

MAHARASHTRA ELECTRICITY REGULATORY COMMISSION

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Case No. 8 of 2011

In the matter of

Application of Lanco Infratech Limited for grant of Distribution Licence in the area of supply served by RInfra-D in the State of Maharashtra

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

Lanco Infratech Limited

Registered office:

Lanco House, Plot No. 4,
Software Units Layout, HITEC City,
Madhapur, Hyderabad- 500 081,
Andhra Pradesh, India

....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. LITL filed an application on January 28, 2011, registered as Case 8 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. The prayer set out in the application are as follows:-

“... to consider application of Lanco Infratech Limited for the Grant of Distribution License in the Area of Supply served by RInfra-D in Maharashtra.”

5. The Technical Validation Session (TVS) for LITL’s application was held in the presence of authorised consumer representatives on February 23, 2011 at the Commission’s office. LITL 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 LITL was analysed for data gaps. The data gaps were then communicated to LITL through letter dated April 29, 2011. LITL submitted its response on May 4, 2011. The details of LITL’s application, the identified data gaps and LITL’s response were hosted on the website of LITL on May 10, 2011.

Admission of LITL’s application and Public Notice

6. After holding of Technical Validation Session (TVS), and having examined the data gaps, the Commission admitted LITL’s application for Grant of Distribution Licence on May 5, 2011 and directed LITL 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. LITL 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 (Times of India & Indian Express) and in two (2) daily Marathi newspapers (Lokmat and Maharashtra Times) in the proposed area of supply. A copy of the same was made available on the Commission’s as well as LITL’s websites. LITL invited suggestions and/or objections on its application within thirty (30) days from the date of publication of notice.
8. Subsequently vide letter dated May 30, 2011, LITL revised the proposed area of supply in its application. An addendum to the aforesaid public notice was published by LITL on June 4, 2011 in two (2) daily English newspapers (Times of India and Indian Express)

and in two (2) daily Marathi newspapers (Lokmat and Maharashtra Times) to notify this amendment in its application. A copy of the same was made available on the LITL's website. According to the addendum, LITL 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 LITL 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 LITL

10. In response to the Public Notice published by LITL 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 LITL. 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 clarity regarding name of applicant

The full name of the applicant in the application filed by LITL is of an individual named Shri Sreekumar Majumdar. According to the 2003 Act, the applicant should be a person, where "person" has been defined to include any company or body corporate or association or body of individuals, whether incorporated or not, or artificial juridical person. It is not clear whether LITL intends to be awarded distribution licence in the name of the company "Lanco Infratech Limited" or in the name of an individual "Sreekumar Majumdar".

LITL's response

LITL has clarified that it is seeking the distribution licence in the name of "Lanco Infratech Limited".

Commission's view

The Commission noted LITL's response.

Objection 2: Lack of previous experience in distribution of electricity

Some of the respondents have taken objection to LITL's lack of experience in the business of electricity distribution. Respondents raised concerns over 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.

LITL's response

LITL has responded that as per the 2003 Act and MERC (General Conditions of Distribution Licence) Regulations, 2006, it is eligible for consideration for the grant of distribution licence. Further, it has been submitted that the company is one of the leading power generation companies in the country with an excellent record of accomplishment of project planning, execution and operations. The company is confident of extending its experience in the entire value chain of power sector including distribution to meet the consumers' expectations and provide better value to the consumers. LITL also submitted that its business plan clearly indicates its commitment to provide quality service and reliable power supply on a sustained and competitive basis to all the consumers in Mumbai suburban licence area.

Commission's view

The Commission will need to take the decision, of granting of licence keeping in view the interest of the consumers.

Objection 3: LITL has not met the requirement of minimum area of supply

A few respondents have contended that LITL has failed to revise its application to meet the minimum area of supply criteria as defined in the National Electricity Policy, 2005.

LITL's response

In order to fulfil the criteria of minimum area of supply, LITL has proposed to add the areas of Chene and Varsova of Mira Bhayandar Municipal Corporation area to its proposed area of supply vide its public notice on June 4, 2011 published in Lokmat, Maharashtra Times, Times of India and Indian Express.

Commission's view

LITL has published an addendum to its public notice mentioning the addition of the areas of Chene and Varsova of Mira Bhayandar Municipal Corporation area 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 4: Sales growth assumptions are abnormal

Some respondents have contended that LITL's assumption regarding sales growth of 10% and 11% in FY 2015 and FY 2016 respectively is unreasonable, against a normal 7% to 8% growth rate.

LITL's response

LITL has responded that the sales growth for FY 2015 and FY 2016 is higher because of the additional growth in sales arising out of changes in CRZ and FSI regulations.

Commission's view

The Commission finds the explanation of LITL logical.

Objection 5: Proposed power procurement plan is not satisfactory and it has not considered competitive bidding

Some respondents have objected that LITL has not considered the PPAs of the existing licensee in its power procurement plan. According to them, the Commission's past orders mention that PPAs are assignable to the utility, which takes over the activity of distribution. The objectors have also raised concerns over possible litigation due to such omission by the applicant.

