BEFORE THE KERALA STATE ELECTRICITY REGULATORY COMMISSION

In the Matter of: **Review Petition against the KSERC order dated 16th March 2017 in Petition OA No 9/2016 in the matter of Truing Up of accounts of KSEB for the year 2011-12.**

Petitioner : **Kerala State Electricity Board Limited, Vydyuthi Bhavanam, Pattom, Thiruvananthapuram**

THE PETITIONER HUMBLY STATES THAT:

1. Hon'ble Commission as per order dated **16th March 2017 i**n Petition **OA No 9/2016** in the matter of Truing Up of accounts of KSEB for the year 2011-12 has approved the revenue gap for the year at Rs 1386.97 crore as against the revenue gap of Rs 1934.14 crore as per the C&AG audited accounts. A comparison of the various expenses as per the C&AG audited accounts and the order on Truing Up for the year is detailed below.

Table-1

Comparison of the expenses as per the C&AG audited accounts and KSERC order

Sl No.	Particulars	Actual	True Up order	Variation over Truing Up order & actuals (-) decrease /(+) increase
		(Rs. Cr)	(Rs. Cr)	(Rs. Cr)
1	Generation Of Power	281.65	281.65	0.00
2	Purchase of power	4375.31	4352.32	22.99
3	Interest & Finance Charges	340.52	247.98	92.54
4	Depreciation	466.00	330.60	135.40
5	Employee Cost	1903.33	1822.43	80.90
6	Repair & Maintenance	251.70	182.28	69.42
7	Administration & General	202.72	80.10	122.62
8	Other Expenses	73.23	73.23	0.00
9	**Gross Expenditure (A)**	**7894.46**	**7370.59**	**523.87**
10	Less : Expenses Capitalized	126.61	126.61	0.00
11	Less : Interest Capitalized	30.51	30.51	0.00
12	**Net Expenditure (B)**	**7737.34**	**7213.47**	**523.87**
13	Statutory Surplus/ Roe **(C)**	240.72	217.42	23.30
14	**ARR (D) = (B) + (C)**	**7978.06**	**7430.89**	**547.17**
15	Less Non-Tariff Income	450.86	450.86	0.00
16	Less : Revenue from Tariff	5593.02	5593.02	0.00
17	Revenue from subsidies and	0.04	0.04	0.00
18	**Total Income**	**6043.92**	**6043.92**	0.00
19	**Revenue Gap**	**1934.14**	**1386.97**	**547.17**

2. As detailed above, Hon'ble Commission had made a total disallowance of Rs 547.17 crore for the year 2011-12 from the actuals as per the audited accounts. The major disallowance are:

Table-2 Summary of disallowances (Rs in crore)

Sl. No	Expense head	Amount (Rs. in crore)
1	Cost of power purchase	22.99
2	Employee cost	80.90
3	Repair & Maintenance expenses	69.42
4	A&G expenses (excl 3(1) duty)	29.31
5	Depreciation	135.40
6	Interest and finance charges	92.54
7	Return on equity	23.30
8	Section 3(1) duty	93.31
9	Total	547.17

3. KSEBL submits that, while approving the truing up petition based on the C&AG audited accounts, Hon'ble Commission was pleased to approve most of the claims made by KSEBL. However, Hon'ble Commission has not considered the actual expenditure furnished by KSEBL in certain instances and made factual errors in assessment while approving certain expense components. Hence, KSEBL submits this petition before the Hon'ble Commission for the kind review of the order dated**16th March 2017**.

4. Detailed explanations in respect of the disallowances are furnished in the following paragraphs.

I. <u>Disallowance under interest and finance charges by Rs.92.54 crore.</u>

5. Break up of disallowance by the Hon'ble Commission under this head is summarized below:

Table3 Break up of disallowance under Interest and finance charges

Sl. No	Description	Amount (Rs in crore)
1	Interest on loans	4.96
2	Interest on security deposit	9.82
3	Interest on borrowings for working capital	82.25
4	Interest on PF	0.42
5	Total	97.45
6	Less: Additional interest for funding capital expenditure	4.91
7	Total disallowance (5-6)	92.54

a. Interest on loans Rs.4.96 crore

6. Hon'ble Commission has disallowed Rs.4.96 crore from interest on loans in view of the Audit observation that interest for the year is overstated by this amount since the interest on loan under R APDRP

has been worked out at 11.50% instead of 9%.In this connection, it is humbly submitted as follows:

(a) KSEB has already incorporated necessary corrections in accounts in April 2012 (in the year 2012-13) as per journal No. 9 of 04/2012 by crediting to prior period income. Further, it may also be noted that the fact of subsequent rectification has duly been disclosed in replies of the Board to the audit comments in page 111 of the Annual statement of accounts for 2011-12 enclosed herewith.

(b) Hence, Other income relating to prior period amounting to Rs.16.82 crore for 2012-13 is inclusive of Rs.4.96 crore excess interest charged for the year 2011-12 and the Hon'ble Commission has approved prior period charges net of prior period income as per para 146 of the truing up order for 2012-13.

(c) In view of the above submission, it is clear that the disallowance in 2011-12 as well as considering the same in 2012-13 as prior period income amounts to duplication and hence Hon'ble Commission may kindly review the decision so as to rectify the anomaly.

b. Interest on security deposit Rs.9.82 crore.

7. In respect of disallowance under interest on security deposit, it is humbly submitted that:

(a) Hon'ble Commission has considered the actual interest disbursed to consumers in 2011-12 against the provision created for that year. The provision for 2011-12 has been created on the closing balance of security deposit in the previous year (ie as on 31.03.2011) by applying the bank rate prevailed as on that date. Hence the interest as per accounts denotes the provision created which is meant for disbursement during the succeeding year. Therefore these two figures are not comparable.

