra as shown in Table below. In an effort to substantiate MSETCL had also given details of Circle-wise break up of Energy handled and Generation Capacity break-up in Annexure to its Review Petition.

Table: Region-wise break-up of Generation Capacity and Energy handled by MSETCL

Region	Energy Handled by MSETCL		Generation	
	MU	%	MU	%
Western	34849	56%	18667	37%
Eastern	27830	44%	32341	63%

MSETCL had further pointed out that in accordance with Para 2.7.7 of the Commission's Order in Case 58 of 2005 on Transmission Pricing Framework for the State of Maharashtra, the transmission loss considered for estimation of the energy transmitted is the average loss level in the intra-State transmission network. As the loss levels in the transmission network of The Tata Power Company Ltd. (TPC) and Reliance Energy Limited (REL) are lower than the average loss level of the intra-State transmission network, owing to their significantly lower network size, the loss level in MSETCL's transmission network would be higher than the average loss level of the intra-State transmission network. Thus, as the intra-State transmission losses have been specified as 4.85% for FY 2006-07, the transmission loss in the MSETCL system will be higher.



MSETCL had submitted, without prejudice to its contention, that the approved level of transmission loss at 4.60% and 4.85% is incorrect. Even for argument's sake if the same level is accepted as the theoretical level of transmission loss for a system of MSETCL's size on the basis of the CPRI Report, it is still inappropriate to consider the transmission loss at these levels, because these are theoretical loss levels, and the actual loss levels are higher. MSETCL emphasized that the National Tariff Policy issued on 6th January 2006, discusses the general approach to tariff fixation in detail. In section 5.3 (h) (2), the NTP stipulates that "where operations have been much below the norms for many previous years the initial starting point in determining the revenue requirement and improvement trajectories should be recognized at "relaxed" levels and not at "desired" levels." Hence, they urged the Commission to allow the actual loss levels in FY 2005-06 and FY 2006-07 and give adequate time to MSETCL to reduce the losses to normative levels.

MSETCL, based on the above arguments, submitted that the transmission loss allowed by the Commission for FY 2005-06 and FY 2006-07 qualifies for 'review' under all the heads stipulated under the MERC (Conduct of Business) Regulations, 2004, viz.:

- *"upon the discovery of new and important matter or evidence which, after the exercise of due diligence, was not within his knowledge or could not be produced by him at the time when the direction, decision or order was passed, or*
- *on account of some mistake or error apparent from the face of the record, or*
- *for any other sufficient reasons".*

Hence, MSETCL requested the Commission to review the transmission loss allowed in its Order, and allow loss level of 6% for both FY 2005-06 and FY 2006-07, as sought by MSETCL in its ARR and Tariff Petition.

1.2 Commission's Observations and Ruling

The Commission, since its inception, has been alarmed with the high level of T&D Losses in the erstwhile MSEB network. It has continuously focussed on the urgent steps needed to reduce the same for commercial viability of the utility. Despite several directions in the past to first carry out scientific assessment and then to target reduction of the transmission and distribution losses in a time bound manner, the concerned Utilities (both before and or after restructuring) have not displayed any meaningful action. The Commission has time and again reiterated the need for carrying out the State-wide load flow studies of the transmission network in order to arrive at the scientifically determined levels of transmission losses. This need was set out consistently in various orders on renewable energy sources (Case No. 25 of 2004 dated 9th November 2005, _ Case No. 37 of 2003 dated 8th August 2005, Case No. 17(3), 3,4 & 5 of 2002 dated 24th November 2003, Case No. 8/9/10/.../21 of 2001 dated 16th August 2002, and captive power plants (Case No. 55 & 56 of 2003 dated 8th September 2004). This interim situation is even referred by MSETCL in its reply to MEL (Point no. 2.2 on 'MSETCL's response' on page 15 of the Commission's detailed order in Case No.49 of 2005 on Determination of ARR for MSETCL for FY 2005-06 and 2006-07). It is regrettable that neither the erstwhile MSEB nor the successor entity MSETCL has displayed any serious efforts to carry out such studies on their own initiative in order to bring in transparency as well as take steps to reduce the transmission losses; a highly controllable element.



In fact, it was expected that while filing the ARR Petition due care would be taken by MSETCL, a restructured transmission arm of the erstwhile MSEB, also designated as State Transmission Utility (STU) under the Act. It should have carried out the Load Flow studies before approaching the Commission with its petition for ARR determination for FY 2006-07. It is unfortunate that they have submitted the ARR Petition after 3 years without any back-up study to substantiate its claim for Transmission Losses. The Commission had no option but to appoint CPRI for carrying out the Load Flow Studies.