Few other respondents have expressed dissatisfaction about LITL's proposed power procurement plan. They contended that LITL has assumed supply of power from its own generating plants specifying neither the plant nor its location and such procurement was considered without competitive bidding.

LITL's response

LITL has responded that the assignment of PPAs is in the jurisdiction of the Commission and in the event of PPAs being reassigned, appropriate steps shall be taken in the best interest of the consumers.

LITL further submitted that the location and relevant details of its power plants has been mentioned in Table 1, Table 2 and Table 3 of the business plan. The application clearly indicates the optimum power procurement plan based on generation capacities (operational and under construction), and capacities being tied up for Mumbai suburban

licence area, subject to the Commission's approval. The cost of power procurement in the business plan is indicative in nature and if any power is available at a rate lower than that considered in the plan, the same will be taken up for the purpose of supplying to the consumers. Further, LITL will abide by the directions of the Commission for procurement of power for supply to consumers in its area of supply.

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 licensee 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).

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, it will be consumers' interest to stipulate that power procurement by the distribution licensee would have to be done through competitive bidding.

Objection 6: Proposed power procurement plan indicates supply arrangement of existing licensee

RInfra has objected that LITL has considered 500 MW from Dahanu as a source of power procurement, and with certain renewable energy sources in respect of which the existing licensee has already tied up.

LITL's response

LITL denies that its business plan takes into account any power generation from Dahanu project of RInfra. The purchase of renewable energy proposed in LITL's business plan has also not considered any such energy from sources already tied up with RInfra.

Commission's view

The Commission noted that LITL's application does not propose supply of power from Dahanu. Therefore, the Commission does not find any merit in this objection.

Objection 7: Proposed power purchase cost is not satisfactory and there is no reduction in retail tariff

Some respondents have expressed dissatisfaction about the proposed increase in power purchase cost from Rs 4.96/unit in FY 2012 to Rs 6.20/unit in FY 2015. They have expressed dissatisfaction about LITL's failure to propose a substantial reduction in the retail tariff in any of the business plan scenarios. Few respondents have also highlighted that in the option of third parallel licensee, the Average Billing Rate (ABR) is Rs 7.35/unit in FY 2012, which is 8% higher than the current levels of ABR of the existing licensee.

LITL's response

LITL responded that the average power purchase cost should be calculated by factoring the surplus power sale shown for respective years in its revised business plan/submissions. LITL has stated that the ABR highlighted in the objection above is based on certain assumptions applicable to third parallel licensee scenario, and the decision in this regard would be taken by the Commission.

Commission's view

The Commission does not find LITL's response tenable; as sale of surplus power cannot be factored into the calculation of power purchase cost per unit. However, in accordance with the Commission's view expressed in the context of objection 5, it will be in consumers' interest to stipulate that 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, regulated by its Tariff Regulations in a transparent manner. Therefore, in the matter of grant of a distribution licence, this objection is not sustainable.

Objection 8: LITL has assumed acquisition of distribution assets of existing licensee without any supporting document

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

- LITL has not planned properly to give uninterrupted supply to the consumers in the proposed licence area.
- The assumptions made by LITL in its business plan with respect to, transfer of existing licensee's assets by carving them out of the existing licensee, treatment of regulatory assets, treatment of employees are based on the premise that the entire undertaking of the existing licensee would be purchased by LITL. This is contrary to the provision of the 2003 Act.
- Such assumption is against the spirit of Section 14 and 15 of the 2003 Act, under which LITL 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.
- Moreover, LITL has assumed to acquire the assets of existing licensee at net book value when existing licensee has nowhere suggested or hinted the sale of its distribution assets.
- There can be no separation of retail supply and wires licence under the 2003 Act. Therefore, LITL's application that the existing licensee's assets be transferred to LITL at the end of a period of 5 years at nil cost is against Section 14 of the 2003 Act.

LITL's response

LITL submitted that its application fully complies with the requirements of the 2003 Act and the Rules and Regulations made by the Commission under the 2003 Act for the reasons mentioned below. Therefore, the contention that LITL's application does not comply with Section 14 of the 2003 Act is incorrect.

LITL submitted that the contention of the existing licensee, that any prospective applicant is required to apply for a licence on the basis of its own distribution system within an area in which there exists other distribution licensees, is erroneous since it ignores the basic objectives of the 2003 Act which is to promote competition and protect the interest of the consumers. If new applicants are required to set up their own distribution systems in an area in which other distribution licensee(s) exist, then this would entail making huge

investments in setting up a parallel distribution network, resulting in higher costs, and higher tariffs for the consumers as compared to consumers of the incumbent licensee. While empowering the Commission to grant two or more distribution licensees in the same area, the purpose of the sixth proviso to Section 14 could not have been to increase the tariff payable by the consumer. Thus, the sixth proviso to Section 14 must be read as containing an enabling provision that empowers the Commission to grant two or more distribution licences for the same area of supply subject to such conditions as the Commission deems fit.