(b) Actual disbursement during 2011-12 has been made against the provision created for the year 2010-11. The software calculates the exact amount of interest payable to each and every consumer by applying bank rate while making payment. Therefore actual disbursement has to be compared with the provision for the previous year only.

(c) Interest was provided at bank rate at 6% till 2011-12, @8% for 2012-13, @8.50% for 2013-14 and 9 % for 2014-15 on the opening balance of security deposit in respective years. But the interest so provided in accounts has been credited to the consumers account in the first quarter of the next financial year only. This practice is being followed consistently in line with the provisions contained in Regulations 67 to 74 in Chapter 4 of the Supply Code.

(d) In short, as against the provision for security deposit for 2011-12 amounting to Rs.68.01 crore, and Rs. 113.98 crore for 2012-13, subsequent actual disbursement during the respective succeeding years were Rs.58.49 crore and Rs. 86.19 crore.

(e) Year wise break up of interest on security deposit provided in accounts at the year end and actual disbursement accounted during the year is furnished below illustrates the above fact.

Table4 Details of Security deposit and interest thereon

Financial Year	SD Balance (Rs. in cr)	Interest provided (Rs.in cr)	Rate	Interest disbursed during the year (Rs.in cr)
2009-10	1078.92	58.04		38.28
2010-11	1242.54	64.74	@ 6% (on 1078.92 cr)	44.80
2011-12	1424.73	68.01	@ 6% (on 1242.54 cr)	58.19
2012-13	1586.30	113.98	@ 8% (on 1424.73 cr)	58.49
2013-14	1805.61	134.84	@ 8.50% (on 1586.30cr)	86.19
2014-15	1975.31	162.50	@ 9% (on 1805.61cr)	121.48
2015-16	2287.31	167.90	@ 8.50% (on 1975.31cr)	153.64

(f) Hon'ble Commission may kindly approve the subsequent actual disbursement against provision created for the year of true up instead of allowing actual payment made against the provision created in preceding year.

(g) On the basis of above submission, Hon'ble Commission may be pleased to true up Rs.58.49 crore under interest on security deposits for 2011-12.

c. Interest on overdrafts Rs. 82.25 crore.

8. Hon'ble Commission has fully disallowed the interest on Overdrafts for the year 2011-12, actually paid by KSEB, to various financial institutions amounting to Rs 82.25 crore. While denying interest, Hon'ble Commission, per Table 21 of the truing up order, has ascertained Rs.3909.75 crore as negative working capital for the year 2011-12 and concluded that working capital needs have been more than compensated by the current liabilities. In this connection, it is humbly submitted as follows:

(i) It is understood that the Hon'ble Commission has assessed the need for borrowings towards working capital but did not considered the need for the borrowings requirement due to factors other than working capital. It seems that the nomenclature used to disclose the expenditure in accounts as 'interest on working capital' may have misguided the Hon'ble Commission. Hon'ble Commission may kindly consider the following in this regard:

(ii) Kerala State Electricity Board had compiled its Annual Statement of Accounts till 31.10.2013 in accordance with the related provisions of the Electricity (Supply) Act, 1948 and the rules made there under it viz. Electricity Supply Annual Accounting Rules, 1985 (ESAAR), which has been saved under section 185(2)d of the Electricity Act, 2003. Accordingly had prepared its Annual Accounts for 2011-12 in the format prescribed for the purpose in ESAAR, 1985.

(iii) As per ESAAR, the overdrafts availed by the Board are to be disclosed under Schedule 30 of the Annual Statement of Accounts titled 'Borrowings for Working capital'. Interest on such borrowings is to be disclosed under 'Interest on borrowings for working capital', a sub item of schedule 12 titled 'Interest and Finance charges'. Accordingly, KSEB has disclosed the details in the Annual Statement of Accounts.

(iv) Section 59 of the Electricity (Supply) Act, 1948 mandates to carryout operations and adjust the tariff so as to ensure a surplus not less than 3% of the value of fixed assets of the Board at the beginning of the year. This statutory requirement negate the need for short term borrowings to meet the revenue gap arising out of operations and necessitates only with regard to the working capital borrowings. Hence ESAAR, 1985 had contained the nomenclature as mentioned above. It is pertinent to mention that from the year 2014-15 onwards, overdrafts were classified under Note 7 to the Annual statement of Accounts titled 'Short Term Borrowings' and 'interest on overdrafts' under Note 30 Finance cost.

(v) It is humbly clarified that even though nomenclature under which disclosure is made in accounts were that of 'working capital' in reality, overdrafts were availed by KSEB to make good the revenue deficit.

(vi) Hon'ble Commission may kindly consider the fact that KSEB had to avail overdrafts to meet the accumulated revenue gap and the interest on such borrowings were prayed to be allowed as carrying cost of Revenue gap in the truing up petition. The revenue gap , overdrafts, interest etc are showing increasing trend year after year as tabulated below, which clearly reveals that the revenue gap kept increasing year after year justifying the year on year increase in overdraft:

Table 5 Comparison of revenue gap and overdraft

Year	Cumulative approved and un bridged revenue Gap as per orders of Hon'ble Commission	Revenue gap as per audited Accounts- Year on year accumulation.	Cumulative Generation and Power purchase cost over approval by KSERC.	Overdraft outstanding at the year end.	Interest on OD for the year
31.03.2011	424.11			310.36	35.78
2011-12	1352.73	1934.13	731.71	1114.36	82.25
2012-13	1984.75	5933.27	3294.67	1942.96	167.94
2013-14	2445.73	7031.79	3849.26	2303.62	265.43
2014-15	2925.01	8847.04	4360.49	2110.48	269.08

Note: The Overdraft as on 31.03.2015 has come down by Rs.193.14 crore in comparison to the corresponding figures as on 31.03.2014 primarily because of the utilization of FD maturity proceeds aggregating to Rs.524.68 crore with interest Rs.53.74 crore in March 2015 for repayment of Overdrafts.

