

BSES

BSES Rajdhani Power Limited

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Ref no: RA/2010-11/01/E/65

July 19, 2010

To,
The Secretary,
Delhi Electricity Regulatory Commission,
Shivalik, Malviya Nagar,
New Delhi -110017.

Sir,

Sub: Factual position vis-à-vis representation given by BSES Rajdhani Power Ltd. to the GoNCTD on May 03, 2010

**Ref: 1. F.11 (570)/DERC/2010-11/2492 dated 28.05.2010 ("Letter 1")
2. Our letter no. RA/2010-11/01/E/34 dated 03.06.2010 ("Response 1")
3. F.11(570)/DERC/2010-11/C.F.No.2293/ dated 21.06.2010 ("Letter 2")**

This is with reference to the letter dated 21.06.2010 from the Director (Tariff) of the Delhi Electricity Regulatory Commission (hereinafter "**Commission**") being letter No. F.11(570)/DERC/2010-11/C.F.No.2293, (hereinafter "**Letter 2/letter under reply**"). At the outset, M/s BSES Rajdhani Power Limited (hereinafter "**Licensee**") has the following to submit:

1. The Licensee most respectfully submits that it is one amongst the three privatized distribution utilities of Delhi which is an embodiment of successful public-private partnership between the Government of National Capital Territory of Delhi (hereinafter "**GoNCTD**") and companies of International repute with the GoNCTD having a 49% shareholding in the Licensee. Further, as a result of the significant shareholding of the GoNCTD in the Licensee, the Board of Directors (hereinafter "**Board**") of the Licensee also comprises of directors nominated by GoNCTD from amongst the top bureaucrats and experts. In fact, as on date the

Page 1 of 15



Board of the Licensee has more number of Directors appointed by the GoNCTD. The Licensee states that it observes strict principles of good corporate governance and is managed, supervised and guided by the Board which inter alia includes eminent persons who are well qualified with extra-ordinary management skills and who are highly respected in the country.

2. In a short span after unbundling of the erstwhile Delhi Vidyut Board, the Licensee has been able to achieve excellence in its operations, significant reduction in the distribution losses, and has brought about several technical interventions for system strengthening and augmentation thus achieving significant reduction in number and duration of interruptions in power supply to the consumers
3. Financial statements and books of accounts of the Licensee are audited by a reputed auditing firm with an experience of over 50 years in the country and recognized by The Institute of Chartered Accountants of India. Our auditors are also empanelled with various Regulatory bodies like RBI, SEBI, CAG etc.
4. The Licensee submits that the Hon'ble Commission has in the letter under reply doubted the veracity of figures submitted to the Government. It may be noted that representation made by the Licensee before the Government was on the basis of facts and figures duly audited by the statutory auditors and approved by the Board. It needs to be highlighted that a four tier system of auditing / review is followed by the Licensee which includes:
 - a. Internal Audit by Auditors nominated by the Board;
 - b. Statutory Audit
 - c. Review by the Board nominated Audit Committee
 - d. Final approval by the Board of Directors.
5. Unfortunately, the letter under reply, by alleging that facts and figures has not presented true and fair position before the Government and has tried to mislead the Government, has implicitly questioned the integrity of the renowned members of the Board and their professional skills and ability of the statutory auditors.
6. The Licensee submits that it is indeed disappointed that the Commission, being a sectoral regulator is not able to appreciate the financial crisis that the Licensee finds itself today in. It is submitted that the Commission, ought to have

- interpreted the audited accounts of the Licensee in correct perspective by reading the documents as a whole as well as understanding its true and correct import in accordance with the Generally Accepted Accounting Principles (hereinafter “**GAAP**”). The Licensee regrets that the Commission has either not considered or has selectively considered the elaborate submissions on all the issues raised by the Commission on the audited accounts of the Licensee as well as the Report of its credit rating agency and other documents.
7. The Licensee submits that if a non cost reflective tariff, based on an insufficient and incorrect reading of the cash situation and the audited accounts of the Licensee is passed in the forthcoming Tariff Order, the same would adversely affect the Licensee, its consumers and the sector as a whole.
 8. The Licensee submits that today its financial health is very much contingent on a suitable cost reflective tariff, which may not be forthcoming unless the issues raised by it are addressed in their entirety. The Licensee would also like to place on record that it is witnessing a consistent denial of its rightful claims on unreasonable and incorrect grounds by the Commission. These actions are incorrect and show complete disregard to the factual position of the Licensee.
 9. Further, all the returns and incentive towards overachievement of operating targets which the Licensee is entitled under law and specially as a part of the Policy Directions of the Government and/or MYT Regulations, have been denied to it through inadequate cash inflow by setting a non cost reflective tariff.
 10. Moreover, even though the Profit and Loss statement for FY 2009-10, on the basis of accrual accounting, reflects profits because the Licensee has accounted for an **income recoverable from future tariff** aggregating to Rs. 827 crores, the Licensee is undeniably in severe liquidity crunch as is clearly evident from the cash flow statement attached as a part of the financial statements and which has to be read together with Balance Sheet and the Profit and Loss account. It is submitted that the Licensee is continuing to resort to heavy borrowings not only for its Capital Expenditure but also largely to sustain its operations and to service its debt obligations because the Tariff Orders issued by the Commission do not reflect cost. This fact of non cost reflective tariff has also been held out in the