LITL submitted that the Supreme Court, vide its judgment in Tata Power Company (TPC) Limited vs. Reliance Energy Limited & Ors., (2008) has already operationalized the concept of parallel distribution by utilizing the existing distribution licensee's distribution system. Thus, notwithstanding the fact that in the said case, where TPC had not applied for a new distribution licence for an area in which REL or any other person was an existing licensee, the ratio of the decision in that case is squarely applicable to LITL's application for a licence. The Supreme's Court judgment has resolved the issue of permissibility of use of the existing distribution licensee's network by another supplier in the same area and for this purpose; it is not relevant whether such supplier is an existing licensee or a new licensee.

LITL further submitted that the Commission has already implemented the law declared by the said judgement of the Supreme Court through the order passed on October 15, 2009 in Case 50 of 2009. In that order, it set out the operating procedure for supplying power by Tata Power Company (TPC) to consumers in the area of supply of the existing licensee. In view of the fact that the Commission has already allowed TPC to use the distribution system of the existing licensee viz. RInfra in various parts of suburban Mumbai in order to give effect to the objectives of the 2003 Act, the application of LITL cannot be said to be non compliant with Section 14 of the 2003 Act on the ground that the applicant does not have its own distribution system. In this context, the order passed by the Commission on June 15, 2009 in the Tariff Petition for FY 2009-10 (Case No. 113 of 2008) states that:

“TPC-D will have to meet its licence obligations in its entire licence area, and cannot pick and choose the Wards wherein it will supply electricity. Moreover, incurring heavy capital expenditure for the network roll-out is not the only option available to TPC-D in its efforts to supply electricity to different consumers in its licence area, and the provisions of the EA 2003 relating to Open Access and the provisions of the MERC (General Conditions of Distribution Licence) Regulations, 2006 relating to use of the distribution network of another distribution licensee, need to be explored by TPC-D, so that the cost is optimised. The Honourable Supreme Court also, in its Judgment on the matter of TPC's distribution licence, observed that TPC could supply to consumers in its licence area, by utilising the distribution network of the other distribution licensee already present in the area. Hence, incurrence of capex cannot be a condition for meeting the Licensee's obligations to all the consumers. In

fact, the capital costs should be incurred only when there is no better optimal solution.”

Further, the existing licensee, in its business plan submitted as part of its application for grant of distribution licence (Case No. 65 of 2011), has already admitted that it is obligated to offer non-discriminatory open access on its distribution system to other distribution licensees in the same area of supply for supplying electricity to their consumers.

“Hence, this Business Plan of RInfra-D has been prepared considering only TPC-D and other distribution licensees (if any) to avail open access on the distribution system of RInfra-D for supplying electricity to their consumers. For the purpose of business plan RInfra-D has assumed that it is obligated to offer non-discriminatory Open Access to TPC-D and Other Licensees on payment of wheeling charge and surcharge thereon (cross-subsidy surcharge and additional surcharge) as may be determined by the Hon'ble Commission.”

Therefore, it is not open for the existing licensee to contend that LITL can apply for a licence only on the basis that it will set up its own distribution system in the area served by an existing licensee.

LITL further submitted that the assumptions contained in its business plan for various scenarios have been prepared pursuant to the directions of the Commission as set out in the minutes of the Technical Validation Session dated February 23, 2011. The business plan assumes partial/full takeover of the existing licensee's assets subject to the approval of the Commission, in order to ensure quality service and reliable supply of power on a sustained and competitive basis to all consumers in the Mumbai suburban licence area. The business plans submitted by the other applicants also contain similar assumption regarding asset purchase. LITL submitted that the takeover of assets of existing distribution licensee is not in violation of any provisions of the 2003 Act. It is up to the Commission in its role as a facilitator, as mentioned in the minutes of the meeting dated November 29, 2010, to take an appropriate decision on transfer of the existing licensee's assets with due regard to the overall interest of the consumers.

LITL submitted that the distribution network of the existing licensee is a regulatory asset, which has already been and/or is being paid for by the consumers of its licence area and therefore, if the existing licence is not renewed, the assets of the existing licensee must be transferred to the new licensee.

LITL also submitted that there is no provision in the 2003 Act, which prohibits determination of book value/any other value and subsequent takeover of assets from existing licensee. Under Section 14 read with Section 86(1)(d) of the 2003 Act, the Commission is fully empowered to determine the conditions subject to which assets of the existing distribution licensee would be transferred to a new licensee having due regard to the best interests of the consumers.

