Issues with Tariff based Competitive Bidding under Case I route

May 5, 2010
Our comments focus on

Policy framework - bid documents

Regulatory framework - CERC’s regulations for bid evaluation
Comments on bid documents cover

1. Qualifying Requirements
   1.1 Land
   1.2 Fuel
   1.3 Environmental & Forest Clearance
2. Contract Performance Guarantee
3. Qualifying requirement & time period for meeting the Condition Subsequent
4. Application for Open Access
5. Escalation Rates
1.1 Qualifying Requirement - Land

**Bid Conditions**

- Bidder should have acquired & taken possession of at least 50% of the area of the land as indicated in the environmental clearance.
- Bidder to certify through affidavit the total land acquired for the power station & that there are no pending claims/litigation of any nature against/involving the Bidder vis-à-vis land & that Bidder has absolute rights & authority to establish & run power plant on the land.

**Our suggestion**

Condition of land availability be modified such that land acquisition is correlated with the phase of development of the project.

- Developer spends money upfront for acquiring 50% of the land before financial closure.
  - Only bidder with deep pockets can meet requirement.
- Developers plan phased project development. But environmental clearance required for entire planned capacity.
  - Even if bidder bids for capacity targeted in the first phase, he would need to show land acquisition for more than that phase.
1.2 Qualifying Requirement - Fuel

**Bid Conditions**

- In case of *domestic coal*, Bidder should have fuel tied up for total installed capacity for the term of the PPA.
- In case of *imported coal*, Bidder shall have either acquired mines having proven reserves for at least 50% of the total installed capacity for the term of the PPA or should have at least signed Fuel Supply Agreement for 5 years for the total installed capacity.
- Similarly for *domestic gas & RLNG*.

**Our suggestion**

Fuel availability or tie-up in case of coal based projects should be correlated to 70% of the coal linkage according to phased development of the project.

**Most projects with coal linkages do not meet requirement**

- Do not have the quantity of fuel on normative basis or the linkage is only for one unit while projects is defined in environmental clearance as two units.

**For coastal projects, coal linkage provided for only 70% of requirement as per policy. Balance fuel tied-up by through import**

- Project with only domestic coal linkage becomes non-responsive & can get rejected if imported coal is not tied for balance capacity.
- Linkage available for non-coastal projects usually insufficient when computed on normative availability basis.
1.3 Qualifying Requirement - Environmental & Forest Clearance

**Bid Conditions**

- Bidder shall have submitted the requisite proposal, for the final environmental clearance approval.

**Process of obtaining environmental clearance is time taking**

- At the time of bidding, the process of obtaining such clearance may be at an initial or intermediate stage.
- Process of public hearing and its outcome is crucial for clearance. But condition is somewhat restrictive.

**Our suggestion**

- Since bid process takes time to conclude, bidder may be required to submit the requisite proposal for final environmental clearance approval by the time of opening of the financial bid.
- Bid should be returned as unresponsive or disqualified if bidder cannot meet requirement at the time of opening of the financial bid.
Contract Performance Guarantee

Bid Conditions

- Successful bidder required to provide Contract Performance Guarantee within 30 days of issue of Letter of Intent by Procurer
- Guarantee is determined on the basis of Rs. 30 lakhs/MW of the total Contracted Capacity

- Level of Guarantee may turn out to be very high (for 1000 MW, Rs. 300 Crores)
  - Bidder without deep pockets may be unable to furnish guarantee before financial closure
- Procurer recognizes bidder & not developer. So Bid Bond & Contract Performance Guarantee are provided by Bidder
  - In case Bidder is a Trader, developer provides the requisite Bank Guarantee to the trader on back-to-back basis leading to two Bank Guarantees for one single sale contract

Our suggestion

- Level of Contract Performance Guarantee may be lowered
- To prohibit non-serious bidders, termination cost of the PPA may be increased to a very high level
- Need to evolve a way out of the trader-developer dilemma
3 Qualifying requirement & time period for meeting the Condition Subsequent

**Bid Conditions**

- Conditions Subsequent under PPA need to be fulfilled by the Bidder in minimum 10 months
  - Execution of the Fuel Supply Agreement
  - Obtaining all necessary permission for long term open access
  - Obtaining all Consents, Clearances & Permits required for supply of power to Procurer
- Failure to meet Condition Subsequent within given time frame means payment of additional Bank Guarantee on weekly basis @ Rs. 1.50 lakhs per MW of Contracted Capacity
  - Maximum liquidated damages limited to Rs. 40 lakhs/MW before Bank Guarantee encashed & contract terminated

**Our suggestion**

- Time period for meeting condition subsequent may be increased to at least 18 months with project progress reviews at monthly levels
- Would be win-win situation for Developer & Procurer who can get base load power at competitive tariffs vis-à-vis volatile short terms prices