(vii) With regard to Table 21 of the truing up order in which negative working capital for the year 2011-12 has been ascertained Rs.3909.75 crore, it is humbly submitted that certain components like accumulated revenue gap have not been considered assessing the need for borrowings.

(viii) In the tabulation referred above, Hon'ble Commission has fully considered other current liabilities amounting to Rs.4697.92 crore. A substantial portion of this liability (Rs.2058.90 crore) represents sums payable to Government of Kerala. This amount consists of (1) Electricity duty collected from consumers under section 4 of KED Act, 1962, (2) Electricity duty payable by KSEB u/s 3(1) of the KED Act, 1962 (which had never been approved by the Hon'ble Commission by virtue of Section 3(3) of the KED Act and subsequently netted off against receivables from Government), (3) guarantee commission payable to Government etc. However, the sums receivables to KSEB from Government along with other sums to be netted off against payables to Government were not at all considered.

(ix) It is humbly submitted that subsidy receivable amounting to Rs.533.06 crore together with net subsidy to be written off to the tune of Rs. 1202.30 crore, aggregating to Rs.1735.36 crore existed as on 31.03.2012 has not been considered. It is submitted that the subsidy receivables from Government till 31.10.2013 were actually net off against sums payable to Government at the time of re vesting. Further, un bridged revenue gap as per accounts as on 31.03.2012 was Rs.5327.99 crore, which could only be financed through borrowings.

(x) When these elements, which form an integral part of accounts, are duly considered, actual requirement of borrowing suffice to the tune of Rs.3153.60 crore, but KSEB had availed just 35% of requirement to carry out the operation during the year as detailed below:

Table 6 Computation of net requirement of borrowings

Sl. No	Particulars	Rs. in crore	Rs. in crore
1	Working capital as per Table 21 of the order		-3909.75
2	Add: Subsidy receivable from Government	533.06	
3	Net subsidy to be written off	1202.30	
4	Accumulated revenue gap	5327.99	7063.35
5	Net requirement of borrowings (1+4)		3153.60
6	Actual overdrafts as on 31.03.2012		1114.36
7	Borrowings as a % of requirement (6/5*100)		35.34

(xi) Hence it is evident that borrowings are required to in order to meet the financing requirement and it can be firmly ascertained that borrowings were made to finance the un bridged revenue gap. KSEB has been able to restrict actual borrowings to one third of requirement as tabulated above because of the financing strategy adopted by KSEB, ie to utilize all internal resources (Electricity duty collection, security deposit, consumer contribution etc and deferred payments) before borrowing at lowest possible interest.

(xii) It is further submitted that the revenue gap as per accounts as well as the same approved by the Hon'ble Commission has been increasing year after year as shown below:

Table 7 Comparison of the approved revenue gap and actual as per accounts

Year	Un-bridged gap as per the orders of the Commission	Actual Revenue gap as per audited accounts including RoE	Increase over approval	Remarks
	(Rs. Cr)	(Rs. Cr)	(Rs. Cr)	
Up to 2010-11	424.11	3393.86		As per truing up 2010-11
2009-10-	290.00			Provisional order dated 01.12.2016 in Suo motu proceedings for 2016-17 and 2017-18 (additional gap determined In line with Hon'ble APTEL directions.
2010-11	340.00			
2011-12	1386.97	1934.13	547.16	As per True up order (Rs.928.61 cr as per ARR order)
2012-13	3132.97	3999.14	866.17	As per True up order (Rs. 632.03 crore after tariff revision in ARR)
2013-14	460.98	1098.52	637.54	ARR order
2014-15	479.28	1815.25	1335.97	ARR order
Total	6514.31	12240.90		

(xiii) The increasing trend in overdraft amply proves the fact that it was necessary to borrow for bridging the huge revenue gap of previous years. The OD balance as on 31.03.2008 had been Rs.51.81 crore which increased steadily thereafter and never decreased because of the above reason. The following table giving details of month wise balance of overdrafts from 2007-08 clearly establish the fact that the borrowings are directly related to the ever increasing revenue gap.

Table 8 Details of month end balance of Overdraft								
Month	2007-08	2008-09	2009-10	2010-11	2011-12	2012-13	2013-14	2014-15
Apr	0.26	25.95	263.47	244.63	345.35	1275.76	2381.63	2431.58
May	28.11	20.16	303.59	252.07	464.23	992.85	2240.95	2619.45
Jun	53.00	52.58	282.04	98.63	317.99	1329.23	2666.25	2938.32
July	1.39	36.18	250.87	365.35	457.58	1479.85	2582.55	2572.77
Aug	39.22	140.86	491.67	232.59	600.89	1414.12	2651.03	2609.24
Sep	10.06	246.39	221.10	214.84	630.91	1368.81	2578.67	2517.98
Oct	0.26	219.41	146.67	139.13	763.95	1568.64	2816.5	2522.47
Nov	2.81	175.29	179.40	246.95	837.07	1511.65	2631	2602.21
Dec	-0.18	277.45	203.32	295.62	917.13	1624.01	2681.9	2858.46
Jan	38.89	356.33	159.20	276.69	968.53	1761.65	2545.43	2517.08
Feb	0.41	360.93	62.27	717.07	1239.33	1842.15	2716.03	2686.26
Mar	51.81	230.13	153.20	310.36	1114.36	1942.96	2303.62	2110.48
Interest on OD	**2.80**	**22.14**	**24.58**	**35.78**	**82.25**	**167.94**	**265.43**	**269.08**

