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DRAFT ELECTRICITY (AMENDMENT) BILL, 2020

Relevant for: Indian Economy | Topic: Infrastructure: Energy incl. Renewable & Non-renewable

Highlights of the Draft Bill

- The Bill provides for the constitution of Electricity Contract Enforcement Authority (ECEA). The ECEA will have sole authority to adjudicate upon specified contract-related disputes in the electricity sector.

- A common selection committee will be constituted to select the chairperson and members of the Appellate Tribunal (APTEL), the central and state regulatory commissions (CERC, SERCs), and ECEA.

- Currently, SERCs are required to specify regulations to progressively reduce cross-subsidy. The Bill requires them to adhere to the National Electricity Tariff Policy while determining the cross-subsidy.

- Government subsidy will not be accounted for while determining the tariff. Such subsidy will be provided directly to consumers.

- The Bill adds that a franchisee will be authorised with the information given to the SERC. The Bill provides for a new entity called Distribution Sub-licensee. A distribution licensee can authorise a sub-licensee to distribute electricity on its behalf with the prior permission of the SERC.

- State and regional load despatch centres will not schedule or despatch electricity if the distribution licensee has not provided adequate payment security, as agreed in the contract.

- The Bill empowers the central government to notify a National Renewable Energy Policy in consultation with state governments and prescribe minimum renewable and hydro purchase obligation.

Key Issues and Analysis

- The proposed common selection committee will have chief secretaries of two states as members, by rotation. A concerned state may not have a representative in the committee when recommending appointments to its SERC. The question is whether this undermines a state's powers to appoint its regulator.

- The proposed selection committee will also recommend appointments to the Appellate Tribunal. The composition of the proposed selection committee is contrary to the principles laid out by the Supreme Court to safeguard the independence of tribunals.

- The Draft Bill requires the SERCs to adhere to the National Electricity Tariff Policy for determining cross-subsidy. The question is whether matters of cross-subsidy should be determined by a uniform National Policy or continue to be determined by the SERCs.

- A distribution licensee can authorise a franchisee as well as a distribution sub-licensee to distribute electricity on its behalf. There is a need for clarity on the role of a franchisee and a distribution sub-licensee.

PART A: HIGHLIGHTS OF THE DRAFT BILL

Context

The electricity sector could be classified into three segments: generation, transmission, and distribution. Generation is the process of producing power using different sources of energy. High voltage power is carried from the generation plants to the distribution sub-stations through a transmission grid. Electricity is finally transferred from the sub-stations to individual consumers through a distribution network. The Electricity Act, 2003 is the central law regulating the electricity sector.[1] The Act provides for Electricity Regulatory Commissions at both the central and state levels (CERC and SERCs). Functions of these Commissions include: (i) regulating and determining tariff, (ii) issuing licenses for transmission, distribution, and electricity trading, and (iii) adjudicating upon disputes, within their respective jurisdiction.

One of the key concerns in the power sector has been the financial health of the distribution companies (discoms), which are mostly state-owned. Discoms have had a high level of debt and have been running losses for the past several years.[2] The Ujwal Discom Assurance Yojana (UDAY) was launched in 2015 to bring financial and operational turnaround of discoms. Under UDAY, 15 states took over debt of their discoms worth Rs 2.1 lakh crore.2 However, the losses of distribution utilities have increased by 69% between 2017-18 (Rs 29,452 crore) and 2018-19 (Rs 49,623 crore).[3]

Underpricing of tariff, and high technical and commercial losses (including theft and billing issues) are some of the major reasons for financial issues of the discoms.[4] Currently, the state-owned discoms, on average, make a loss of Rs 0.41 for every unit of power supplied.[5] The overdue payment to generation companies has also increased (from Rs 57,352 crore in March 2019 to Rs 94,598 in March 2020), indicating financial stress in some discoms.[6] Moreover, in March 2018, the regulatory assets[*] of discoms were Rs 34,526 crore, which is a 16% increase from March 2017 (Rs 29,103 crore).[7] Delay in the release of government subsidy also adversely impacts the liquidity of discoms contributing to their financial crisis.4