Further, LITL responded that given the existing urban nature of Mumbai suburbs, it would be extremely difficult to assess the extent of investment requirement at this stage to establish an independent duplicate distribution network. Creation of such an avoidable asset calls for a high level of investment resulting in increased burden to the consumers. Therefore, in its business plan, LITL has not submitted a separate network rollout plan at this stage since the business plan assumes partial or complete takeover of the existing licensee's assets. It has considered that the assets of the existing licensee be acquired at net book value, subject to the approval of the Commission. However, broad projection of capital expenditure required for network augmentation/expansion has been provided in the business plan. In addition, LITL has mentioned that additional capital expenditure in its business plan primarily caters to the demand growth envisaged in the designated area and investment requirement towards application of advanced technologies shall be considered as per the approval of the Commission. LITL has also submitted that the issue of takeover of the existing licensee's assets, its valuation and wheeling charges, etc. shall have an impact of tariff and expects the Commission to take the appropriate decision on the same in the interest of the consumers.

LITL's application is for a composite electricity distribution asset and not for segregated retail supply licence or wires licence. The business plan scenario considering utilisation of the existing licensee's assets for a temporary period after award of licence has been presented based on the direction of the Commission as per the minutes of the Technical Validation Session dated February 23, 2011.

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 licensee 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 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 and to the extent relevant to the contention raised by LITL, 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 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 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. Hence, the ratio of the 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. An opportunity has been given to all the applicants to give their views in the matter.

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

Moreover, the Commission views that LITL's reference to the Commission's order dated October 15, 2009 in Case 50 of 2009 and order dated June 15, 2009 in the Tariff Petition for FY 2009-10 (Case No. 113 of 2008), is to be read with the Hon'ble Supreme Court's judgment in the case of Tata Power Co. Ltd vs. Reliance Energy Ltd., *Supra*, where, the ratio of the Hon'ble Supreme Court judgment is specific to the facts of the case, and hence the Commission's order dated October 15, 2009 in Case 50 of 2009 and Order dated June 15, 2009 in the Tariff Petition for FY 2009-10 (Case No. 113 of 2008), is also confined to the case of Tata Power Co. Ltd Reliance Energy Ltd (now renamed as RInfra). As regards the business plan submitted by RInfra stating therein that it is obligated to offer non-discriminatory open access on its distribution system to other distribution licensees in the same area of supply for supplying electricity to their consumers, such a position is not applicable to the present applicant in view of the provisions of law discussed above.

The Commission also notes that LITL's interpretation about the Commission's view regarding asset transfer is not fully correct.

Objection 9: Duplication of network will lead to wastage of resources

Some respondents have objected that if the licence is awarded to a new player, it will be against the principle of economical use of resources as stated in the 2003 Act, and would eventually lead to national waste. It would also result in additional burden in the form of higher tariffs for the consumers. Some respondents have also submitted that LITL's proposal to incur capital expenditure to implement advanced technologies such as SAP, GIS, AMR, etc. is tantamount to reinventing the wheel, which have already been implemented by the existing licensee, resulting in higher tariff for Mumbai consumers.

LITL's response

LITL has responded that it recognizes that duplication of network calls for high level of investment resulting in increased burden to the consumers. Accordingly, in its business plan, LITL has proposed that existing licensee's assets be acquired at net book value, subject to approval of the Commission. LITL has also mentioned that additional capital expenditure in its business plan primarily caters to the demand growth envisaged in the designated area and investment requirement towards application of advanced technologies shall be considered as per the approval of the Commission.

Commission's view

For the reasons stated in the preceding objection, the submissions are not sustained. For avoiding prolixity, the same reasons are not reiterated.

Objection 10: LITL has ignored the impact of TPC being a parallel licensee in the area

Some respondents have contended that LITL has not considered the impact due to existence of Tata Power Company (TPC) as a parallel licensee in the Mumbai suburban area.

LITL's response

In its response to the above objection, LITL has submitted that the impact of TPC as a licensee in the designated area has been considered in the business plan.

Commission's view

The Commission is of the opinion that the presence of TPC as another licensee in the same area of supply does not affect the eligibility of LITL for grant of Distribution Licensee.

Objection 11: LITL has not adhered to MYT Regulations

Some respondents have contended that LITL has not adhered to the latest MYT regulations in its business plan.

LITL's response

LITL has reiterated that its calculation of each component in the business plan is based on the new Tariff Regulations considering assumptions relating to the business.

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, the assumptions have effects on retail tariff, which the Commission deals with through a separate process under the provisions of its Tariff Regulations. Therefore, the Commission believes that such assumptions by LITL, 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 12: Increase in cost due to increased power generation

Some respondents objected that since LITL is one of the leading independent power producers in the country with existing capacity of 3,292 MW and plans to increase this capacity to 15,000 MW by 2015, this increased power generation is going to result in high cost.

LITL's response

LITL has responded that an increase in power generation capacity by an entity does not necessarily increase the cost of electricity supply.

Commission's view

The objector has not explained as to how the objection raised could be a ground either for disqualifying an applicant from the grant of distribution licence or from supporting the application for the grant of distribution licence. As such, the objection raised has no substance.

