

Ministry of Power

Development of Large Size “Ultra Mega Projects”

Section 63 of the Electricity Act, 2003 provides that the Regulatory Commissions shall adopt the tariff if it is determined through transparent process of bidding accordance with the guidelines issued by the Central Government. This aims at moving away from cost plus support for tariff determination and it is expected to further encourage private sector investment.

Guidelines for competitive bidding for determination of tariff for procurement of power by distribution licensees were issued on 19th January, 2005. Main objectives of these guidelines are promoting competitive procurement, facilitating transparency and fairness, reducing information asymmetry, protecting and finally providing flexibility to suppliers on availability of power while ensuring certainty on tariffs for buyers.

2. Provisions of the National Electricity Policy

One of the issues sought to be addressed by the policy is ‘Competition aimed at Consumer Benefits’. The policy recognizes that competition will bring significant benefits to consumers, in which case, it is competition which will determine the price rather than any cost plus exercise on the basis of operating norms and parameters. The policy stipulates that all efforts will need to be made to bring the power industry to this situation as early as possible, in the overall interest of consumers.

3. Provisions of Electricity Tariff Policy

One of the main objectives of the tariff policy is to promote competition, efficiency in operations and improvement in quality of supply. The policy mentions that introducing competition in different segments of the electricity industry is one of the key features of the Electricity Act, 2003 and that competition will lead to significant benefits to consumers through reduction in capital costs and also efficiency of operations. It will also facilitate the price to be determined competitively.

The policy stipulates that all future requirement of power needs to be procured competitively by distribution licensees except in cases of expansion of existing projects or where there is a State controlled/ owned company as an identified developer and where regulators will need to resort to tariff determination based on norms. Even PSUs will have to bid for projects for determination of tariff after a transition period of 5 years.

4. Launch of Ultra Mega Projects through tariff based competitive bidding

Recognizing the fact that economies of scale leading to cheaper power can be secured through development of large size power projects using latest super critical technologies, Ministry of Power, CEA and Power Finance Corporation are working in tandem for development of five projects under tariff based competitive bidding route. The Ultra Mega Power Projects with each having a capacity of 4, 000 MW, would also have scope for expansion in future as well. The size of these projects being large, they will meet the power needs of a number of states through transmission of power on regional and national grids. In the last six months several rounds of discussions were held with states and a number of them, independent of this initiative, would facilitate state specific projects in the range of 1000-2000 MW through competition on similar lines.

In order to enhance investor confidence, reduce risk perception and get a good response to competitive bidding, it was deemed necessary to provide the site, fuel linkage in captive mining blocks, water and obtain environment and forests clearance, substantial progress on land acquisition leading to possession of land, through a Shell Company. In addition, shell companies would also be responsible for tying up necessary inputs from the likely buyers of power and also appropriate terms and conditions with Utilities and Payment Security Mechanism.

In the first phase, two projects at pit head site and three projects at coastal locations have been identified for development of Ultra Mega Projects. Government approval has already been accorded on 16th January, 2006 for setting up of following five shell companies under the Article No.86 of Articles of Power Finance Corporation :-

- (i) Sasan Power Limited (M.P)
- (ii) Akaltara Power Limited (C.G)
- (iii) Coastal Gujarat Power Limited
- (iv) Coastal Karnataka Power Limited
- (v) Maharashtra Ultra Mega Power Project Co.

On the basis of this approval, Power Finance Corporation has submitted necessary papers to Registrar of Companies for the registration of the suggested names on 17th January, 2006. It is expected that approval of Registrar of Companies with regard to availability of names would be available by 23rd January, 2006. Simultaneously, for appointment of Technical Consultants, bids have been invited, which would be opened on 24th January, 2006. The Technical Consultants for at least two sites will be appointed by 31.1.2006. They will prepare Project Report and Report on Environment Impact Assessment.

5. Functions of the Shell Companies

- (a) Preparation of Project Report
- (b) Land acquisition

- (c) Allocation of fuel linkages/ coal blocks
- (d) Allocation of water by the State Govt.
- (e) Appointment of consultants for Environment Impact Assessment & Project Report
- (f) Appointment of consultants for international bid (ICB) document preparation & evaluation.
- (g) Various approvals and statutory clearances.
- (h) Off-take/ sale of power – Section 63 of EA 2003 provisions
- (i) Power Evacuation System, Load Flow Study, Grid Tolerance/ System Stability with new capacity addition.

6. Payment security mechanism would consist of :

- (a) Revolving Letter of Credit by distribution licensees;
- (b) Escrow account establishing irrevocable claims of receivables of distribution utility;
- (c) In a likely event of any default, direct supply to HT consumers or any other more credible distribution licensees as per the provisions of Electricity Act, 2003.