- Some conditions are not under the bidder’s control
  - Bidder can only apply & follow up
- Bank Guarantee, if encashed, may suffice to purchase short term power for a very small duration
4 Application for open access

**Bid Conditions**

- For plant located within the Procurer State, project bus-bar is Delivery Point & Procurer is responsible for coordinating with the state transmission network for evacuation of power
- For plant located outside the State, Bidder is responsible for obtaining Open Access
- LC is provided to Bidder only for the generation charges, not for transmission charges which are ‘reimbursed’

- In case Open Access is sought by Developer/Trader, PGCIL demands Bank Guarantee equal to 6 months billable amount as payment security in addition to Letter of Credit
- In case Open Access is obtained by the Procurer, only Letter of Credit suffices for PGCIL
  - When bidder obtains Open Access, procurer gets higher tariff

**Our suggestion**

- Procurer already has a power transmission agreement with PGCIL & contracted capacity is dedicated to the Procurer for 25 year period
- Procurer obtaining the Open Access would provide parity between plants located within & outside the state and limit/reduce the loading of 6 months Bank Guarantee charges on tariff
5 Escalation Rates

Bid Conditions

- On today’s base cost, escalation rate used for evaluation is applied to find the base cost for the 1st year of operation.
- This 1st year base tariff becomes the basis on which the escalation for making payment is applied.

- If fuel charges are Rs. 0.50 per kWh on the basis of current coal price, considering the present escalation rate for evaluation of bid as say 5%, coal price for 1st year would be Re. 0.58/kWh.
  - Base price on which CERC escalation rates for payment will be applied for making payments.
- If coal prices escalate by more than 5% during the 48 months of project commissioning, Bidder has no protection.

Our suggestion

SBD may be amended to take care of actual escalation in coal price including freight escalation rate during the construction period of 48 months to arrive at 1st year base tariff.
Our comments focus on

Policy framework - bid documents

Regulatory framework - CERC’s regulations for bid evaluation
5 Escalation Rates for Bid Evaluation

Regulatory Provisions

- Earlier, transmission charges (as applicable on date) were added to the levellised generation charge to evaluate the bids.
- Now, transmission charges have been escalated on annual basis in the same way as fuel transportation charges to bring about parity between fuel transportation & power transmission charges for evaluating the tariff at the procurer periphery.

- Comparison of increase in freight charges & transmission charges is incorrect:
  - Capacity addition in railway network cannot be compared with capacity addition in power transmission network.
  - Large generation capacity addition necessitates corresponding increase in transmission capacity.
- CERC escalation rates applied on an annual compounding basis from the date of bid submission till the tenure of the contract:
  - Maximum Inland Freight Escalation Rates - 2.48% & Power Transmission Escalation Rates - 5.61%
  - Plant located at the pit head becomes unviable compared to plant located within the State which has invited the bid as the transmission charges would be zero.
### Illustration - Impact of Escalation of Transmission Charges

<table>
<thead>
<tr>
<th>Plant Location</th>
<th>Delivery State</th>
<th>Transmission charges</th>
<th>Escalated transmission charges as considered during evaluation</th>
</tr>
</thead>
<tbody>
<tr>
<td>1. Maharashtra (WR)</td>
<td>Maharashtra (WR)</td>
<td>ZERO (CTU+STU)</td>
<td>ZERO (CTU+STU)</td>
</tr>
<tr>
<td>2. Chhattisgarh (WR)</td>
<td>Maharashtra (WR)</td>
<td>Rs. 0.12 per kWh</td>
<td>Rs. 0.256 per kWh</td>
</tr>
<tr>
<td>3. Orissa (ER)</td>
<td>Maharashtra (WR)</td>
<td>Rs. 0.28 per kWh</td>
<td>Rs. 0.618 per kWh</td>
</tr>
<tr>
<td>4. Uttar Pradesh (NR)</td>
<td>Maharashtra (WR)</td>
<td>Rs. 0.26 per kWh</td>
<td>Rs. 0.577 per kWh</td>
</tr>
<tr>
<td>5. Karnataka (SR)</td>
<td>Maharashtra (WR)</td>
<td>Rs. 0.33 per kWh</td>
<td>Rs. 0.731 per kWh</td>
</tr>
</tbody>
</table>

- If Maharashtra is the procurer, it is a forgone conclusion as to who wins the bid in case a plant located within Maharashtra is qualified financially and technically.
- Negates the common understanding that carrying coal is more expensive than transmitting power.

### Our suggestion
- Revise transmission escalation rate & fixing it at a more realistic level keeping in view of the future growth of transmission system & estimated cost.
- Since transmission charges are to be paid by the procurer on an actual basis, there should be no loading of transmission charges for evaluation of bids.
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