Objection 13: Data gaps in LITL's application

An authorised consumer representative and an existing licensee objected that the preliminary data gaps found on May 4, 2011 have not been replied to, in respect of the following:

- Details relating to roll-out of distribution network and funding of the same, which will determine whether LITL 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

LITL's response

LITL responded that it has indicated availability of adequate resources to ensure requisite level of equity investment via its submission of Additional/Missing Information dated May 30, 2011 to the Commission. LITL has submitted the last three years' balance sheet as part of its application. LITL has also submitted the actual data for the top 5 projects via its submission of Additional/Missing Information dated May 30, 2011 to the Commission.

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.

The Commission noted LITL's response in relation to top 5 projects. In relation to details of roll-out of distribution network, the Commission's observations and views are expressed in Para 43 through 51.

Salient features of LITL's application

11. The salient features of LITL'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	LITL has provided all the basic details as specified in this section of the application. Primary contact details, registered office details, registration number, date of incorporation and registration are provided.
Part A: 7	Name and addresses of the	LITL has provided details of the Board of

Part/Section	Description	Details provided
(c)	Board of Directors	Directors and promoters in Annexure – A of its application
Part A: 7 (c)	Ownership/Shareholding pattern	LITL has provided the shareholding pattern in Annexure-A of its application. According to the Annexure, the promoter group holds 67.94% of the total shares; institutional investors hold 24.33% of the share and 7.72% is held by non-institutional investors. 16.24% of the promoters' shares have been pledged as on March 31, 2011. The largest shareholder is LITL Group Limited, which hold 3.6% of the shares.
Part B: 1	Memorandum and Articles of Association (in case of a company) as in force on the date of application	LITL has provided a copy of the Memorandum of Association & Articles of Association in Annexure – B 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 functions) a) Senior Executive Management (along with curriculum vitae);	LITL has provided the Organizational chart which is attached in Annexure-C of the application form. LITL has submitted all the necessary information with respect to the management details in Annexure-C of its application.
Part B: 2b	b) Board of Directors (along with curriculum vitae);	LITL has submitted that it has 10 Directors on the Board. The details of the Board of Directors are attached along with the application form in Annexure-C.
Part B: 2c	Number of middle/lower management personnel	Middle/Lower management personnel: 6,046 Regular Employees: 4,642 Trainees: 386 Consultants: 48 Project Specific: 970
Part B: 2d	Relationship (including intending relationship, where applicable between the Applicant and key to the application for grant of Licence.	LITL stated that it would undertake EPC work and construction services through its EPC and Construction Divisions respectively.
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 given. The copy of import licence has also been attached in the application.

Part/Section	Description	Details provided
Part B: 5	Bank references asserting that the Applicant is financially solvent	Bank of Maharashtra has provided the Solvency Certificate (AV-52/Adv./2010-11) declaring that Lanco Infratech Ltd. is solvent to the extent of Rs 3,166.00 crore as per Audited balance sheet as of 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).	LITL has provided its Annual Reports for the financial years FY08-FY10. The same are attached in Annexure-D.
Part B: 7	Any other documentary evidence to substantiate the financial capabilities, technical competence and others.	LITL has attached in Annexure-E its financial turnover for the last seven years, an auditor's certificate (from Brahmayya & Co.) stating the Networth of the company as Rs 3,156.35 crore as on March 31, 2010 as per the audited financial statements, a company brochure highlighting its competencies in Power, Non-Power Infrastructure, Construction & EPC, Renewable, Property Development, along with details of major projects executed as well as projects on hand.
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 lines, and the area to which the application for Licence relates.	<p>LITL 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. The data gap was highlighted to the applicant. LITL, in response to this, submitted that it proposed to acquire the existing licensee's assets at book value, subject to the decision of the Commission. In the absence of detailed information of the existing system, LITL has stated that the broad projection of capital investment has been submitted as part of the business plan and the consequent to the grant of licence, detailed information would be submitted.</p> <p>Further, LITL revised its proposed area of supply on May 30, 2011 to include the following additional areas a) Chene Village; and b) Varsova Village, in order to fulfil the minimum area of supply criteria as laid down in the National Electricity Policy and the Distribution of Electricity Licence (Additional requirements of</p>