7. Time Schedule

The requisite manpower required for making shell companies operative is already in place. It is envisaged that Expression of interests for pre-qualification would be issued for each of the five projects between last week of January and second week of February, 2006. The Road Map of critical milestones has been identified as follows :-

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| (a) | Expression of Interest | - | January '06/Feb'06* |
| (b) | Selection of qualified bidders | - | March, 2006 |
| (c) | Issue of bid document (RFQ) | - | 1-April, 2006 |
| (d) | Closing date for receipt of final bid | - | September, 2006 |
| (e) | Selection of successful bidder | - | December, 2006 |
| (f) | Transfer of projects of Shell Company to the selected bidder. | - | December, 2006 |

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| * For two sites | - | January, 2006 |
| For three sites | - | February, 2006 |

8. Funds requirement

The Ultra Mega Projects being developed on super critical technology would entail substantial investment to the tune of Rs.15,000 crores for each project. From the initial rounds of discussions held with the financial institutions, it emerged that for good and credible developers and for power projects offering less expensive power debt funding may not emerge as a constraint at all. To keep the financial institutions update about the developments in setting up of Ultra Mega Projects, FIs are being involved at

various stages including the final evaluation of the bids. However, development of these large projects would have to have the involvement of large private business groups in our country, who either on their own or through consortiums with parties and agencies from outside could take implementation of these projects.

9. Discussions with Heads of Financial Institutions

In order that there is full support of the financial world on the concept and during implementation of these large size projects, as also with a view to inviting their suggestions as to how to make this initiative succeed, a meeting of the Heads of Financial Institutions was organized on 6th January, 2006. Chairman, SBI, Chairman, LIC, CMD, IDBI, CMD, HDFC/IDFC, Executive Director of ICICI, CMD, PFC, besides many other senior officers of Financial Institutions and banks participated. They fully supported this initiative and made valuable suggestions. These include the following :

- ▶ For good projects with competitive Tariff and credible developer, funds will not be a constraint.
- ▶ The proposed payment security mechanism is adequate.
- ▶ F.I. representation in Pre-Qualification Committee.
- ▶ Rating of Green Field Projects for better terms of funding
- ▶ Publicise globally
- ▶ Involvement of F.I. in selection of Consultant for Project Report
- ▶ Activating Bond Market
- ▶ Access ECB (Present limit to be liberalized)
- ▶ 20 year debt tenure {12+8 (LIC)}
- ▶ Attracting Venture Capital

10. Discussions with Top Industry Leaders

The scheme was discussed in detail with the Finance Minister and at his suggestion, an interaction was organized with the top industry leaders on 13th January, 2006. The response was overwhelming. They also made valuable suggestions which include the following :

- a. Granting mega power status to these projects even though they do not need access to the Central Plan devolution in the payment security mechanism package. In fact, this condition should be deleted from the conditions of mega project scheme because this condition was provided in early days when the system of guarantee was being taken away. Lenders and developers are now convinced that with the changes that have happened in the wake of Electricity Act, 2003, this condition is not necessary to be included for concession under the mega power policy.
- b. There should be full State Govt. support so that facilitation like land acquisition, water availability etc., consent of State Pollution Control Board etc. are available to Shell Companies/Project Developers.

- c. Since these are large projects, each involving a capital expenditure of the order of Rs.15,000 crores, the sectoral capping and the group capping for the purpose of debt financing, as notified by the RBI, will need to be revisited and properly enhanced.
- d. The present expectation of the lenders that debt : equity ratio should be 70:30 may also need to be revisited and the proportion of the debt could be enhanced because otherwise, this could entail much larger amount of equity to be raised by the developers.
- e. Ministry of Power should ensure that power evacuation and transmission system is put in place in time and there should also be sufficient redundancy in the system so that the advantages of Open Access in transmission and distribution is fully availed of.
- f. It is good that the pit-head power stations are being provided captive coal blocks rather than linkage. Even for such future projects, the same arrangement should continue.
- g. The criteria for evaluation of bids should be comprehensively formulated by the Shell Company on the basis of advice of consultants so that there is no ambiguity and once the bidders have been pre-qualified the commercial consideration like tariff should be the sole criterion for selection.
- h. Long Term debt and take out financing would be useful and render better tariff.
- i. 80 1A benefit under Income Tax Act should be extended.

11. Meeting with States

Right at the initial stage, the Chief Secretaries of the states have been kept apprised of the above initiative with the request that during the initial phase of these projects, for the purpose of investigation etc., necessary support should be provided to the Shell Companies and to CEA and other agencies. Now, after the inputs have been received from the FIs and from the industry leaders, meetings have been organized with each of these states on 25th and 27th January, 2006 so as to discuss the specific issues which will need to be attended to. Similarly, meetings have been planned with all the states which are likely to be the buyers of power of these plants so that the broad framework of the Power Purchase Agreement with mutual rights and obligations are properly structured.