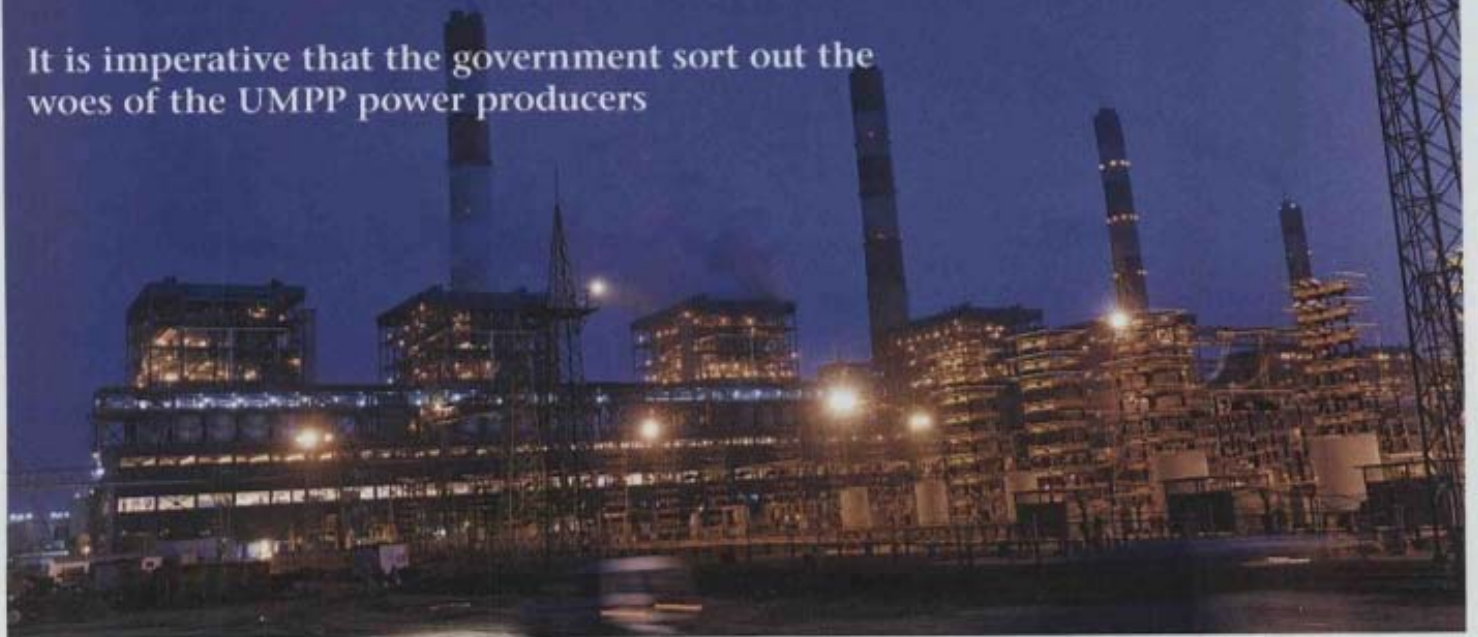


Playing the power game

It is imperative that the government sort out the woes of the UMPP power producers



SANJAY BORADE

Tata Power's offer to sell 51 per cent equity stake in its 4,000 MW power plant at Mundra, operated by its subsidiary, Coastal Gujarat Power Ltd, at a price of ₹1, last fortnight, raised many eyebrows. The offer for sale was made to the state utility company, with letters sent to the power ministry. It was made apparently at the behest of the lenders, which included PSU banks, as a tactical move. It will also help the company to pare a part of the accumulated debt which, according to the last audited balance sheet of CGPL for 2015-16, was ₹12,107 crore. Along with the equity stake, a proportionate amount of debt would also be transferred to the procurers (including Gujarat Urja Vikas Nikam and state power utilities in Rajasthan, Haryana, Punjab and Madhya Pradesh). Half of the debt is foreign currency loans, while the balance is domestic loans, which includes ₹3,200 crore given by Tata Power.

CGPL has offered to remain as part owners of 49 per cent and continue to operate the plant as before. With procurers (power purchasers) in the driver's seat, CGPL would be able to operate the plants for the full life of the plant, estimated at 40 years, as

against the current PPA for 25 years, since 2012, and continue to get power at competitive rates.

Along with Tatas, Essar Power and Adani Power had also made similar moves. In the case of Adani Power, the company proposed to transfer its power plant at Mundra into a 100 per cent subsidiary, which would subsequently be offered to the procurers of power, again comprising various state power utilities. Essar Power also wrote a letter to the lenders and Gujarat seeking a long-term solution to the problem.