Such kinds of Load Flow Studies are not a one-time effort but are to be carried out periodically. The Commission hereby directs MSETCL to conduct such studies, both in the capacity of STU and as MSETCL as a Transmission Licensee, by associating with other utilities, periodically. It is cautioned that in the absence of such efforts, the Commission cannot be expected to accept its unsubstantiated claims whatsoever. To meet the need of scientifically validated projection the Commission will get these studies done whenever needed and apply the findings and / or results thereof for meaningful regulatory exercise. As regards the factual 'discrepancy' pointed out, the Commission notes that the CPRI study was carried out solely on the basis of information/data supplied by MSEB transmission wing (now MSETCL) and SLDC itself with inputs from other licensees and as such MSETCL's disputing the same cannot be accepted.

With respect to the issue raised by MSETCL on varying levels of Koyna generation and availability of peak generation levels (1700-1850 MW) for only about 1 or 2 hours in a day (which could result in increased transmission losses during the remaining peak demand than that arrived at through the load flow studies), the Commission clarifies that the generation data file prepared for the load flow studies is based on generation scheduling information provided by SLDC, Kalwa, an arm of erstwhile MSEB. As such this point of finding error with the report is not understood.

On the issue of assumption in the CPRI Report that for all the 52 sample days during FY 2004-05, the HVDC Bi-pole operation has been assumed at the current level of 1200 MW and that this does not reflect the actual HVDC operation during FY 2004-05 (which would directly impact on the transmission losses of MSETCL), the Commission feels that instead of furnishing information to CPRI on actual HVDC operation during FY 05 during study and maintaining the asset properly to ensure system availability, MSETCL has proposed increase in losses. Expenditure on the installation of HVDC bipolar equipment at the cost of consumer has been justified as such for reducing the transmission loss while carrying bulk power over a longer distance. The Commission is very much dissatisfied with MSETCL's (erstwhile MSEB) inability to meet its responsibility to maintain the highest level of availability of the HVDC Bi-pole link in its network. Any burden of increased level of transmission losses due to MSETCL's inability to maintain the availability of the HVDC Bipole Link operation cannot be passed on to the consumers and has to be borne by MSETCL. Besides the Commission has weighed the impact of the Monopole Operation vis-à-vis the Bipole Operation of the HVDC Link and given due consideration while prescribing the allowable transmission loss levels. Hence, the Commission does not find any rationale in the argument of MSETCL pointing out error in assumption of CPRI Report on the operation of HVDC link and that the determined level of losses should be reviewed.



On the issue raised by MSETCL that CPRI Report has considered duration of peak, intermediate and light load based on load duration curves for 52 sample days during FY 2004-05 to undertake load flow studies for all seasons the Commission has already considered this as the limitation of the data sampling to capture operation in 2004-05 and accordingly allowed for a higher loss levels of 4.6% for FY 2004-05 and FY 2005-06. Also, Keeping in view the additional power flows from the eastern corridor and some uncertainties in the western corridor generation (e.g. Koyna Hydro generation and Dabhol Power Company) and considering that the demand for power is going to be high, the Commission envisaged that the transmission losses in the MSETCL network are bound to increase in FY 2006-07. The issue here is of projections based on scientific model at hand; hence, the Commission had consciously approved a higher transmission loss level of 4.85% for the MSETCL network for FY 2006-07.

The Commission has noted the point raised by MSETCL on the usage of gross generation levels for MSPGCL power plants in its load flow studies in place of the net generation at bus level. The impact of usage of net and gross generation levels in the load flow study and the resulting difference in the transmission loss levels is not highly significant as being contended. Therefore, the approved loss level by the Commission should adequately meet the actual correctly metered loss level.

The Commission finds it ironic, when in order to justify review of loss level, MSETCL seeks to compare the voltage level in the network of other States with that of its own voltage levels at 132 kV or 110kV or 100 kV (three voltage transformation levels for comparison as referred to by it). These levels are in effect comparable to one genre of normative voltage transformation level of either 110 kV or 132 kV in other state networks. Hence, the voltage level of 132kV, 110kV or 100 kV for MSETCL should be considered as a single step down voltage level in its network. With this metric for comparison the numbers of transformation / transmission voltage levels in MSETCL's network are just 4 levels, excluding the HVDC level (which is in effect implemented to reduce the network losses and cannot be considered as a separate voltage level for the purpose of comparison). Therefore, the argument of MSETCL, pointing out error or discovery of new matter, is not worth considering.

The Commission has already taken into consideration the point that the geographical spread between the generating Stations in the State and the load centres is greater in Maharashtra as compared to other states when it ruled in the detailed order that:

“Keeping in view the additional power flows from the eastern corridor and some uncertainties in the western corridor generation (e.g. Koyna Hydro generation and Dabhol Power Company) and considering that the demand for power is going to be high, the transmission losses in the MSETCL network are bound to increase in FY 2006-07. Therefore, the Commission has approved a transmission loss level of 4.85% for the MSETCL network for FY 2006-07.”

Hence, the argument of MSETCL that the Commission is not taking cognizance of the effect of the geographical spread while approving loss level of 4.85% for FY 2006-07 is not correct.