Part/Section	Description	Details provided
		Capital adequacy, Creditworthiness, and Code of conduct) Rules, 2005.
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.	LITL did not submit the detailed electrical distribution map as part of the original application on December 6, 2010. The data gap was highlighted to the applicant. LITL, in response to this, has provided a geographical map showing the proposed licence area spread across 384 sq. kms of Mumbai suburbs, as provided in the "Information for bidders". LITL has also stated that information w.r.t list of the whole or any part of any cantonment, aerodrome, fortress, etc. in the occupation of Government for defence purposes located within the proposed area of supply, names of streets or parts of streets which are repairable by a person other than Central Government, State Government or local authority, etc. for which applicant has obtained authorization to undertake works, list of all local authorities vested with administration of any portion of the area of distribution shall be submitted subsequent to the grant of licence.
Part B: 10	Business plan details	LITL submitted its revised business plan on April 16, 2011, after taking into consideration the scenarios discussed during the TVS and the meeting held on April 7, 2011 about minimum area of supply. LITL was asked to submit a revised business plan subsequent to addition of Chene and Varsova villages in the proposed area of supply. However, LITL responded that the additional capital investment requirement for the new area could be accommodated within the provision of the business plan already submitted.
Part B: 12	Supporting information on compliance with the additional requirements prescribed by the Central Government, as may be applicable.	LITL had provided a statutory auditor's certificate from Brahmayya & Co. to certifying compliance with the additional requirements prescribed by the Central Government as part of its original application submitted on December 6, 2010. LITL was subsequently asked to submit the certificate duly signed by the authorized Company Secretary, under

Part/Section	Description	Details provided
		affidavit. LITL then submitted the revised certificate on June 25, 2011.
Part C	Format for assessing competence of applicant	LITL submitted its previous experience (past 5 years for Related Business) and information on Appropriate Expertise (Personnel) as part of Annexure G and H of its original application. However, this information was not in the format prescribed in the MERC (General Conditions of Distribution Licence) Regulation, 2006. Further, LITL had not provided information in Part C-2 on Details of Proposed Project (Business for which Licence is sought) and Part C-4 on Revenue Potential (Business for which licence is sought). The data gaps were highlighted to LITL. Accordingly, LITL submitted the complete information in Part C-4 on April 29, 2011 and in Part C-2 on May 30, 2011.

Evaluation of LITL’s eligibility for grant of Distribution Licence

12. On the date of expiry of the present licence of RInfra, another Licensee viz., the 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. 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 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, 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 LITL’s eligibility for grant of the distribution licence on the basis of the framework described above, and various information provided in LITL’s application and other submissions made by LITL from time to time. Accordingly, the Commission used the following criteria to determine LITL’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, LITL sought a licence to distribute electricity in and around suburbs of Mumbai. However, subsequently, LITL 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.

LITL 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, LITL 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 LITL 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, LITL 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 that such ability is to be assessed based on the Networth and Internal Resource Generation of 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, the 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, LITL 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 was 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. LITL 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. LITL vide its letter dated June 20, 2011, submitted the computation of Networth and Internal Resource Generation for the company on a standalone basis as per audited financial statements, which is shown below.

Table 1 : LITL - Networth and IRG on a standalone basis

(Rs. crore)	FY 2008-09	FY 2009-10	FY 2010-11
Networth	1,857.2	3,156.3	3,435.1
IRG	56.7	-718.4	1,900.4

29. The Networth as on March 31, 2011 is Rs. 3,435.1 crore, which is the maximum in the preceding 3 years. The maximum IRG over the last 3 years was Rs. 1,900.4 crore in FY 2010-11. LITL had negative IRG in FY 2009-10.
30. To assess whether LITL has committed investments tied up in other projects, LITL 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. LITL 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 27,535 crore. Out of which, Rs 21,762 crore represents sanctioned debt. Therefore, the committed investments to be financed through equity amounts to Rs 5,773 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. 1,501 crore.
31. Therefore, according to the test determined by the Commission, the Networth, adjusted for the committed equity investments elsewhere, is computed to be Rs.1,934 crore. However, LITL 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. 1,934 crore) is greater than the equity requirement (Rs. 362 crore). Therefore, the Commission is of the opinion that LITL 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.8,001 crore. LITL 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. 8,001 crore) is greater than the equity requirement (Rs. 362 crore). Hence, LITL satisfies the IRG criteria.
33. Therefore, LITL 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, a discussion 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) requires 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, LITL was asked to submit the latest available Credit Rating report. The Credit Rating report provides a credit rating, which represents the rating agency's opinion on the likelihood of a rated debt obligation being met in full and on time. 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 repayments record 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 LITL. Thus, based on the solvency certificate and credit rating report submitted, the Creditworthiness of LITL was assessed.

