THE OBSERVER
OF BUSINESS AND POLITICS

MONDAY NOVEMBER 6, 1995

# Bidding for power

The bidding methodology is not being taken up seriously even by the government, says **Uttam Gupta**

It all started with a big bang, but, seems to be ending in a damp squib. After announcing scrapping of the Dabhol power project, the Maharashtra government does not know what to do further. Whether it would finally scrap the project (meaning cancellation of PPA and related agreements) or renegotiate a fresh deal can be known only in due course.

In respect of other projects on fast track, the concerned state governments have announced their intentions to review. But they, too, do not know which way to go. A state of utter confusion prevails even as the country is progressively moving towards a situation of acute power shortage.

The central government has, at last, taken note of some of the flaws in its power policy. In a recent interview, minister for power N K P Salve admitted that 68.5 per cent PLF for providing assured return is too liberal and that the guarantee of return itself is an unacceptable proposition.

To look into all this and develop a new power policy, Salve has announced that the government will constitute a review committee. However, the committee is yet to be set up. Till such time new set of recommendations flow (no time frame is indicated), private power development programme will remain directionless.

In the meanwhile, there has been a sea change in the perception and approach of private developers. Majority of them have offered substantial reduction in cost and are ready to rework the PPAs to match the reasonable expectations of SEBs. Besides, new players have entered the fray offering to supply power at still lower tariff.

While on the one hand, this exposes the weaknesses of the MOU route, on the other, it confirms the enormous potential that is available for procuring power at reasonable rates if only we have a clear-cut and comprehensive policy and interactions with promoters are transparent.

Competitive bidding is the obvious choice. In fact, this has been endorsed by the Parliamentary Sub-Committee on Energy while stressing transparency in the process of tendering, evaluation, negotiations and taking decisions.

Various state governments need to work on this basis. However, if the government feels that private developers earlier on the MOU route, can come up with fresh cost competitive package, they could still do so, under the bidding dispensation.

Unfortunately, all the fast track projects still continue to enjoy special privileges as these have been exempted from the mandatory competitive bidding required under the guidelines issued by the ministry of power in February, 1995. This anomaly needs to be corrected.

The bidding methodology is not being taken up seriously even by the government. Salve's formulation asking for a single quote (depending on fuel type) in regard to power tariff is a hint. This is just not practical.

Apart from the capital cost, the cost of generation is also influenced by the supply of fuel, its price, cost of transporting and impact of various taxes and duties etc. The private developer has little or virtually no control over the latter set of factors, which in our set-up is primarily the function of the government and agencies controlled by it.

Supplies of coal, naphtha, fuel oil, gas etc. as well as their pricing are controlled by the government. Transportation by rail or through pipelines too is a government-controlled operation. Imposition of various taxes and duties and development cess etc can also lead to substantial modification in overall cost.

Moreover, there is a great deal of uncertainty about their supply and pricing. The natural gas pricing policy is presently under review. Following completion of this exercise, a new set of prices will take effect from 1.1.1996. Contemplated deregulation of the hydrocarbon sector will unavoidably result in increases in prices of other fuels like naphtha, fuel oil etc. Prices of coal are also not likely to remain unchanged. Position in regard to railway freight is no different. With these changes, impact of taxes and duties (levied on ad valorem basis) will also get modified.

Against this backdrop, how can a developer be expected to come up with a single quote for power tariff? This will not be possible even when it makes its own arrangement for fuel through import as depending on location of the station, transportation, taxes and duties will affect the delivered cost of the fuel.

In the selection process, we should go strictly on the basis of investment cost since this is what is within full control of the developers. This is also the area in which you have maximum scope for cost reduction. Instead of abandoning the two part tariff formula, the need is to use competitive bidding to bring down capital cost and to use reasonable norms in regard to the return, PLF and other factors to minimise per unit cost.

Whereas for coal based plants, PLF may be retained at 68.5 per cent, in respect of others particularly gas, this should be fixed at much higher level say, 80 per cent. This is because the latter being distinctly better fuel, it is possible to operate at higher PLF. Highest priority needs to be given to use of coal as this is available in plenty, unlike other fuels whose supplies are limited and imports entail foreign exchange outgo.

Provision for 16 per cent return on equity at prescribed PLF would appear to be reasonable. However, there is no need for additional incentive (under the present policy, additional 0.7 per cent for every 1 per cent incremental PLF is provided) as there is built-in incentive by way of saving in fixed charges including capital servicing due to actual operations above the prescribed PLF.

Protection of investment from the effect of fluctuation in exchange rate is no doubt important. But, this should be restricted only to servicing of loans raised in foreign currency.

Having selected the developer mainly on the investment criterion, the government must evolve legally enforceable fuel supply agreement and transportation arrangement with clearly stipulated price tags and taxation structure along with the time frame. It presupposes a stable long term administered pricing and taxation regime and perfect coordination between various administrative ministries and departments of the Union and between the it and state governments.

True, in all these respects, presently our house is not in order. But, there is no escape from setting things right on an urgent basis, if we are to avert the impending power famine in the country.

We should endeavour to facilitate timely payment to the IPPs without having to invoke the guarantee by state government or the counter guarantee by the Centre. For this, the long overdue reforms in the functioning of SEBs should be implemented to make them viable and financially sound. Critical areas that need immediate attention are reduction in transmission and distribution losses, proper billing and timely collection of dues.