In its Order on transmission pricing framework, the Commission had crystallised the transmission-pricing framework for all the transmission licensee's in the State based on aggregating the Annual Revenue Requirement of these transmission licensees and design of a combined statewide transmission tariff. The Commission observes that out of system energy consumption of 80259 Million Units (MU) the annual energy loss in Maharashtra transmission network is 3467 MU (4.319%) as per CPRI load flow study report based on actuals for FY 2004-05. Hence MSETCL's contention of higher loss in its system, when considered alone, has been adequately taken care of. In view of the above observations the Commission rules that the transmission loss levels as approved in the detailed order (4.6% for FY 2004-05 and FY 2005-06 and 4.85 % for FY 2006-07) hold and MSETCL should make a sincere attempt to meet the approved transmission loss levels.

2. OPERATIONS AND MAINTENANCE (O & M) EXPENSES

2.1 MSETCL's Submission

MSETCL in its ARR and Tariff Petition proposed O & M expenses at Rs. 410.3 Crore and Rs. 467.08 Crore for FY 2005-06 and FY 2006-07 respectively. In its Review Petition, MSETCL had referred to the O & M Norms specified in CERC (Terms and Conditions of Tariff) Regulations and stated that if these norms were to be applied to the calculation of O&M expenses, the allowable O & M expenditure would be significantly higher than the actual expenses claimed.

MSETCL in its Review Petition stated that the Commission had allowed O & M expenses to the extent of Rs. 375.55 Crore and Rs. 388.09 Crore for FY 2005-06 and FY 2006-07 respectively. MSETCL was of the view that reduction in the allowable O&M expenditure by the Commission would lead to problems for MSETCL, and restrict MSETCL's ability to maintain its system effectively. MSETCL submitted that since the O&M expenses claimed by MSETCL in its petition were much lower than the CERC norms, the Commission should have allowed the O&M Expenses to the extent claimed.

2.2 Commission's Observations and Ruling

While approving the expenditure projections for FY 2005-06, the norms for approval of ARR and principles for determination of tariff as enunciated in the latest Tariff Orders of the licensee have been taken as the basis. Thus, the principles enunciated in the Commission's Order dated 10.03.2004 (Case No. 2 of 2003) for MSEB as a whole have been applied while approving the expenses of MSETCL for FY 2005-06.

However, for the determination of ARR for FY 2006-07, the MERC (Terms and Conditions of Tariff) Regulations 2005, have been followed.

As regards the adoption of the CERC norms, the Commission is of the view that these norms take into consideration the entire transmission function across the States like Assam and Jharkhand at one end of the spectrum and Maharashtra, Andhra Pradesh at the other end of the spectrum. MSEB had been claiming itself to be one of the most efficient utilities in the country; therefore the Commission is of the view that the same norms cannot be made applicable to O&M expenses for MSETCL, a restructured identity of MSEB in transmission function.



O & M expenses comprise (a) Employee expenses, (b) Repairs & Maintenance (R&M) expenses, and (c) Administration & General (A&G) expenses. Issues regarding each of these expenses and the Commission's rulings on the same have been discussed in the subsequent paragraphs.

3. EMPLOYEE EXPENSES (PART OF O & M EXPENSES)

3.1 MSETCL's Submission

MSETCL submitted that 44 new substations had been added in the past three to four years with no corresponding change in the number of sanctioned employees of MSETCL. Hence, MSETCL projected the cost of additional employees for FY 2006-07.

MSETCL submitted in its Review Petition that the Commission has disallowed the cost of additional employees without assigning any specific reason for the same. MSETCL submitted that even if the management of these substations were to be outsourced, this would correspondingly increase the A&G expenses. However, the Commission had significantly reduced the allowable expenditure on A & G expenses. MSETCL further submitted that the disallowance of additional cost either under employee expenditure or A&G expenditure would pose difficulties in managing the new substations. .

MSETCL requested the Commission to review the employee expenses allowed in its Order under the head, "on account of some mistake or error apparent on the face of the record, as well as under the head, "for any other sufficient reasons", and allow employee expenses for FY 2005-06 and FY 2006-07, as sought by it in its ARR and Tariff Petition.

3.2 Commission's Observations and Ruling

a. Growth in employee expenses

The Commission is of the view that for FY 2005-06, ARR should be computed based on the principles in the earlier Tariff Order dated March 10, 2004 for MSEB as a whole. As per the principles in the said Order, the Commission has projected the employee expenses for FY 2005-06 and FY 2006-07 by applying a 5-year CAGR to employee expenses of the previous year.

Based on the trends for the past 5 years (FY 2001 to 2005), it is observed that employee expenses have increased @ CAGR of 6.2%. Similarly for the years 2002 to 2006, the CAGR is @ 7.1% in employee expenses. Thus the Commission has applied a growth rate of 6.1% for FY 2005-06 and FY 7.1% for 2006-07 for estimating employee expenses for MSETCL.