In 2014, a Bill to amend the 2003 Act was introduced in Lok Sabha but lapsed with the dissolution of 16th Lok Sabha. The 2014 Bill sought to: (i) increase competition in the sector by segregating the distribution segment into distribution and supply, (ii) rationalise tariff determination, and (iii) promote renewable energy. The Bill was examined by the Standing Committee on Energy (Chair: Dr Kirit Somaiya). In 2018, based on the Committee's recommendations and other stakeholder consultations, the Ministry proposed draft amendments to the 2003 Act. The Draft Amendments sought to: (i) introduce direct benefit transfer mechanism for the transfer of subsidy directly to consumers, and (ii) define renewable generation and purchase obligations, among others. In April 2020, the Ministry of Power released the Draft Electricity (Amendment) Bill, 2020 proposing amendments to the 2003 Act.[8] As per the Ministry, the Draft Bill seeks to address critical issues which have weakened commercial and investment activities in the electricity sector.8

Key Features

- **Electricity Contract Enforcement Authority: The Draft Bill sets up the Electricity Contract Enforcement Authority (ECEA). ECEA will consist of: (i) a chairperson, (ii) two or more judicial members, and (iii) three or more technical members. ECEA may**

have multiple benches, and every bench must have at least one judicial member and one technical member. ECEA will adjudicate on matters involving the performance of contracts regarding the purchase, sale, or transmission of electricity between a generation company and other licensees. It will not adjudicate over any matter related to regulation or determination of tariff, or any dispute involving tariff. Such matters will continue to be adjudicated by concerned SERCs and CERC.

- **Common selection committee to recommend appointments: The Act provides for a selection committee in each state to recommend appointments to the respective SERC, and separate committees to recommend appointments to CERC and the Appellate Tribunal for Electricity (APTEL). The Draft Bill proposes a common selection committee to recommend appointments to all SERCs, CERC, APTEL, and ECEA.**

- **Cost-reflective tariff: The Act provides that the tariff for the retail sale of electricity should progressively reflect the cost of supply. The Draft Bill amends this to require that tariff must reflect the cost of supply.**

- **Government subsidy: The Act provides that the state governments may provide subsidy to consumers. The Draft Bill requires that tariff for the retail sale of electricity must be determined without accounting for the government subsidy. The Act provides that state governments must pay the subsidy in advance to the distribution licensee or any other person concerned to implement the subsidy. The Draft Bill removes this provision and requires that subsidy must be provided directly to consumers.**

- **Regulation of cross-subsidy: The Act requires the cross-subsidy in tariff to be reduced progressively. The Act empowers the regulatory commissions to make regulations regarding the manner of reduction of cross-subsidy. The Draft Bill removes the powers of the regulatory commissions to make these regulations. It requires that cross-subsidy should be reduced in the manner provided in the National Electricity Tariff Policy prescribed by the central government.**

- **Sub-contracting of power distribution activities: The Act empowers a distribution licensee to authorise a Franchisee to distribute electricity on its behalf. The Draft Bill adds that a Franchisee will be appointed with the information given to the SERC. The Draft Bill also introduces another entity named Distribution Sub-Licensee which can be authorised by a distribution licensee to distribute electricity on its behalf. Prior permission of SERC will be required for authorising a Sub-Licensee. No separate license will be required for operating as either a Franchisee or a Distribution Sub-licensee.**

- **Functions of National Load Despatch Centre (NLDC): The Act provides for load despatch centres at state, regional, and national level. The load despatch centres are responsible for optimum scheduling and despatch of electricity in their respective jurisdiction. Under the Act, the central government is empowered to prescribe the functions of NLDC. The Draft Bill adds that functions of the NLDC will include: (i) monitoring of grid operations, (ii) exercising supervision and control over inter-**

regional and interstate transmission network, and (iii) carrying out real-time operations of the national grid.

- The Bill also empowers NLDC to issue directions for ensuring the stability of grid operation and safety and security of the national grid. Such directions will be binding on various entities involved in the operation of power systems including generators, and regional and state load despatch centres.

- **Payment Security Mechanism: As per the Act, the regional and state load despatch centres (RLDCs and SLDCs) are responsible for scheduling and despatch of electricity from the generator to the distribution licensee. The Draft Bill adds that the supply agreement between a generator and a distribution licensee may require adequate payment security. The Bill prohibits the RLDCs and SLDCs from dispatching electricity if adequate payment security, as agreed in the contract, has not been provided by the distribution licensee.**

- **National Renewable Energy Policy: The Draft Bill empowers the central government to formulate a National Renewable Energy Policy in consultation with state governments. The policy will be aimed at promoting renewable sources of energy. The central government may prescribe a minimum percentage of purchase of electricity from renewable and hydro sources of energy.**