36. LITL in its application dated December 6, 2010 provided a solvency certificate from Bank of Maharashtra. Bank of Maharashtra, in the solvency certificate has mentioned that Lanco Infratech Limited to be solvent to the extent of Rs. 3,166 crore. Bank of Maharashtra was contacted to verify the authenticity of the certificate. No response has been received from the Bank of Maharashtra regarding the same.
37. In response to the Commission's letter dated May 25, 2011, LITL submitted its credit rating report on May 30, 2011. CRISIL issued a credit rating report, in which, the long term debt instruments, Rs. 12 Billion cash credit, Rs. 17.7 Billion Term Loan were rated A-, the short term debt instruments, including Rs. 15.85 Billion Letter of Credit/Bank Guarantee, Rs. 15.40 Billion Bank Guarantee, and Rs. 4.5 Billion Letter of Credit were rated P2+. As per CRISIL, instruments rated 'A' are judged to offer an adequate degree of safety, with regard to timely payment of financial obligations. However, changes in circumstances can adversely affect such issues more than those in the higher rating categories. A short-term rating of P2 indicates that the degree of safety regarding timely payment on the instrument is strong.
38. The debt requirement of LITL 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 Bank of Maharashtra, LITL can be treated as solvent to the extent of Rs. 3,166 crore. Based on the credit rating report and solvency certificate, the Commission is satisfied that LITL 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, the LITL 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. LITL, in its original application dated December 6, 2010, had submitted a statutory auditor's certificate 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. However, this declaration needed to be certified by the Company Secretary of Lanco Infratech Ltd. The Commission, vide email dated May 27, 2011 had directed LITL to submit a declaration, as required under the said Rules. LITL, in reply to the email, submitted the said declaration to the Commission on June 25, 2011.

41. Based on the information submitted by LITL, the Commission is satisfied that LITL 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.

LITL's Network Rollout Plan

43. LITL 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. However, LITL did not submit a network roll-out plan as part of the business plan. The applicant was asked to submit a roll-out plan for the complete distribution network over the proposed area of supply vide letter dated May 25, 2011. It was also asked to submit a geographical roll-out plan for the same. LITL, in its response, has submitted that it would be difficult to assess the extent of investment requirement to establish its own 'duplicate' network. The applicant has also submitted that creation of an independent distribution network would be an 'avoidable' asset because it would result in additional burden on the consumers in the form of higher tariffs. LITL has clarified that the business plan submitted does not cater to the requirement to invest and establish its own distribution network but has preferred that the existing licensee's assets be acquired at net book value. In addition, it has made a separate provision in the business plan to cater to the future growth in the proposed licence area. However, in the matter of purchasing the existing licensee's assets, as proposed in the business plan, LITL has not produced a firm substantiation in the form of a mutual agreement reached between the concerned entities.
44. It is clear from LITL's submissions that it does not intend 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 6th 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 un-remunerative 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 6th proviso to Section 14.
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) 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. LITL 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. It has admittedly not submitted a separate network rollout plan since its business plan assumes partial or complete takeover of the existing licensee's assets. LITL has submitted that it would be difficult to assess the extent of investment requirement to establish its own 'duplicate' network. LITL has also deemed the creation of an independent distribution network as an 'avoidable' asset because it would result in additional burden on the consumers in the form of higher tariffs. LITL has clarified that the business plan submitted does not cater to the requirement of investing and establishing an independent distribution network but has preferred that the existing licensee's assets be acquired at net book value. However, in the matter of purchasing the existing licensee's assets, as proposed in the business plan, LITL has not produced a firm substantiation in the form of a mutual agreement reached between the concerned entities. The Commission is of the view that such a stipulation on the part of LITL is contrary to the Sixth Proviso to Section 14 of the 2003 Act. For these reasons, LITL's contentions are not sustained in law. Therefore, the Commission found that LITL'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 LITL'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, LITL'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 LITL'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 LITL from time to time, the Commission assessed LITL's application for its
- Power Procurement Plan (S1); and
 - Management and Technical Expertise (S2)

Power Procurement Plan (S1)

LITL's power procurement plan considered availability of power from own generating stations and the progressive availability of power from its generating capacity currently under various stages of commissioning. It submitted that various projects are under construction or development by the company, totalling to a generating capacity of 8,430 MW. These included coal based, gas based, wind, solar and hydro projects.

The projection of power procurement from various generating stations was done on the basis of the following assumptions

- Interstate transmission losses currently applicable considered without any escalation
- Intrastate transmission losses considered as approved by the Commission, without any escalation
- Power purchase quantum under RPO has been considered as per MERC regulations
- Any shortfall in quantum of power required to be met through bilateral purchase

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

Particulars	FY12	FY13	FY14	FY15	FY16
Sales (MUs)	8,013	8,584	9,225	10,162	11,319
Distribution Loss (%)	9.83%	9.58%	9.33%	9.18%	9.08%
Energy input to the Distribution System (MUs)	8,948	9,552	10,229	11,243	12,505

LITL submitted that the above demand will be met through own generating capacity and bilateral power purchase which is required only in FY 2011-12 and FY 2012-13. It submitted that beyond FY 2012-13, its own generation capacity will be sufficient to meet the projected energy requirement.