The immediate cause of the move was by the stoppage of loans by lenders, as the power plants, based on imported fuel, were hemorrhaging and losses were going up steadily. "There was under recovery in the cost of fuel since the last five years," points out Anil Sardana, CEO & MD, Tata Power, a veteran in the industry, having worked in several companies including NTPC and BSES (now Reliance Infrastructure of ADAG), before joining Tatas. The lenders' support had waned, following the Supreme Court's judgment disallowing the tariff revision petition filed by Tata Power and Adani Power. It held that the changes arising in the price

of coal imported from Indonesia, following the changes made by the Indonesian government cannot be construed as a *force majeure* in India.

In a judgment delivered by the full bench of the Supreme Court, it was held that the power purchase agreements inked by the power generators with the state electricity procuring companies did not have any provision for meeting such an eventuality, which related to a change in the law by a foreign country. Overruling an earlier order of the Central Electricity Regulatory Commission, which had passed an order in 2014 providing for compensatory tariff to offset additional costs, till hardships continued, the Supreme Court held that the commission has no regulatory powers to modify tariffs or grant compensatory tariff. The court also remarked that the arrangement for fuel is the obligation of the petitioners (Tatas and Adanis), who are free to procure it from anywhere in the world.

Changes in Indonesian laws

The genesis of the problem lay far from the shores of India. The ultra mega power plant (UMPP), envisaged by the government in early 2000 and given on the basis of the

lowest bidder, envisaged the usage of imported coal in the plants. In 2006, the letter of intent was received by Tatas, which had made a bid based on a levelised tariff of ₹2.26 per kWh. A PPA was inked with Gujarat Vikas Nikam and other procurers in April 2007. GVN had contracted to take 1,805 MW, Punjab 475 MW, with others taking the balance. Some 200 MW was initially kept for merchant sale.

Tatas and Adanis had both tied up with Indonesian companies to procure coal from that country. Essar had also made arrangements for bringing coal from Indonesia. The rationale was that Indonesian coal with high calorific content was the best available and the transport cost was lower than procuring coal of equal quality from Australia or South Africa. Tatas and Adanis also bought stakes in companies in Indonesia. Tatas in April 2007 also inked an agreement with an Indonesian coal company to take a 30 per cent stake for \$1.1 billion (about ₹4,950 crore) to ensure a regular supply of coal.

Tata Power also inked an agreement with a company, Indo-Coal Resource (Cayman Islands) for ensuring yearly supply of 10.11 million tonnes of coal in 2007. Arrangements were also made with a shipping and logistic company, which were for lifting and transporting the coal to India through its own fleet of ships purchased by Tatas. The landed price of coal at that time was under \$50 per tonne. Adani, as the biggest trader in coal, could source coal from virtually any country across the globe.

Everything went according to plan, with equipment for the 800x5 super critical power plants ensuring the highest efficiency ordered from Japan and Korea; and the project execution was also ahead of schedule. During March 2012-January 2013, a record was created, with all five units being commissioned within a year.

The twist in the tale however, was the decision taken by the Indonesian government. In September 2011, it mandated that all coal in the country would be sold at an import-parity price. With China and India both importing huge quantities of coal,



Sardana: gung ho

volatility increased, with prices moving up to three digit levels, leaving power generators in a tizzy. Appeals to CERC and thereafter to the appellate tribunal were filed, seeking compensatory pricing to ensure recovery of this sudden rise in the prices.

A clause in the agreement had mandated that 45 per cent of the fuel energy component was escalable with 55 per cent non-escalable. The escalable portion was also determined on the basis of the CERC Escalable Index, which in turn was based on import-parity prices of coal in India over the previous 12-year period. Given the relative stability of the prices of coal during the earlier period, a 3.46 per cent per annum price was built in the PPA contract.

Post the increase in Indonesian coal prices, and the huge demand for coal, the price increase during 2007-12 was in the vicinity of almost 150 per cent, as against 17 per cent, which one would have got under the PPA.

The regulators did provide some relief by allowing an increase in the compensatory tariff. However, a decision to provide for past losses of two years was held in abeyance. The procurers, however, felt that it was a water-

tight contract and the power producers were obliged to supply power at the rate contracted, come what may. Their rationale was that allowing them to increase the rates would in turn force them to increase the rates to the consumers and it would be politically detrimental to hike rates. This forced them to fight the case against the regulators' decision to provide a compensatory tariff hike.