- **Renewable Purchase Obligation: The Act empowers the SERCs to mandate a percentage of electricity purchase from renewable sources known as Renewable Purchase Obligation (RPO). The Draft Bill adds that SERCs will specify RPO as may be prescribed by the central government. The Draft Bill also provides for certain penalties for non-compliance by licensees in meeting RPO.**

PART B: KEY ISSUES AND ANALYSIS

Selection Committee for Regulatory Commissions, ECEA, and APTEL

Electricity is a subject in the concurrent list of the Constitution.[9] The Electricity Act, 2003 created independent regulators at the state and central level. As per the Act, each state has a selection committee for the respective SERC. There are separate selection committees for CERC and Appellate Tribunal (APTEL). The Draft Bill proposes a common selection committee for CERC, SERCs, APTEL, and the Electricity Contract Enforcement Authority (ECEA). This raises a few questions on the composition of the proposed selection committee.

Composition of the selection committee may undermine states' powers to appoint its regulator

Currently, the SERC selection committee has the Chief Secretary of the respective state as a member (Table 1). The proposed common selection committee includes chief secretaries of two states as members, by annual rotation (alphabetically). This implies that a concerned state may not have a representative in the selection committee when selecting members of the state's regulator. The question is whether this undermines a state's powers to appoint its regulator.

Table 1: Comparison of the composition of selection committees for SERCs under the

Act with the Proposed Selection Committee under the Draft Bill

Selection Committee for SERCs under the Electricity Act, 2003	Common Selection Committee for SERCs, CERC, APTEL, and ECEA under the Draft Bill
- Chairperson: former Judge of the High Court.	- Chairperson: a retired or current Supreme Court Judge.
- Other members include: (i) Chief Secretary of the concerned state, and (ii) chairperson of Central Electricity Authority or chairperson of CERC.	- Other members: (i) Secretary of the Ministry of Power, (ii), Chief Secretaries of two states on a rolling basis for one year, and (iii) Secretary of a Ministry to be nominated by the central government.

Sources: The Electricity Act, 2003; The Draft Electricity (Amendment) Bill, 2020; PRS.

Composition of selection committee may be contrary to the principles laid out by the Supreme Court

The selection committee proposed by the Draft Bill will also be responsible for recommending appointments to the APTEL. The proposed Selection Committee comprises one judicial member and four executive members. This is contrary to the principles laid out by the Supreme Court to safeguard the independence of a statutory Tribunal like the APTEL.

The Supreme Court has held that any search-cum-selection committee mainly consisting of executive members will lead to excessive interference of the Executive in the appointment of members of Tribunals.[10] The Court further added that it would be detrimental to the independence of judiciary besides being an affront to the doctrine of separation of powers.10

Moreover, the Finance Act, 2017 provides for uniform processes for various tribunals including the APTEL.[11] The Draft Bill proposes a selection committee for the APTEL, different from the one in the Rules issued under the Finance Act, 2017 (Table 2).[12] These Rules have also been challenged in the Supreme Court for not adhering to the principles of separation of powers and independence of the judiciary.[13]

Table 2: Comparison of Selection Committee for recommending appointments to the APTEL

As per the 2020 Rules under Finance Act, 2017	As per the Draft Electricity (Amendment) Bill, 2020
Chairperson: Chief Justice of India or a judge of the Supreme Court nominated by the Chief Justice of India	Chairperson: A sitting or former judge of the Supreme Court nominated by the Chief Justice of India
Members:	Members:
- APTEL Chairperson[†]	- Union Power Secretary
- Union Power Secretary	- Another central government Secretary
- Union Petroleum Secretary	- Chief Secretaries of two state governments in rotation

Sources: The Draft Electricity (Amendment) Bill, 2020; The Tribunal, Appellate Tribunal, and

other Authorities (Qualifications, Experience, and Other Conditions of Service of Members) Rules, 2020; PRS.

National Policy may not address state-level variations in cross-subsidy

The Act empowers SERCs to determine the retail tariff for electricity and make regulations on tariff-related matters. This includes regulating the manner of reduction of cross-subsidy and determining such cross-subsidy. The Draft Bill: (i) removes the SERCs' powers to make regulations regarding the manner of reduction of cross-subsidy, and (ii) requires them to adhere to the National Electricity Tariff Policy for determining cross-subsidy. The Statement of Objects and Reasons of the Draft Bill notes that tariff determined by SERCs has not been cost-reflective and has resulted in the weakening of the financial health of discoms. The question is whether cross-subsidies in tariff should be determined by the state regulator or be based on a national policy.