The capitalization rate applied is the average capitalization rate observed in the past 3 years (for employee expenses and A&G expenses for MSEB as a whole).

b. Increase in employee cost due to addition of 44 sub-stations

The Commission is of the view that the employee expenditure should be reduced through redeployment of manpower currently not used effectively and increases in productivity per person. However, the Commission notes that MSETCL's employee expenses have been increasing as it has shown in the ARR Petition as for year 2004-05 it is Rs.245.83 Crore, for year 2005-06 it is Rs. 264.28 Crore and for year 2006-07(P) it is Rs. 297.13 Crore. However, neither the generation nor the quantum of energy transmission has increased in that



proportion. Also, control has to be exercised over the expenses of MSETCL on transmission of electricity.

For the addition in employee expenses due to an increase in the number of employees for the 44 new sub-stations, MSETCL in its Petition dated 23.5.2006 has stated that the additional requirement of employees on this account has been calculated, after considering the redeployment possible. Further, MSETCL has also estimated the increase in employee expenditure on a proportional basis, considering the increase in number of employees at different levels. However, the MSETCL has not substantiated this with submission of any supportings/ Assessment Report on the reasoned basis of the requirement of addition of employees. MSETCL's contention is not validated by rationalized manpower deployment and this can be managed within cost. Addition of more employees purely on account of 44 additional substations is not justified. Effective redeployment of manpower is licensee's responsibility and there are also different ways of managing the employee expenses. Further, the Commission feels that the O&M Expenses are to be taken as a whole and MSETCL could combine the approved levels of Employee Expenses (as in detailed order) with the approved level (as in detailed order) of A&G Expenses to manage the overall costs for these expense heads within limits. MSETCL has compared the Employee Expenses just for 2 years and shown that there is a decrease in approved levels but without providing any justification. Therefore, the Commission had to take an average growth rate of 5 years for estimating the Employee Expenses. In fact, even while submitting the Review Petition on 10th August 2006, MSETCL has not submitted actual figures up to July 2006, in support of the data of the past years. MSETCL has also not submitted any authenticated/ audited Report on Revenue Statement in absence of Audited Annual Accounts for FY 06.

However, as it may be seen in the Commission's Order dated 28.06.2006, the employee expenses allowed by the Commission are Rs. 289.66 Crore and Rs. 303.96 Crore for FY 2005-06 and FY 2006-07 respectively as against those proposed by MSETCL viz., Rs. 264.28 Crs for FY 2005-06 and Rs. 297.13 Crs for FY 2006-07 respectively. Thus the employee expenses allowed by the Commission are in fact higher than the expenses projected by MSETCL.

The Commission is therefore of the view that there is no mistake or error apparent on the face of record, neither there is any other sufficient reason for the issue to qualify for a review under the Commission's Regulations.

4. REPAIRS & MAINTENANCE (R & M) EXPENSES

4.1. MSETCL's Submission

In its Petition, MSETCL had projected R & M expenses at Rs.105 Crore for FY 2005-06 and Rs. 127 Crore for FY 2006-07 and in its Review Petition it pointed out that, the Commission had allowed R&M expenses at Rs. 61 Crore and Rs. 60 Crore for FY 2005-06 and FY 2006-07 respectively.

MSETCL submitted in its Review Petition that the R&M expenses were very low @ 0.9% of GFA for FY 2004-05 and needed to be increased to at least 1.5% of opening GFA in order to enable MSETCL to maintain its system network in proper working condition.



MSETCL submitted that since it was a newly formed company, there was a greater need for adequate R&M expenditure. MSETCL further submitted that if the appropriate R&M expenditure were not allowed, regular maintenance work would suffer and hamper smooth grid operations, which would result in demand supply gap.

MSETCL submitted that the actual R & M expenses for FY 2004-05 for the Transmission division were Rs. 70 Crore. However, the approved R&M expenses were much lower than the actual expenses incurred in prior years and hence MSETCL requested for a review of the same.

4.2. Commission's Observations and Ruling

In the last Tariff Order of MSEB (dated 10.03.2004), R&M expenses were projected at 3% of opening GFA. However, this was for MSEB as a whole. The R&M expenses for Generation and Distribution function are higher than the Transmission function (based on past trends). The Commission has analysed the R&M expenses for the Transmission function/ MSETCL based on past years Statement of Accounts of MSEB.

The Commission is of the view that the Repairs and Maintenance (R&M) expenses should be computed on the basis of the average R&M expenses of the Transmission function (i.e. MSETCL) of MSEB as a percent of opening GFA for past 3 years.

The R&M expenses have been capitalised at the average capitalisation rate observed in the past 3 years (for MSEB as a whole). The opening GFA considered for FY 2005-06 and FY 2006-07 is for MSETCL as a State Transmission Utility and does not include GFA of the SLDC function.

The Commission shall consider any actual incurrence of one-time R&M expenses in FY 2006-07 over and above the approved R&M expenses for current year, for truing up in next year. However, to be eligible for such truing up, MSETCL should get the Commission's prior approval on its detailed R&M Expenses plan supported by appropriate justification.

The Commission is therefore of the view that there is no mistake or error apparent on the face of record, neither there is any other sufficient reason to justify a review under the Commission's Regulations.