(xiv) From the table it can also be seen that the Overdrafts has gone up to Rs.2110.48 crore as on 31.03.2015 from Rs.51.81 crore as on 31.03.2008.KSEBL, being a regulated utility, the increase in Provident Fund balance and non cash flow expenses like depreciation and Return on equity etc do not create cash availability unless these are allowed to be fully recovered through tariff. The huge un bridged gap amply makes it clear that the expenses were not allowed to be recovered in full, which in turn resulted in financial crunch.

(xv) It is humbly submitted that Hon'ble Commission, by duly recognizing these realities, had been pleased to approve interest on overdraft in full till 2010-11 as per orders on truing up for the respective years. However, it is seen from the truing up orders for 2011-12 and 2012-13 that amount spent on this account has been disallowed in full even though ad hoc allowances to the tune of Rs.15 crore and 20 crore were made in the respective ARR orders as detailed below.

Table 9 Details of actual interest on OD and approval by KSERC (Rs in crore)

Year	Interest on Overdraft	Interest on OD approved as per truing up order	Order reference
2007-08	2.80	2.80	10.06.2011
2008-09	22.15	22.15	10.06.2011
2009-10	24.58	24.58	25.10.2012
2010-11	35.78	35.78	30.10.2012
2011-12	82.25	0.00	16.04.2017. Allowed Rs.15 crore as per ARR Order dated 01.06.2011.
2012-13	167.94	0.00	20.04.2017. Allowed Rs.20 crore as per ARR Order dated 28.04.2012.

(xvi) Hon'ble Commission may kindly note that interest on overdrafts paid by KSEBL from 2011-12 till 2015-16 has exceeded Rs.1000 crore and denial of this expense would result in grave financial difficulty to the utility. The details are furnished below:

Table 10 Details of year end OD and interest for the year (Rs in crore)

Year	Year end OD balance	Interest for the year
2011-12	1114.36	82.25
2012-13	1942.96	167.94
2013-14	2303.62	265.43
2014-15	2110.48	269.08
2015-16	2171.94	229.43
Total		1014.13

(xvii) Having considered the reality and gravity of the situation, Hon'ble Commission, as per orders on ARR for 2014-15 dated 14.08.2014 was pleased to approve an amount of Rs. 50.89 crore towards interest as carrying cost for approved revenue gap till 2010-11 as per truing up orders. However, similar consideration of the matter was not accorded while issuing orders on truing up for 2011-12 and 2012-13.

(xviii) Moreover, the actual interest claimed in true up is well within the limits specified by the Hon'ble APTEL and hence eligible for pass through as explained below:

(xix) Hon'ble APTEL, in many judgments, had ordered allowance of carrying cost on approved and un recovered revenue gap. In this connection KSEBL submits that:

(a) Hon'ble APTEL, in its judgment dated 10.11.2014 in appeal petition no 1 of 2013 and 19 of 2013, judgment dated 06.05.2016 in the appeal no 135 of 2014 and judgment dated 27.04.2016 in appeal no 81 of 2014 has directed the Hon'ble Commission to pass orders in terms of its findings <u>along with carrying cost</u>. It may kindly be noted that the decision of the Hon'ble Commission in not allowing carrying cost, is not in line with the Hon'ble APTEL's specific direction to allow the same while issuing consequential orders.

(b) Hon'ble Commission as per order on ARR & ERC for the year 2014-15 dated 14.08.2014 had allowed Rs. 50.89 crore towards carrying cost on trued up revenue gap till 2010-11. In this context, it is kindly submitted that the additional revenue gap in view of the Hon'ble APTEL orders dated 10.11.2014 and 06.05.2016 in the matter of Truing up of Accounts for 2010-11 and 2009-10 should also have invariably been considered along with Rs.424.11 crore revenue gap already trued up till 31.03.2011. Hon'ble Commission has provisionally assessed Rs.290 crore for 2009-10 and Rs.340 crore for 2010-11 as per provisional order dated 01.12.2016 in the matter of suo motu proceedings for the years 2016-17 and 2017-18.

(c) The stand of Hon'ble Commission is not in line with the directions given by the Hon'ble APTEL as per judgment dated 11.11.2011 in Appeal No. 1 of 2011, a decision which has been relied by the Hon'ble Commission to initiate the suo motu proceedings, that,

"*create a problem of cash flow for the distribution licensees which are already burdened with heavy debts"* and that *"opening balances of uncovered gap must be covered through transition financing arrangement or capital restructuring", "Carrying Costs of Regulatory Asset should be allowed to the utilities"* and the "*Recovery of Regulatory Asset should be time-bound and within a period not exceeding three years at the most and preferably within control period".(para 62)*
Thus, creation of the regulatory asset will neither be in the interest of the respondent no. 1 nor the consumers.