When deciding the reduction of cross-subsidy, SERCs may account for various factors. These include consumer mix, sale projections of electricity, power procurement mix, and cost of power procurement and supply. These factors vary significantly from state to state. Such variations across states may not be adequately captured in the National Policy.

Note that the Electricity (Amendment) Bill, 2014 (that lapsed with the dissolution of 16th Lok Sabha) sought to make it mandatory for SERCs to adhere to the National Tariff Policy in all matters of tariff determination.[14],[15] The Standing Committee on Energy (2014) examining the Bill recommended that this provision should be modified to give due autonomy to states to act within the broad framework of the National Tariff Policy given the federal structure of the country.15 The Committee added that a rigid and uniform approach for determination of tariff may not be as beneficial as ground realities such as availability of raw material, manpower, and other essential inputs may vary from state to state.

Need for clarity in the role of distribution sub-licensee and franchisee

The Act provides that the distribution licensee may authorise a Franchisee to distribute electricity on its behalf in a particular area within its area of supply. The Draft Bill adds that a discom can authorise a Franchisee, and inform the SERC. The Draft Bill introduces a new entity named Distribution Sub-licensee which can also be authorised by the distribution licensee for distributing electricity on its behalf. Unlike a franchisee, prior permission of SERC will be required to authorise a sub-licensee. The functions of Franchisee and Distribution Sub-licensee are the same; hence, the question is whether there is a need for two separate entities under the law to serve the same purpose.

The Draft Bill also provides that no separate license will be required for either sub-licensee or franchisee. Further, prior permission of SERC is not required for authorising a franchisee. The Standing Committee on Energy (2014-15) while examining the Electricity (Amendment) Bill, 2014 had observed that as franchisees are free from seeking any permission from appropriate bodies, their accountability may not be ensured.15 It suggested that franchisees must be held accountable since they interact with consumers directly.15

Transfer of government subsidy directly to consumers

The Act provides that state governments may subsidise retail consumption of electricity. However, it does not explicitly specify the manner of accounting for such subsidy in the tariff determination process.[8] Typically, the tariffs charged to the consumers are lowered to the extent of the subsidy provided by the government to the state discoms. The Draft Bill requires

that government subsidy will not be accounted for while determining tariff. It introduces a Direct Benefit Transfer (DBT) system under which state governments will pay the subsidy directly to the consumers.

DBT system in electricity can help improve accountability, reduce delays, and deliver subsidy to consumers more efficiently.4 It is expected to provide following benefits: (i) better targeting of subsidy to actual consumption, therefore reducing power theft or losses, (ii) improvement in the segmentation of consumers based on consumption rather than based on consumer category, and (iii) encouraging efficient utilisation of electricity by subsidised consumers otherwise they would move out of the subsidised slabs.4 However, implementing DBT could throw some challenges such as:

- Typically, the electricity connection is in the name of the owner of the house, agricultural land, shop, or establishment. However, the consumer may be a tenant renting that place. Hence, the DBT system may be required to identify the actual user of electricity in such cases as the beneficiary of subsidy.

- If the subsidy is to be based on the amount of electricity consumed, the measurement of such consumption will be necessary. However, 100% metering is yet to be achieved for certain categories of consumers.4,7 For example, the Maharashtra State Electricity Distribution Company Limited (MSEDCL) was estimated to have around 15 lakh unmetered agricultural consumers (37.5% of the total agricultural consumers) as of March 2018.[16] Around 1.33 lakh agricultural consumers were surveyed as part of the study and it was found that only 39% of consumers reported having a metered connection (against ~65% as per official records). Further, only 17% of these consumers actually had meters installed.16

- While the Act requires state governments to pay subsidy in advance, in many instances, disbursement of subsidy by governments to discoms has been delayed.4 If such delays were to happen in the DBT system, it will adversely impact the ability of low-income consumers to pay bills on time. For instance, the average monthly power bill for a farmer using a tubewell for farming could be around Rs 3,000-5,000. This could be a significant amount for a small farmer, who may be currently getting electricity for free.

Renewable Generation Obligation has not been defined

The Draft Bill empowers the central government to make rules on the Renewable Generation Obligation. However, Renewable Generation Obligation has not been defined in the Act or the Draft Bill.

[*] Regulatory asset refers to the unrealised revenues of discoms which are to be recovered from consumers but are not charged with immediate tariff hikes to avoid economic instability among them.

[†] The chairperson of the APTEL is a sitting or former Supreme Court Judge or High Court Chief Justice.

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