5. ADMINISTRATION & GENERAL (A & G) EXPENSES

5.1. MSETCL's Submission

MSETCL in its Petition had considered increase in the A&G expenses at a nominal rate of 5% per annum in FY 2005-06 and FY 2006-07, over FY 2004-05 and FY 2005-06 levels, respectively, which was lower than the prevailing Consumer Price Index (CPI) for industrial workers in India.

MSETCL had submitted that actual net A&G expenses incurred in FY 2004-05 were Rs. 33.89 Crore. However, the A&G expenses allowed by the Commission for FY 2005-06 and FY 2006-07 was much lower than the actual expenses in FY 2004-05.



MSETCL submitted that the Commission had considered year-on-year growth of 4.21% on the approved expenses in FY 2003-04 Tariff Order for projecting A&G Expenses, instead of allowing A&G expenses in accordance with the Commission's Tariff Regulations, which provided for consideration of past trend.

MSETCL further submitted that the Commission needed to consider that the A& G expenses would not reduce with the passage of time. Also that the MSETCL's submission that the increase in A & G expenses at a rate lower than that of the inflation rate was very reasonable. However, the Commission did not consider this.

MSETCL in its Review Petition submitted that if the 44 new substations were to be managed through outsourcing, instead of additional manpower, the A&G expenses would correspondingly increase. However, the Commission had significantly reduced the allowable expenditure on A&G also.

5.2. Commission's Observations and Ruling

In its Order dated 10.03.2004 (Case No. 2 of 2003) for MSEB as a whole, the Commission has specified that it is of the view that the A&G expenses can and should be controlled by the MSEB. Hence, it cannot simply allow an increase over the actual expenses in FY 2002-03. The Commission has hence considered a YOY increase of 4.2% over the A&G expenses allowed by the Commission in FY 2001-02, to determine the A&G expenses for FY 2003-04.

Based on the data provided by MSETCL, the CAGR for A&G expenses for the past 4 years (FY 2001 to 2004) and past 5 years (FY 2001 to FY 2005) is negative (after allocating the common expenses of MSEB to the Transmission division on a pro-rata basis). Thus the CAGR cannot be taken as a basis to project expenses for FY 2005-06 and FY 2006-07.

Therefore, for estimating the Administration and General (A&G) expenses for FY 2005-06, the Commission has considered a year-on-year (YoY) increase of 4.21% over the A&G expenses as approved by the Commission for FY 2004 in its Tariff Order dated 10th March 2004 for MSEB as a whole. For estimating the A&G expenses for FY 2006-07, the Commission has considered a year-on-year (YoY) increase of 4.21% over the A&G expenses of the previous year (i.e. 2005-06).

The A&G expenses have been capitalised at the average capitalisation rate observed in the past three years (for employee expenses and administration and general expenses for MSEB as a whole).

In any case, as ruled earlier, O & M Expenses are to be treated as a whole and if MSETCL decides to outsource the additional manpower, then it can allocate these expenses as a part of A&G Expenses and accordingly manage Employee Expenses, A&G Expenses and R&M Expenses collectively within the overall limit of O&M Expenses.

Based on the above, the Commission is of the opinion that the A&G expenses as projected in the Order (Rs. 25.08 Cr for FY 2005-06 and Rs. 24.50 Cr for FY 2006-07) are adequate and justified. The Commission is therefore of the view that there is no mistake or error apparent on the face of record, neither there is any other sufficient reason to qualify for a review under the Commission's Regulations.



6. INTEREST EXPENDITURE

6.1. MSETCL's Submission

MSETCL, in its ARR and Tariff Petition, projected interest expenditure on long-term loans as Rs. 429 Crore each in FY 2005-06 and FY 2006-07. MSETCL submitted that the Commission, however allowed only Rs. 289 Crore and Rs. 275 Crore of long-term interest expenditure in FY 2005-06 and FY 2006-07, respectively.

MSETCL had stated that the Commission's Order did not provide the calculations, the source-wise loans considered and the interest allowed in each year, which was usually given in the Commission's Orders, when source-wise loan details were available and actual loans were being considered. Hence, MSETCL requested the Commission to share the calculation of loans and interest details for each year, to enable MSETCL to study the same and put forth a studied response. MSETCL further submitted in its Review Petition that this data was not shared with MSETCL.