Thus, we hold that the creation of the regulatory assets on the basis of projected shortfall in revenue, that too without any directions for time bound recovery for the regulatory asset along with its carrying cost, is in contravention of the Tariff Policy and the 05 Regulations". (para 8.12)
Further, the creation of the regulatory asset without any directions for carrying cost and time bound recovery was neither in the interest of the distribution licensee nor the consumers. (para 63)

Hon'ble APTEL, by invoking the powers under Section 121 of the Act issued directions to the State Commissions inter alia to allow

> *recovery of the Regulatory Asset should be time bound and within a period not exceeding three years at the most and preferably within Control Period. Carrying cost of the Regulatory Asset should be allowed to the utilities in the ARR of the year in which the Regulatory Assets are created to avoid problem of cash flow to the distribution licensee. (para 64(iv)*

(d) Kind attention of the Hon'ble Commission is also invited to the Hon'ble APTEL judgment dated 28 th November-2013 in Appeal petition No. 190 of 2011, in which circumstances necessitating the creation of regulatory asset and ordered as follows

83. The relevant principles which have been laid down in these decisions are extracted below:
(a) We do appreciate that the State Commission intents to keep the burden of the consumers as low as possible. At the same time, one has to remember that the burden of the consumers is not ultimately reduced by under estimating the cost today and truing up in future as such method also burdens the consumer with carrying cost.
(b) The carrying cost is allowed based on the financial principles that whenever the recovery of cost is deferred, the financing of the gap in cash flow arranged by the distribution company from lenders and /or promoters or accruals, has to be paid for by way of carrying cost.
© Carrying cost is a legitimate expense and therefore recovery of such carrying cost is legitimate expenditure of the distribution company.

(e) Further, as per judgment in Appeal 153 of 2009 dated 30.07.2010, which had been relied on the judgment dated 28.11.2013 referred to in (d) above, the Hon APTEL has clearly spelt out the circumstance in which carrying cost has to be allowed to utilities, as under:

83 (d) "11.5 The utility is entitled to carrying cost on its claim of legitimate expenditure if the expenditure is:

a) accepted but recovery is deferred e.g. interest on regulatory assets,
b) claim not approved within a reasonable time, and
c) disallowed by the State Commission but subsequently allowed by the Superior Authority."
d)Revenue gap as a result of allowance of legitimate expenditure in the true up.

(f) Hon'ble APTEL judgment dated 18 th October-2012 on Appeal petition No. 7 of 2011, 46 of 2011 and 122 of 2011, in respect of creation of regulatory asset and ordered that *carrying cost be allowed for such additional expenditure if approved during truing up, recovery is differed or allowed subsequently by a superior authority.*

(g) The above decisions were upheld in the order dated 30-05-2014 in appeal nos. 147, 148 and 150 of 2013 also.

(i) It is humbly submitted that the Hon'ble Commission had already identified a revenue gap of Rs 424.11 Cr up to 31-03-2011 as per truing up orders for the year up to 2010-11. Further, an amount of Rs 928.62 Crore has already been recognized as revenue gap for 2011-12 as per ARR order that has not been bridged through tariff revision. Thus an amount of Rs 1352.73 Cr comes under case (a) and (d) identified by Hon APTEL as above.

(ii) Further, Rs 290 Cr in 2009-10 and Rs 340 Cr in 2010-11 were provisionally identified by the Hon'ble Commission as part of implementing the Hon'ble APTEL order regarding true up of respective years. Thus a further amount of Rs 630 Cr (290 + 340) is also eligible for carrying cost as per ratio position held by Hon APTEL vide (c) above.

(iii) Hence, KSEB is eligible for carrying cost on Rs. 1982.73 Crore (Rs.1352.73 cr+Rs.630 cr) but the actual borrowings was of Rs.1114.36 crore for the year, which was well within this limit. It may kindly be noted that KSEBL has sought approval only for the actual interest payment made.

h. It is further submitted that the Hon'ble APTEL, as per judgment dated 08.04.2015 in Appeal 160 of 2012 and batch has laid down the principle on which carrying cost is to be allowed. The decision was reiterated in judgment dated 22.04.2015 in Appeal 174 of 2013 as well. The same is reproduced below:

42. We find that for carrying cost, the State Commission has considered the revenue gap to be applicable from the end of the year of the occurrence of the revenue gap up to the middle of the year in which the same is proposed to be recovered. This is not correct. The interest to be calculated for the period from the middle of the financial year in which the revenue gap had occurred up to the middle of the financial year in which the recovery has been proposed…This is because the expenditure is incurred throughout the year and its recovery is also spread out throughout the year. Admittedly, the revenue gap will be determined at the end of the financial year in which the expenditure is incurred. However under or over recovery is the resultant of the cost and revenue spread out throughout the year. Similarly, the revenue gap of the past year will be recovered throughout the financial year in which its recovery is allowed. Therefore interest on revenue gap as a result of true up for a financial year should be calculated from the mid of that year till the middle of the financial year in which such revenue gap is allowed to be recovered.
43. To explain this point let us assume that there is a revenue gap of 12 crores in the true up of FY 2010-11. If the cost and the revenue and the permitted expenditure had been properly balances, this gap of 12 crores would have been recovered throughout the 12 months of FY 2010-11. Now, this revenue gap is allowed to be recovered in tariff during FY 2013-14. The recovery of gap of Rs. 12 crores from the distribution licensee consumers will be spread over the 12 months period of 2013-14. Therefore carrying cost would be calculated from the middle of FY 2010-11 to middle of FY 2013-14 ie 3 years.

(xx) In short, Hon'ble APTEL through various judgments has established the fact that carrying cost for the revenue gap is a legitimate expenditure, specified the components of revenue gap as eligible for carrying cost and the manner in which carrying cost is to be allowed.

(xxi) It is humbly submitted that the Hon'ble Commission may kindly consider the fact that the revenue from tariff as well as the non-tariff income for the year has fully been considered on accrual basis while approving the orders on truing up. Further, KSEBL has no business other than the regulated business and therefore left with no option other than to borrow to make good the accumulated revenue gap.

