More Power to Efficient Reforms

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The proposed changes to the National Tariff Policy (NTP) for the power sector, along with the long-awaited Draft Electricity (Amendment) Bill, 2020, will bring critical and structural changes to the existing Electricity Act, 2003. The proposed reforms should also be viewed under the larger umbrella of the Atmanirbhar Bharat Abhiyan (ABA).

Key changes proposed include the creation of an Electricity Contract Enforcement Authority (ECEA), reduction of cross-subsidies and separating state subsidies from tariff by introducing direct benefit transfers (DBT) to beneficiaries, and round-the-clock supply of power through standards of performance (SOP). Also included are simplification of tariff categories and rationalisation of retail tariff, and better compliance of renewable power-purchase obligation (RPO) including hydropower by creating distribution sub-licensees and franchisee.

The structure of distribution companies (discoms) and tariffs built over the last several decades is complex. At the very core of this maze is an unsustainable tariff structure. Power being a concurrent subject, the roles of GoI and state governments are often at loggerheads. Simply put, there is no uniform tariff structure for the whole country. For example, power supplied to agriculture and household consumers are heavily subsidised by commercial and industrial consumers.

This high cost of power (and of logistics) has made the Indian industrial and commercial sector far less competitive compared to countries like China and those in Southeast Asia. The subsidy-driven tariff structure has also led to a massive payment backlog owed by state discoms to power producers (generating companies, or gencos) that now stands in excess of ₹93,000 crore.

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Grid expectations

To correct this anomaly, the current round of reforms mandates that cross-subsidies cannot exceed about 20%. In other words, the tariff gap of an average cost of supply and average billing rate for residential, agricultural, industrial and commercial consumers cannot be more than about 20%.

The new rules also mandate that subsidies, if any, be paid directly by state governments to the consumer through DBT. This will ensure that the subsidy money reaches directly to the beneficiary, and doesn't result in any loss due to the inefficiency of state discoms. Along with the introduction of smart meters, this will help state discoms improve their collections. Better collection or lower aggregate technical and commercial (AT&C) losses will help get discoms more investment. One can expect the financial health of the state discoms to start improving considerably, provided they start operating themselves on commercial lines.

The new set of reforms also seek to improve the operational and financial performance of discoms through the introduction of new standards of performance that empower the regulator to levy a financial penalty for underperformance. Further, the new rules also mandate that AT&C losses in excess of 15% cannot be passed on to consumers, which will force discoms to operate their businesses more efficiently.

Over the last four years, India has made considerable progress in its attempts to migrate to clean energy sources. We have even managed to find price parity between electricity produced by thermal and renewable energy sources, an objective that had eluded us for long. However, India has been falling behind in achieving the 175 GW clean energy target set for 2022. With less than two years from the target, we have barely managed to cross the halfway mark.

To this end, the draft amendments also include a new National Renewable Energy Policy that, among other things, seeks to enforce better compliance to RPO. Under this framework, a minimum percentage of the purchase of electricity from RPO and hydro sources of energy will be prescribed in consultation with state governments and GoI. This move will also help improve investor confidence in the renewable energy sector.

The new GoI initiative to privatise distribution of electricity for eight Union territories will be a precursor to many more privatisation opportunities of discoms by other states too. The overarching objective of the proposed reforms acknowledges the role of an efficient and economically sustainable power sector needed to bring the country back into a double-digit growth path.

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