MSETCL submitted that it had recreated the calculations in absence of relevant details in the Commission's Order. MSETCL further stated that the Commission's approach for computation of interest expenditure was inappropriate on the following counts:

a. Computation of interest on the basis of average of opening and closing loan balances for the year

MSETCL had submitted that Interest computation is usually undertaken on the basis of average and closing loan balances, only when the actual tranche-wise loan repayment details are not available. MSETCL submitted that the Commission should appreciate that the loan repayment and interest payments are made in accordance with the actual loan agreements with the lenders, which specify the moratorium period, tranche-wise loan repayment schedule and frequency of interest payment, and are not based on simplistic calculation on the basis of average of opening and closing loan balances. MSETCL stated that during the tariff process, the Commission had specifically sought information on source-wise and tranche-wise loan repayment and interest payments due for FY 2004-05, FY 2005-06 and FY 2006-07, which was duly submitted by MSETCL in its review petition. MSETCL submitted that the Commission should have rightfully considered the actual tranche-wise loan repayment and interest payment, for computing the interest expenditure for FY 2005-06 and FY 2006-07, rather than considering the average and closing loan balances.

b. Allowance of actual interest payable in FY 2005-06 and FY 2006-07

MSETCL further submitted that the Commission had disallowed interest expenditure and repayment on account of loans held by the Holding Company (which had not been allocated to the successor companies) as well as Dabhol Power Corporation (DPC) related loans. The Commission had also allowed additional loans only to the extent of capitalization of fixed assets. MSETCL submitted that the Commission's approach of considering additional loans only to the extent of capitalization of fixed assets was incorrect for the past years, wherein the loans had actually been serviced by MSETCL. During the tariff process, MSETCL had



provided details of the assets capitalised, which included the component of interest capitalised.

6.2. Commission's Observations and Ruling

a. Disallowance of loans

In its earlier Tariff Order of MSEB dated 10.03.2004, the Commission had disallowed the interest on loans taken for investment in the Dabhol Power Corporation (DPC). Thus, while computing interest for FY 2005-06 and FY 2006-07 for MSETCL, the interests on loans taken for investment in DPC have been disallowed.

In order to compute the interest on loans, the loan balance outstanding of MSETCL (as per the Balance Sheet as on 31st March, 2004) based on the Provisional Transfer Scheme has been considered as the Opening loan balance in FY 2004-05. The loans held by the Holding Company (which have not been allocated to the successor companies) have not been considered while computing loans and interest of MSETCL. Hence interest on such loans has also been disallowed.

As per the earlier Tariff Order of MSEB (dated 10th March 2004), the Commission observed that the MSEB has been taking loans to meet its revenue shortfall apart from the projected capital expenditure. However, the Commission has allowed additional loans only to the extent of the projected capital investment.

Thus in line with the earlier Tariff Order (dated 10th March 2004) for MSEB as a whole, the Commission has allowed additional loans (borrowings for the year) only to the extent of capitalisation of fixed assets for FY 2005-06. Further, the Commission has assumed that the capitalisation of fixed assets for FY 2004-05 and 2005-06 has been funded entirely through debt since no equity has actually flown into MSETCL.

For the year 2006-07, the loan amount is taken as 70% of the allowable capital expenditure for the year, in line with the MERC (Terms and Conditions of Tariff) Regulations, 2005.

b. Interest Computation

The Commission notes that MSETCL has submitted source-wise and tranche-wise data. However, the Commission has made various adjustments while computing the loans as under:

In order to compute interest on loans, the loan balance outstanding of MSETCL (as per the Balance Sheet as on 31st March 2004) as per the Provisional Transfer Scheme has been considered as the Opening balance for FY 2004-05. The loans held by the holding company (which have not been allocated to successor companies) have not been considered while computing interest on loans. In addition, adjustments have been made to the loans such as disallowing DPC loans, allowing additional loans only to the extent of capitalisation of fixed assets, adjustments for repayment in case of loans disallowed, etc. The Commission would like to spell out that interest on loans has to be allowed on actuals; however, it is presumed that all the loans are raised as per the approved and authorised schemes of capital expenditure and additional loans allowed to the extent capitalization of corresponding fixed assets. On scrutiny of the tranche-wise loans the Commission has disallowed certain loans as mentioned above. The Commission reiterates that the loans have to have a relationship with capital



expenditure and cannot be used for revenue expenditure, therefore the Commission is supposed to check the loans and interest on loans as proposed by the licensee.

Thus, the Commission is of the view that there is no sufficient reason to reconsider the review pleas on this ground.

c. Interest capitalisation

As per MSETCL the Commission has considered interest capitalisation twice while computing interest on loans. As regards interest capitalization, if there were any arithmetic error in computation of the interest expenses on account of the consideration of interest capitalization twice then the same would be taken up while trueing up at the time of ARR Determination for MSETCL for FY 2007-08. The Commission notes the point raised by MSETCL regarding sharing the workings for interest computation, which will be duly shared with MSETCL.

7. DEPRECIATION

7.1. MSETCL's Submission

MSETCL had submitted in its Review Petition that the Commission should have allowed sufficient advance against depreciation to meet the repayment obligations of MSETCL. MSETCL submitted that in case it was disallowed it would result in MSETCL defaulting in its repayment obligations.

As per MSETCL, the correct advance against depreciation allowable in FY 2006-07 was Rs. 92.07 Crore, whereas the Commission had allowed only Rs. 36.89 Crore for FY 2006-07.

Hence, MSETCL requested the Commission to review the advance against depreciation allowed in its Order under the head, "on account of some mistake or error apparent on the face of the record" and under the head, "or for any other sufficient reasons", and allow advance against depreciation for FY 2006-07, as sought by MSETCL in its Petition.