(xxii) In view of the above submission, Hon'ble Commission may kindly review the decision to disallow the interest on Overdraft in its entirety and may be pleased to approve the same actually paid during the year.

II. Disallowance of Return on Equity by Rs.23.30 crore.

9. Return on equity has been approved by the Hon'ble Commission at 14% as per Regulation 20 of the KSERC (Terms and Conditions for Determination of Tariff for Distribution and Retail Sale of Electricity under MYT Framework) Regulation, 2006 against 15.50% claimed by KSEBL in the petition. In this connection, it is submitted that:

a. KSEB had filed two separate Appeal petitions before the Hon'ble APTEL against the order of the Hon'ble Commission in the matter of (1) Truing up of Accounts for 2010-11 and (2) ARR & ERC for the year 2012-13. Hon'ble APTEL had admitted these petitions as 1 of 2013 and 19 of 2013 respectively and delivered a common judgment on 10.11.2014.

b. As per paragraph 2 of judgment, Hon'ble APTEL had identified 6 issues in common, 2 issues and 5 issues specific to Appeal No. 1 and Appeal No. 19 respectively and common judgment delivered since most of the issues are common.

c. Six issues which were identified as common in both the petitions, were-Employee cost, R&M, A&G, Return on Equity, Depreciation and Capitalization of expenses.

d. On employee cost, it was ordered to true up accounts in line with the directions of the Hon'ble APTEL for the period from 2010-11 to 2013-14.

e. On depreciation, Hon'ble APTEL has granted liberty to KSEB to file the complete data as per CERC Regulations 2009 and directed the Hon'ble Commission to reconsider the same as per CERC Regulations.

f. On RoE, Hon'ble APTEL directed the Hon'ble Commission to allow RoE of 15.50% as per CERC Regulations.

g. However, Hon'ble APTEL has not intervened in the decision of the Hon'ble Commission in R&M, A&G and Capitalization of expenses.

h. Hon'ble Commission may kindly note that Hon'ble APTEL had issued specific direction to true up from 2010-11 to 2012-13 while addressing the first of common issues ie employee cost. Hon'ble

Commission has carried out truing up in respect of Employee Cost and Depreciation for all the 3 years in line with Hon'ble APTEL directions but the judgment was complied for RoE for the year 2012-13 alone but refused to apply the same for the year 2011-12. Hon'ble Commission has already made known that the additional revenue gap for 2010-11 has been provisionally determined at Rs.340 crore and this enhanced allowance invariably comprise of RoE, Depreciation and Employee cost.

i. Hon'ble APTEL, as per judgment dated 06.05.2016 and 27.04.2016 has upheld the decision on RoE for the years 2009-10 and 2013-14 also. Hence, it is clear that the decision on RoE has consistently been applied for the years 2009-10, 2010-11, 2012-13 and 2013-14.

10. In short, it is humbly submitted that, the Hon'ble APTEL, as per the following judgments, has ordered consistently to allow RoE @ 15.50% from the FY 2009-10 to 2013-14.

Table 11 Details of judgments relating to RoE

Year	Judgment No and date	RoE
2009-10	Appeal petition No. 135 of 2014, dated 6-5-2016	15.50%
2010-11	Appeal petition No. 1 of 2013, dated 10-11-2014	15.50%
2011-12	ARR order not challenged separately. However, Hon'ble APTEL vide the common judgment dated 10-11-2014 in Appeal petition No. 1 of 2013 to 19 of 2013, had directed to true up the employee cost etc from 2010-11 to 2012-13 based on the judgment dated 10-11-2014 in appeal petition No. 1 of 2013 and 19 of 2013	
2012-13	Appeal petition No. 19 of 2013 dated 10-11-2014	15.50%
2013-14	Appeal Petition No. 81 of 2014 dated 27-4-2016	15.50%

11. In view of the above, it cannot be inferred that the Hon'ble APTEL did not wanted to extend relief for 2011-12 alone among 5 years from 2009-10 to 2013-14. Hence Hon'ble Commission may kindly review the decision and may be pleased to approve RoE @15.50 for the year 2011-12.

III. Disallowance of R&M Expenses Rs.69.42 crore

12. Hon'ble Commission, while approving the R&M expenses and A&G expense as per the audited account for 2011-12, has adopted the actual R&M expenses and A&G for the year 2008-09 as the base. The 'R&M cost' and 'A&G expenses- other than section 3(1) duty' for the subsequent years is allowed to escalate at the indices of 'Whole Sale Price Index and Consumer Price Index at the weightage of 30:70.

13. The methodology adopted by the Hon'ble Commission has resulted in disallowance of considerable O&M expenses actually incurred as per the C&AG audited accounts as detailed below.

- Repair and Maintenance expenses by Rs 69.62 crore
- A&G expenses by Rs 29.31 crore.

14. The methodology adopted by the Hon'ble Commission did not consider the business growth of the utility.
    - As a utility engaged in distribution, transmission and generation, the consumer base, energy sale volume, capacity addition etc has been increasing every year.
    - The section-43 of the Electricity Act-2003 has cast upon KSEB the responsibility to provide supply to the consumers on demand. The methodology adopted by the Hon'ble Commission may prevent KSEB from fulfilling its universal supply obligations.
    - while approving the R&M expenses & A&G, expenses, Hon'ble Commission has not considered the business growth of the utility.

15. It is an accepted practice that, in the process of truing up, the State Commissions approve the actual expenses after prudence check. However, for the year 2011-12, Hon'ble Commission has not considered the actuals but merely applied inflation indices on the base value.

