

MoP's Proposal on Electricity (Amendment) Rules, 2023 [Draft]

The MoP issued the Draft Electricity (Amendment) Rules, 2023 on 20th April, 2023. The key highlights of the document is as below:

The notification proposes amendment in Section 15 of the Electricity Rules, 2005 which mandates the accounting and payment of subsidies payable to discoms under section 65 of the Act to be done in accordance with Standard Operating Procedure (SOP) issued by the Central Govt. Respective SERCs will issue quarterly reports for each discom giving the findings on the demands for subsidies raised by the discom in the quarter. Moreover, the above mentioned report to be based on accurate accounts of the energy consumed by the subsidized category and consumer-wise per unit subsidy declared by the states. Further, the actual payment of subsidy and the gap in subsidy due and paid by the respective Govt. will also be reported.

The draft rules proposes framework for financial sustainability of discoms, wherein the loss reduction trajectory to be adopted by the SERCs for tariff determination should be as per the trajectory agreed by the respective state Govt. and approved by the Central Govt. under any national scheme or programme. Further, the trajectory for both collection and billing efficiency for the discoms should be determined by the respective SERCs.

Appropriate Commissions should take into account all the prudent costs of power procurement incurred by the discoms for 24x7 power supply and for meeting requirements should be as per the resource adequacy plan.

Additionally, the rules propose for geo-tagging and recording of assets in the Fixed Asset Register (FAR). Gains and losses resulting from deviations are to be shared between the discom and consumers, with two-thirds of gains passed on to consumers and the remainder retained by the distribution licensee. In terms of losses, half is to be borne by the discom, and the other half is to be included in the tariff passed on to consumers.

The Document can be accessed [here](#).

CER Comments

- 1. Regulation 20 (I) (a):** The Draft Clause states that *“The loss reduction trajectory to be adopted by the State Commissions for tariff determination shall be in accordance with the trajectory agreed by the respective State Governments and approved by Central Government under any national scheme or programme.”*

As per section 62 of the Electricity Act 2003, determination of tariff for distribution licensees falls within the jurisdiction of the respective State Commissions. While the SERCs would continue to fix loss reduction trajectory for determination of tariff, the process of ‘approval’ would influence the tariff determination and may also delay the process.

As an alternative, the Central government, in consultation with the respective state government, may fix a loss reduction trajectory. This would serve as a minimum benchmark, the respective SERCs may fix a higher loss reduction trajectory thus ensuring that a minimum level of efficiency improvement is engrained in the performance of the discoms.

2. **Benchmarking Approach to Fix Loss Reduction Trajectory:** The discoms across the country differ in terms of network characteristics, consumer mix, operational practices etc. Some of the discoms have been able to achieve significantly lower distribution losses, while others continue to have high distribution losses. The methodological approach to set loss reduction trajectory should differentiate the underlying aspects. **A benchmarking based approach, such as Data Envelopment Analysis, can be used to set such differentiated target across discoms.**
3. **Recovery of Prudent Cost:** In Clause 20 (I) (c), the draft Clause states that “*All the prudent Costs of power procurement, incurred by Distribution licensee for ensuring 24x7 supply of electricity to consumers under the Electricity (Rights of Consumers) Rules, 2020 and for meeting requirements as per Resource Adequacy plan prepared under the Electricity (Amendment) Rules 2022 shall be taken into account, provided that the procurement of power has been done in a transparent manner or tariff has been determined by the Appropriate Commission*”.

As per Section 86(1)(b) of the Electricity Act 2003, power procurement by discoms is regulated by the respective SERCs. A coherent approach needs to evolve whereby there is effective role of SERCs, while the Rules provide a wider umbrella to ensure harmonized approach to resource adequacy while providing for localization to suit the conditions of the respective discom/state as per demand-supply pattern and economics thereof.