7.2. Commission's Observations and Ruling

a. Depreciation Expenses

The depreciation expenses for FY 2006-07 have been calculated by MSETCL by using the depreciation rates prescribed under the MERC (Terms and Conditions of Tariff) Regulations, 2005. Thus, the depreciation expenditure is projected at Rs. 265.70 Crore in FY 2006-07. The Commission has noted that the depreciation expenditure proposed by MSETCL for FY 2006-07 is in line with the MERC (Terms and Conditions of Tariff) Regulations, 2005 and accordingly has approved in its detailed order, the depreciation as proposed by MSETCL for FY 2006-07.

b. Advance against depreciation

The MERC (Terms and Conditions of Tariff) Regulations, 2005 also provide for Advance Against Depreciation (AAD), in case repayment obligations are higher than the depreciation expenditure computed as per the Schedule prescribed under the Regulations. In its ARR Petition dated 23rd May 2006, MSETCL has stated that the scheme-wise depreciation details



are not available, and hence it is not possible to compute the cumulative depreciation and the cumulative loan repayment as stated in the Commission's Tariff Regulations.

Hence, MSETCL has stated that it has projected the AAD for FY 2006-07 by comparing the depreciation during the year with the loan repayment during the year for FY 2006-07. As the loan repayment is higher, there is a need to provide for AAD, which is computed as the difference between the loan repayment for the year and the depreciation expense for the year, which works out to Rs. 199.37 Crore, as projected by MSETCL.

The Commission has computed the AAD in line with the MERC (Terms and Conditions of Tariff) Regulations, 2005. The AAD is computed on the basis of the loan repayment (which has been recomputed taking into account the loan outstanding as per the Provisional Transfer Scheme as on 31st March 2004 and making adjustments for borrowings, repayment of loans disallowed, etc. for subsequent years) and the depreciation expense for the year. Based on this the Commission has allowed AAD of Rs. 36.89 Crore for FY 2006-07. MSETCL may collect the details of the computation of interest on loans allowed by the Commission for FY 2005-06 and FY 2006-07, from the Commission's office, which will clarify the computation of AAD as allowed by the Commission in its detailed Order.

8. INCOME TAX

8.1. MSETCL's Submission

MSETCL had submitted that, in its ARR and Tariff Petition, it had projected income tax as Rs. 41 Crore and Rs. 42 Crore in FY 2005-06 and FY 2006-07, respectively. The income taxes paid in FY 2005-06 and projected for FY 2006-07 by MSETCL were based on the payment of Minimum Alternate Tax (MAT). Though the Commission had allowed the actual income tax paid in FY 2005-06, it had disallowed the income tax payable in FY 2006-07.

MSETCL submitted that according to MERC (Terms and Conditions of Tariff) Regulations, 2005:

"The Transmission Licensee shall include an estimate of the income-tax liability of his Transmission Business along with the application for determination of tariff, based on the provisions of the Income-Tax Act, 1961:

Provided that any change in such income-tax liability on account of assessment under the Income-tax Act, 1961 shall be dealt with as being on account of uncontrollable factors:

Provided further that any change in such income-tax liability on account of changes in the provisions of the Income-Tax Act, 1961 shall be dealt with as being on account of uncontrollable factors:

Provided further that any change in such income-tax liability on account of change in income of the Transmission Licensee from the approved forecast shall be attributed to the same controllable or uncontrollable factors as have resulted in the change in income and shall be dealt with accordingly."

MSETCL submitted that the above stipulation in the Tariff Regulations clearly show that Income tax has to be allowed as part of the ARR and is to be trued up based on actuals.



MSETCL submitted in its Review Petition that the Commission however had not considered income tax in FY 2006-07; on the basis that income tax had not been paid till date. MSETCL submitted that advance tax was paid in installments during the year, and already for the current financial year an advance tax of Rs. 6.77 Crore had been paid on 14th June 2006. MSETCL submitted the proof of the same as a part of the Review Petition. MSETCL also submitted that at the time of the Order, when the Commission had sought information whether actual income tax had been paid, no income tax was due and was hence not paid, which was reflected in MSETCL's reply to the Commission. MSETCL further submitted that the Commission's decision to disallow income tax on the basis that tax had not actually been paid was incorrect, as no IT was due at that point in time.

MSETCL further submitted that it couldn't be assumed that the losses of erstwhile MSEB would be allowed to be set off against the future profits of MSETCL and other Successor Companies, and hence Income Tax need not be paid. Even if past losses were to be allowed to be set off, MAT would still be payable, and MSETCL had asked for approval of only MAT payment. Incidentally, MSETCL had paid MAT for FY 2005-06 also. MSETCL submitted that therefore MAT would be payable, and the same should be allowed by the Commission.

MSETCL in its Review Petition therefore requested the Commission to review its decision to disallow Income tax for FY 2006-07 in its Order under the head, "*on account of some mistake or error apparent on the face of the record*", and allow Income Tax for FY 2006-07, as sought by MSETCL in its ARR and Tariff Petition.