16. KSEB is in operation since the year 1957 and the assets created since then are still in operation. The R&M cost is allowed to the utilities to maintain its assets in good condition to provide the service to the consumers. The R&M cost depends primarily on the following.

(i) The volume of the assets in use. As a growing power utility, the Fixed Asset base of KSEB has been increasing every year and therefore higher R&M cost.

(ii) Age of the assets. As the assets become old, the R&M cost required will be high.

(iii) Susceptibility to inflation. The major components of R&M costs are the cost of the material and labour and both are highly susceptible to inflation.

17. However, the merit of the issue had been duly recognized by the Hon'ble Commission while framing the Tariff Regulations, 2014. Hon'ble Commission was pleased to factor the business growth while determining the allowable cost.

18. As per the audited accounts, the R&M cost actually incurred for the year 2011-12 was Rs 251.70 crore. However, Hon'ble Commission has approved only Rs.182.28 crore in truing up This is much less than that approved in corresponding ARR&ERC order (185 crore). It is submitted that, the R&M cost as projected in the ARR increased due to the inflation, age of assets, new assets addition etc.

19. Regarding the need for notifying specific regulations under section-61 of the Electricity Act-2003, instead of generic tariff regulation, Hon'ble Tribunal in judgment dated 7-12-2012 in Petition No.186 of 2011 between Orissa Power Transmission Corporation Limited vs Orissa Electricity Regulatory Commission & Ors has observed that:

the State Commission lays down <u>only general principles as per Section 61 of the Act for determination of transmission tariff without specifying the terms and conditions for determination of transmission tariff. (para 45)</u>
The Hon'ble Supreme Court in PTC Vs CERC (2010) 4 SCC 603 has held that this Tribunal has powers under Section 121 of the Act to direct the Commission perform its statutory function of framing the Regulations.(para 46)

Hon'ble APTEL reiterated this in its judgment in Appeal no. 110 of 2010 delivered on 19.4.2012 and directed the State Commission *to take immediate steps to <u>formulate specific Tariff Regulations for transmission of electricity in accordance with Section 181(zd) read with Section 61 of the Act."</u>*

20. It is further submitted that, while approving the truing up of accounts, the Hon'ble Commission has adopted a part of the KSERC (Terms and Conditions of Tariff for Retail Sale of Electricity) Regulations, 2006) Regulations. Hon'ble Commission had earlier admitted before the Hon'ble APTEL that, the KSERC (Terms and Conditions of Tariff for Retail Sale of Electricity) Regulations, 2006 has limited application to KSEB functioning as a single entity engaged in generation, transmission and distribution for approving its various expense components.

21. The fact being so, the approach adopted by the Hon'ble Commission for approving the expenses in the process of truing up ultimately resulted in considerable reduction of R&M expenses. Hence, KSEBL requests before the Hon'ble Commission to review the decision and to approve the R&M expenses and A&G expenses (other than section 3(1) duty) as per the C&AG audited accounts.

<u>iv.(a) Disallowance of A&G expenses other than Electricity duty Rs.29.31 crore.</u>

22. The A&G expenses (excluding duty) were Rs 109.41 crore. However, Hon'ble Commission has approved only Rs 80.10 crore and disallowed Rs 29.31 crore (26.79%)

23. Though Hon'ble Commission had considered the A&G expenses as fully controllable, expenses like rent, rates and taxes, insurance expenses, conveyance and vehicle hire charges, audit fees, legal expenses, study expenses, SRPC expenses, freight charges,

Professional charges etc are strictly not controllable considering the following.

(i) As a distribution licensee and State Transmission utilities, KSEB has to incur the SRPC expenses, legal expenses, audit fees etc.

(ii) With the networking and computerization of offices, the telephone and internet charges are on the increase every year.

(iii) KSEB as a distribution utility does not have much control on the printing and stationeries.

24. Break up of A&G expenses comprise of Administrative expenses 48%, other expenses 38% and purchase related expenses 14% Break up of Administrative expenses is detailed below:

A&G expense components which recorded increase over approval

Particulars	2008-09	2011-12	
	Actual	As per Accounts	Increase over 2008-09
Conveyance and vehicle hire charges	13.44	34.08	20.64
Other Professional charges, Technical and Consultancy charges	0.56	4.45	3.89
Audit fee	2.25	2.30	0.05
Legal charges	1.74	2.00	0.26
Rent, Rates and Taxes	3.89	5.56	1.67
Telephone and internet	3.94	3.46	-0.48
Insurance	0.50	0.41	-0.09
Total	26.34	52.25	25.91

(i) The conveyance and vehicle hire charges is a major expense component of Administrative expenses, which depends heavily on the price variation of the fuels- petrol and diesel. KSEB has been taking vehicles on hire instead of acquiring new vehicles.

(ii) Predominant portion of other professional charges (Rs.3.84 crore) has been paid to the Hon'ble Commission against corresponding negligible amount in 2008-09.

(iii) Most of the offices of KSEB are taken on rent. Legal charges and audit fee payable to C&AG along with rent, taxes and rates are un controllable.

25. Among other expenses, increase was due to advertisements as part of DSM measures. In addition KSEB has limited control over freight anf other purchase related expenses amounting to Rs.15.93 crore against Rs.11.09 crore in 2008-09.

26. Hon'ble APTEL as per judgment dated 4th September-2012 in petition filed by KSEBL in appeal petition No. 190 of 2010 had directed that.

13.5 Regarding A&G expenses for the FY 2009-10, we direct the State Commission to consider the actual A&G expenses as per the audited accounts of the Appellant in the true up and allow the same with carrying cost, after prudence check."