Stalemate

As a result of the resultant stalemate after the Supreme Court's order in April 2017, the management of all companies, along with the lenders, came to the conclusion that the procurers should be given an equity stake in the respective companies. "The assets are fantastic and the plants are the most efficient ones in the country," points out Sardana, who feels it is the best possible solution in the given scenario. By allowing the procurers a majority stake, they can easily tweak the contracts and run the assets for a period of 40 years, as against the remaining 20 years in the current scenario.

Sardana is of the opinion that another 800 MW power plant could be installed by the procurers in the

same premises at a fraction of the costs. This will enable them to get more power and also recover the fixed cost, which works out to 90 paise per unit, a little faster (once the new power plant goes on stream). The new plant could also be designed to run wholly/ partially on domestic coal or blended coal.

The problem of running on domestic coal or even having more than 30 per cent domestic blend could result in lowering the efficiency of the existing units considerably. NTPC, one of the Indian producers, who could be roped in by the distribution company, has reportedly claimed that it can run on blended coal. Tatas did run it at a time when the prices of imported coal had shot up to about \$120 per tonne.

But, why are the power generators asking for relief at this point in time – especially when the price of imported coal has dropped significantly? In fact, CGPL had reported a maiden profit of ₹2,014 crore. This was largely due to the impairment reversal of ₹2,320 crore made in earlier years. While this was a book entry, a reassessment of the value of the assets by the management, stated that following “the sustained low prices of coal over the last one year and forecast of their continuance at substantially lower prices than have prevailed in the last few years, the management has reviewed and reassessed the value of the assets at Mundra.” The reports were of course prepared before the Supreme Court’s judgment.

Sardana reiterates that the plants are in good condition and no impairment is required. He, however, feels that, even at the current landed price of coal (\$75 at site), under recovery of costs, there is a provision for increase in tariff. “At current coal prices total tariff earned can only meet fuel cost, without leaving any margin to cover the fixed costs and debt servicing.” Swapnil Jain, chief financial officer, Essar Power, points out that, since commissioning, “Essar has made a principal payment of ₹1,270 crore and an interest servicing of ₹2,100 crore, though the EBIDTA levels have been lower during this period.” The



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landed imported coal, on a calorific value works out cheaper than the domestic coal even today.

Price hike inevitable

Everyone – the lenders, power producers and in some case even some SEBs – is of the view that a price hike is inevitable. But against this is the fact that the prices were arrived at through open bidding and PPAs have been signed. Several SEBs are also refusing to pay higher prices, wishing to bind the promoter to the signed contracts. For a new plant, power generation would cost ₹3.50-4.00 per unit, claim experts. Getting power by allowing some increase to cover the bare minimum cost of fuel and servicing could allow SEBs or procurers to get sustained power at a marginally higher cost. The high ground, that a contract once inked cannot be renegotiated, is impractical.

Energy minister Piyush Goyal claims that the Centre can only act as a facilitator, as the renegotiation can only be done by the two parties – SEBs and the power producers. While the bankers are keen to get the imbroglia sorted out and push power producers to offer a generous stake in the existing projects, to ensure viability, SEBs are not budging. The main reason is the fear of being hauled up, many

years later by the vigilance authorities or worse by the CBI on grounds of playing into the hands of the industrialists. The Centre’s apparent hesitation to push the state governments may most likely be based on the fears that the Opposition may gain a handle to beat them with, ahead of the assembly elections in Gujarat later this year. The three companies collectively account for an estimated 45 per cent of Gujarat state power requirements.

Business India feels that, while the sanctity of the contractual agreement is paramount, sometimes a practical solution is required to be taken in the best interest of the country. At one stage, the government will have to bite the bullet and take a decision to increase power tariffs. If there is a trade-off between lower prices and reduced power, as against higher price but sustainable supply of power, the latter is the better option. In any case, if the power plants were compelled to close down the state utilities would have no option but to source power from alternate sources which would be more costly than these plants, even after giving them a compensatory price hike.

‘Users pay’ regime has to be ushered in at some stage. In the telecom industry too, the mode of paying licence fees was changed, when the industry faced an existential threat. In this case, it is better to allow a marginal rise and ensure better capacity utilization, rather than lower production (the minimum, as may be mandated in the PPA agreement). In the Enron case also, tariff hikes were given, though in that case fuel costs were allowed as pass through costs. It is in no one’s interest to shut down the plants when the promoters are exhausted of funds. As of now, of course, none of the assets are classified as NPAs. And the reason for offering ownership could well be a negotiable ploy to get all stakeholders to the negotiating table.

Having put the best of power plants in place, economic sense requires that the assets are sweated more to ensure more power. •

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