8.2. Commission's Observations and Ruling

MSETCL being a company under the Companies Act, 1956, will have to compute the book profit as per the provisions of Section 115JB of the Income Tax Act.

According to Section 115JB, the income tax payable on the total income as computed under the Income Tax Act, in respect of any previous year relevant to the assessment year commencing on or after the 1st day of April 2001, is less than seven and one half percent of its book profit (*this rate has been increased to ten percent from financial year commencing on 1 April 2006*), such book profit shall be deemed to be the total income of the company and the tax payable by the company on such total income shall be the amount of income tax at the rate of seven and one half percent (*this rate has been increased to ten percent from financial year commencing on 1 April 2006*).

MAT is computed on the book profit of the company. The book profit of the company would depend on the actual accounts of the company. *Further while computing the book profits, the company (i.e. MSETCL) will be entitled to reduce the lower of book loss and unabsorbed depreciation as per the books of accounts brought forward from earlier years.*

In case of MSETCL, the accounts are not yet finalised and the *exact amount of brought forward book loss and unabsorbed depreciation in the books of MSETCL are also not known*, and the book profit depends on the actual Accounts of the company and not on the ARR numbers as approved by MERC which would be trued up in the subsequent year based on the actual audited accounts. Further, the transfer scheme is provisional and has not yet been finalised as on date. (As per MSETCL submission dated 19.06.2006)



Thus, the Commission is of the view that although MAT may be payable, an accurate estimate of the book profits is not possible at this stage, thus, for the purpose of ARR computation, only the actual tax paid by MSETCL to the Income Tax Authorities has been considered as part of the ARR. (as validated through the challans submitted by MSETCL vide its reply letter No. MSETCL/CP-TRC/ARR/05609 dated 1st June 2006).

MSETCL in its ARR Petition has shown income tax payment of Rs. 41.01 Crore in FY 2005-06 and projection of Rs. 41.99 Crore in FY 2006-07. The Commission has approved the income tax amount for FY 2005-06, as this is based on actual advance tax paid by MSETCL to the Income Tax authorities for the year.

The Commission, in its Order dated 28th June 2006, has advised MSETCL to examine and claim refund of the MAT paid based on actual financials. MSETCL could make a representation to CBDT for claiming carry forward of the unabsorbed losses as per Section 72A of the ITA. Also, the resulting company MSETCL being a company under the Companies Act, 1956, will have to compute its book profits as defined by the explanation under section 115JB and MSETCL could make a representation to the CBDT for availing benefit of claiming exemption from MAT while computing the tax payable as per ITA.

For FY 2006-07, the Commission had not considered income tax as MSETCL had not submitted any proof of payment of advance tax to the tax authorities, for the year till the date of the detailed order (as per the submissions of MSETCL till the date of the Order – 28.6.2006). As mentioned above, an accurate estimate of the book profits is not possible at this stage, and it is not possible to estimate the MAT accurately. Further, as erstwhile MSEB has accumulated financial losses of Rs. 1,872 Crore (as per the MSEB Accounts as on 31st March 2005), the tax losses on account of depreciation and operations would also be significant, and thus, it was considered that there might be no income tax payable in FY 2006-07.

The Commission points out that its Consultants had asked MSETCL to compute its Income Tax liability for FY 2006-07 on the basis of Profit and Loss Account for FY 2006-07, taking into account various provisions of the Income Tax Act, such as accumulated losses, depreciation, interest payment, etc. based on Profit and Loss Account approach vide their email to MSETCL dated 19/06/06, before the release of the detailed order. In response MSETCL replied that the detailed computations have already been submitted vide letter dated 12th May 2006. The Commission also notes that as per the Review Petition of MSETCL, it has paid an Advance Tax installment of Rs. 6.77 Crore as on 14th June 2006, and MSETCL could have already submitted the copy of the Challan towards Advance Tax payment to the Commission when its Consultants made a request for computation of the same vide their email on 19th June 2006, before the release of the detailed Order.

As the Income Tax is statutory payment to be reimbursed on actual payment basis, the actual Income Tax paid to the Tax Authorities for FY 2006-07 will be considered and will be allowed at the time of truing up process in determination of ARR for MSETCL for FY 2007-08.



This Order should be read with the detailed Order of the Commission on determination of ARR for MSETCL (Case No. 49 of 2005) for FY 2005-06 and FY 2006-07, dated 28th June 2006. The Order for FY 2006-07 will be valid till 31st March 2007 and MSETCL is once again directed to submit their Multi Year Tariff Petitions for the first control period commencing from FY 2007-08 onwards by 30th November 2006.

With the above rulings on the points submitted by MSETCL for review, the Commission hereby disposes of the Review Petition.

Sd/-
(S. B. Kulkarni)
Member

Sd/-
(A.Velayutham)
Member

Sd/-
(Dr. Pramod Deo)
Chairman



F
Secretary, MERC