27. Hon’ble APTEL as per judgment in Appeal 135 of 2014 has upheld the similar view as follows:

After going through the judgment dated 04.09.2012 (supra), we dispose of this issue and direct the State Commission to consider and decide this issue as per our direction contained in para 20(vi) dealing with A&G Expenses in judgment dated 04.09.2010 in Appeal Nos. 190 of 2009 and 46 of 2010.

29. Hon’ble Commission may kindly note that the methodology provide inflationary increase over the base year expense and there are various expenses in 2011-12 and 2012-13 which were not incurred in the base year ie 2008-09. Further, certain expenses, especially statutory payments, do not necessarily move according to inflation such as payments to KSERC etc. Such payments are to be approved in full. Hon’ble Commission did not even approve the payments made by KSEBL to KSERC in line with its regulations to the tune of Rs.3.84 crore.

28. Considering the facts and submission and also considering the directions of the Hon’ble APTEL vide its judgment dated 4th September-2012 on appeal petition No. 190 of 2010, Hon’ble Commission may kindly review the decision and approve the A&G expenses as per the audited accounts for the year 2011-12.

(iv).b Disallowed section 3(1) duty Rs.93.31 crore.

29. One of the major expense items booked under A&G expense is the section 3(1) duty payable by KSEB to the Government. The section 3(1) duty is a statutory levy. While approving the ARR&ERC/ Truing up petitions for the years from 2003-04 to 2006-07, Hon’ble Commission has considered this as revenue expenditure as part of the A&G expenses of the Board. Comptroller & Auditor General (C&AG) have also certified this as an essential expenditure under A&G expenses since the inception of the Board. But, while approving the Truing Up of accounts of KSEB since the year 2003-04 and also while approving the orders on ARR since the year 2007-08, Hon’ble Commission has not been admitting section 3(1) duty as a revenue expenditure quoting the provisions in the “Kerala Electricity Duty Act- 1963” that “(3) The duty under this section on the sales of energy should be borne by the Licensee and shall not be passed on to the consumers”. Accordingly, since the year 2003-04, Hon’ble Commission has not admitted duty aggregating to Rs 748.47 crore so far and the details are given below.

Table 12 Section 3(1) Duty not admitted

Year	Section 3(1) duty not admitted by KSERC (Rs. in crore)
2003-04	51.53
2004-05	54.98
2005-06	63.26
2006-07	71.78
2007-08	77.54
2008-09	74.47
2009-10	80.79
2010-11	84.42
2011-12	93.31
2012-13	96.97
Total	749.15

30. The regulatory practice mandates allowance of an expense if incurred prudently. Hon'ble Commission may be aware that, KSEB has no business other than the regulated business of electricity distribution. KSEB cannot find an alternate means to meet this expense. KSEBL has always felt that disallowing section 3(1) duty is against the provision of the Electricity Act-2003 that, SERC's should have to ensure reasonable return to the utilities after meeting expenses including taxes and duties. If the section 3(1) duty is not allowed as an expense, the commercial viability of the utility will be affected. Hon'ble Commission may have the option to allow higher return to KSEB so that the net return after meeting section 3(1) duty shall be 15.50 % of the equity. As per the provisions of the Electricity Act-2003, Hon'ble Commission is empowered to ensure financial sustainability of KSEBL as a Distribution Utility and with the statutory powers available; the matter of disallowance of section 3(1) duty is being raised again for reconsideration.

31. KSEB has raised this matter before the Hon'ble Supreme Court of India, which is pending disposal as of date.

(v) Disallowed the Depreciation by Rs 135.40 crore for the FY 2011-12.

32. Hon'ble Commission may kindly note that KSEBL as per its submission has worked out gross depreciation as per CERC rates with due regard to the age of asset after excluding depreciation on consumer contribution applicable for the creation of fixed assets. However, Hon'ble Commission has ordered to disallow depreciation attributable to OYEC charges also, which may kindly be reviewed.

(vi) Disallowance of employee cost

33. Hon'ble APTEL in the judgment in Appeal No. 1 and 19 of 2013 has directed the Hon'ble Commission as follows:

We direct the State Commission to true up the employees cost from FY 2010-11 to FY 2012-13 as per the directions given in paragraphs 8.5 and 8.6.

> *8.5 We find that the State Commission has taken the actual expenses trued-up for FY 2008-09 as the base. The State Commission should have at least allowed the actual basic pay and DA increase, pay revision and terminal benefits over the actual base year expenses without accounting for increase in manpower from 2008-09 to 2012-13.*

34. However, Hon'ble Commission has restricted employee cost attributable to the staff strength as on 31.03.2009 without allowing any allowance towards the requirement of additional man power owing to the growth in business. Hon'ble Commission may kindly note that the expenses disallowed on enhanced working strength constitute 4.25% of the employee cost for the year , which is reasonable with regard to the business growth during the period of 3 years from 01.04.2009 to 31.03.2012. Hence the employee cost may kindly be approved in full.

(vii) Treatment of revenue deficit.

35. Hon'ble Commission has determined the revenue gap for the year but the order is silent as to the treatment of approved revenue gap. It is humbly requested that the Hon'ble Commission may specify the same.

Prayer

Considering the reasons, facts and circumstances on the matters as detailed in the paragraphs above, KSEBL requests before the Hon'ble Commission to kindly review the order dated 16th March 2017 in Petition OA No. 9 of 2016 in the matter of 'Truing Up of accounts of KSEB for the year 2011-12 on the items as detailed above in the petition.

Chief Engineer (Commercial & Tariff)