Power from the following generating stations has been considered for long term procurement through power purchase agreements:

Name of Plant	Plant Capacity Allocation (MW)	Status of Plant	Years for which Power availability is considered
Generator 1 (Gas based)	293	Operational	FY 2011-12 to FY 2015-16
Generator 2 (Gas based)	594	To be commissioned in combined cycle mode in FY 2013-14	FY 2013-14 to FY 2015-16
Generator 3 (Coal based)	660	To be commissioned in FY 2013-14	FY 2013-14 to FY 2015-16
Generator 4 (Coal based)	594	To be commissioned in FY 2014-15	FY 2014-15 to FY 2015-16

LITL submitted that it determined the power purchase cost on the basis of the following assumptions:

- Interstate transmission charges currently applicable have been considered without any escalation

- Intrastate transmission charges as approved by the Commission have been considered without any escalation

Power purchase cost was summarised as below:

Particulars	FY12	FY13	FY14	FY15	FY16
Power Purchase Cost (Rs cr)	4,441.1	4,779.0	5,089.2	6,969.1	7,241.3
Energy Input (MUs)	8,948	9,552	10,229	11,243	12,505
Power Purchase cost per unit (Rs/kWh)	4.97	5.00	4.98	6.20	5.79

However, LITL further submitted that the power purchase costs considered in the business plan are indicative in nature, subject to the following:

- Pricing mechanism to be considered by the Commission for the power purchased from own generating stations.
- Uncertainty in policy for fuel allocation.
- Uncertainty on the future prices for procurement of power under short term bilateral route.
- Interstate transmission prices finalization as per CERC Regulations, 2010.

Management and Technical Expertise (S2)

From the information provided in the application, following can be summarised about LITL's application.

Expertise of key personnel

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

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

LITL has managed over 5,000 employees over the last 3 years through their various lines of businesses such as power, EPC and infrastructure. However, the company does not have prior experience in handling customers at a retail level.

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

LITL submitted that it has presence across the value chain of the power business, namely, generation, transmission and distribution projects. It owns and operates several generating plants across the country, and has experience in development of transmission

infrastructure and distribution infrastructure for several transmission and distribution companies in India.

Generation: LITL submitted it is one of the largest Independent Power Producers in the country with a generating capacity of 3,292 MW, with another 5,953 MW of projects under various stages of construction and 4,470 MW of projects under development.

Transmission: LITL submitted that it has been involved in construction of transmission lines for its own power plants as well as for other clients such as Transmission Corporation of Andhra Pradesh Ltd (APTRANSCO), Power Grid Corporation of India Ltd (PGCIL), Gujarat Energy Transmission Corporation Ltd (GETCO) and Rajasthan Rajya Vidyut Prasaran Nigam Ltd (RRVPL).

Distribution: LITL submitted that it has worked on several distribution projects including erection of 33/11 kV substations and 33 kV and 11 kV lines for clients such as Central Power Distribution Company of Andhra Pradesh Ltd (APCPDL) and NTPC . LITL has also been involved in turnkey contracts for supply, construction, erection, testing and commissioning of sub-transmission lines, distribution lines, renovation works for Maharashtra State Electricity Distribution Company Ltd (MSEDCL).

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

LITL, has highlighted the initiatives taken by it in the last few years in various areas such as conventional power generation, EPC and renewable energy.

The EPC division of the company has adopted the latest technological developments and best practices in the industry. In generation, the company has set up two combined cycle power plants at Vijaywada, which are running successfully. The company has also moved towards use of super-critical boilers from sub-critical boilers, with multiple projects under execution. Moreover, the company has adopted Modern Plasma Ignition for boilers for reliable, economical and low-load combustion stabilization. The EPC division of the company has also established ties with various global manufacturers for sourcing of equipment.

LITL submitted that it has forayed into power generation from solar energy and hydro energy. It has commissioned a 5 MW PV power plant in Gujarat, and another 110 MW PV plant is in the pipeline. It is developing a 100 MW solar thermal power plant, and providing EPC services for another 100 MW plant. LITL is also setting up a 1,500 MTPA solar wafer/Polysilicon manufacturing plant at Chhattisgarh using highly advanced technologies.

54. Since, the Commission found that LITL'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 LITL 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 LITL for grant of licence after explaining the grounds, as described in the preceding Para 44 to Para 51.
56. During the hearing, LITL submitted that given the time constraints, it was practically not possible to assess the capital investment requirement to duplicate the network in the proposed area of supply. LITL submitted that a vast technical study needs to be conducted to assess the investment requirement and the cost economics. LITL also cited the Hon'ble Supreme Court Judgement in the case of Tata Power Company Limited vs. Reliance Energy Limited & Ors., (2008), and stated that its application be considered in the interest of consumers and promoting competition in the sector.
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 LITL 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 LITL, the Commission is of the view that LITL's application does not conform to aspects relevant to grant of distribution licence, on account of lack of 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.
59. Therefore, the application filed by LITL is rejected as it does not conform to the provisions of the 2003 Act as discussed above. However, the statute enables the making of application for grant of 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 Lanco Infratech Limited for grant of Distribution Licence in and around suburbs of Mumbai in Case No. 8 of 2011 stands dismissed. Liberty is granted to apply afresh for grant of licence keeping in view the statutory requirements of eligibility.

Sd/-
Vijay L. Sonavane
(Member)

Sd/-
V. P. Raja
(Chairman)