Further, to ensure cost efficient power procurement, the above clause may be modified as

“..... *provided that the procurement of power has been done in a transparent, cost effective and competitive manner as per Section 63, or tariff has been determined by the Appropriate Commission as per Section 62 of the Act*”. (additional text underlined)

4. **Pass through of prudent costs under sub-section (1) of section 42 of Electricity Act, 2003:** The Draft Clause states “*All the prudent costs incurred by the Distribution licensee for creating the assets for development and maintenance of distribution system in accordance with sub-section (1) of section 42 of the Act shall be pass-through*”.

A distribution licensee, as per Section 42 (1) of the Electricity Act, 2003, is duty-bound to develop and maintain a distribution system,

“*Section 42. (Duties of distribution licensee and open access): --- (1) It shall be the duty of a distribution licensee to develop and maintain an efficient, co-ordinated and*

economical distribution system in his area of supply”.

Section 42 refers to the provision for the distribution system, the associated costs are to be approved under Section 62, while being guided by Section 61. SERCs have issued relevant business regulations providing a framework for approval of investment to be made by the distribution licensees. Recovery of such investment is to be done through the approved tariff under Section 62.

- 5. Ratio of Sharing Gains/losses:** As per the Draft Clause 20 (I) (e), the sharing of gains/losses must be allowed between the distribution licensee and its beneficiaries through prudence check in the approved true-up of the year. According to this draft clause “...Half of losses shall be borne by distribution licensee and half shall be passed on to the consumers in tariff”. It is suggested that the losses borne by consumers should be less and may be equal to one-third of the sharing of losses and remaining may be borne by the distribution licensee in order to reduce burden on consumers. SERCs have issued Tariff regulations under Section 61 that also outline a mechanism for sharing of gains. For example, sharing of gains/ losses in Tariff Regulation notified by the State Commission u/s 181 of the Act for example MERC (Multi Year Tariff) Regulations, 2019¹ and KSERC (Terms and Conditions for Determination of Tariff) Regulations, 2021² where the losses shared to consumer is less.

It is important to emphasise that sharing of gains/losses may also depend on the key operating/financial parameter in question. Thus, the SERCs may be provided flexibility to choose gain/loss sharing mechanism as suitable in their individual context. Analysis of the impact of the prevailing (and differentiated) gain sharing approach on performance of the discoms may be undertaken to develop and framework for the same.

- 6. ‘Geo-info-tagged’ Assets (Regulation 20 (I) (d) (ii)):** The Draft Clause states that “Asset are geo-tagged and properly recorded in Fixed Asset Register (FAR) and the details are made available on the website of the Distribution licensee.”
Apart from geotagging of assets, it would be very useful to ensure that information on key aspects of assets including technical specifications, make, year of purchase, year of installation, last 5 repairs (when and by whom), previous location (if any), associated DT/feeder etc., should also be included in a database. This would enable interesting analytics to understand the performance of the assets and its usage..
- 7. Calculation of Equity Base for RoE:** Singh et al. (2022)³ estimated cost of equity for the infrastructure sector including electricity using Capital Asset Pricing Model (CAPM) as well as Fama & French multifactor models and found that the regulated returns are

¹ MERC (Multi Year Tariff) Regulations, 2019 https://merc.gov.in/wp-content/uploads/2022/08/MYT-Regulation-2019_English.pdf

² KSERC (Terms and Conditions for Determination of Tariff) Regulations, 2021 <https://www.erckerala.org/details?id=r1>

³ Singh, K, Singh, A, Prakash, P (2022), Estimating the cost of equity for the regulated energy and infrastructure sectors in India, Utility Policy, 74. See <https://www.researchgate.net/profile/Anoop-Singh-28>

often not in line with the ones offered by the market. It is found to be higher/lower than the regulated returns across various sub-sectors for the period of analysis. Furthermore, it has also been highlighted that post repayment of debt, depreciation should result in reduction in the equity base, thus ensuring that the consumers' interest are protected⁴.

⁴ CER's comments on JSERC (Terms and Conditions for Determination of Generation Tariff) regulations, 2020 [Draft] https://cer.iitk.ac.in/newsletters/regulatory_insights/Volume03_Issue02.pdf