various orders of the Appellate Tribunal for Electricity. In absence of a cost reflective tariff, the Licensee has had to resort to borrowings to sustain its operations. The status of cash flow will be very simple to understand from an overview of all the financial statements read together (Financial statements collectively includes Balance Sheet, Profit & Loss Statement and Cash Flow Statement read along-with Accounting policies and Notes to accounts). The Licensee once again reiterates that its precarious financial position is being consistently overlooked and ignored by the Commission which would clearly lead to damaging consequences. Further, the Licensee submits that a matter, which is so serious for the Licensee's survival, is being dealt with very casually by the Hon'ble Commission. This Licensee fails to understand as to why the Hon'ble Commission is not appreciating the simple fact that the Licensee is today cash starved and continuously resorting to borrowing to fund its operational requirements. The Licensee would also like to point out that if the liquidity crunch being faced by the Licensee is not adequately taken care of by an appropriate increase in tariff, the Licensee may not be in a position to fulfill its obligation to supply continuous power on account of its financial inability and consequently should not be held liable for the same.

11. The Commission ought to appreciate that the financial health of the Licensee is not only reflected by book profits but is also critically dependent on its liquidity position. This is a fundamental aspect of financial management and the Licensee fails to understand as to how this simple financial management proposition has escaped the understanding of the Commission's present consultants, which includes a well reputed Chartered Accountancy firm. The Licensee, therefore, urges the Hon'ble Commission to seek external expert advice either from another reputed Chartered Accountancy firm or through a merchant banker.

In response to factual allegations contained in the letter under reply, the para wise response is as follows:

Query a) That the Licensee in its letter number RA/2010-11/01/E/34 dated 03.06.2010 (hereinafter “Response 1”) has not pointed out any discrepancies and has thus confirmed that the financial position as reflected in the audited accounts and the report of the Credit Rating Agency are correct.

The Licensee vide **Response 1** had categorically and comprehensively denied the allegations of misrepresentation and/or attempts to mislead the GoNCTD or this Commission. The Licensee had vide its **Response 1** also asserted that the contents of the **Letter 1** of the Commission are based on a selective and incorrect reading of the contents of the Licensee’s Representation to GoNCTD, Audited Accounts of the Licensee and the Letter of its Credit Rating Agency dated May 22, 2009 and March 25, 2010 respectively (hereinafter “**Report**”), thereby completely negating both the contents and the conclusion reached by the Commission in **Letter 1**. The Licensee had also pointed out that whilst selectively picking the contents of the aforementioned documents, the Commission has completely ignored the context in which the Representation to GoNCTD (being a Joint Venture partner) was made by the Licensee as well as the sectoral and regulatory realities in Delhi.

Further, the Licensee had strongly denied the correctness of the conclusions drawn by the Commission with respect to the “important points” as the same are either misleading or are a result of comparing two unequals (the years compared are not comparable). For instance, the comparison between FY 2009-10 and any of the previous years is not appropriate as the Licensee accounted for the Regulatory Asset in its books for the first time in FY 2009-10.

The Licensee submits that the Licensee at Page 8 to 10 of **Response 1** had set out the position against the various “important points”, wherein the impact of the Regulatory Assets can be clearly seen and on exclusion of the same, the position of FY 2009-10 would be completely different.

Therefore, the Licensee once again reiterates its earlier stand and submits that it would be factually incorrect and misleading to infer that the Licensee had not pointed out any discrepancies. It is submitted that the Licensee had vide its Response 1 comprehensively pointed out that the Commission had erred whilst construing its audited accounts and the reports of its credit rating agency. The Licensee had also very clearly and comprehensively explained the true factual position to this Commission and had rebutted any allegations of any misrepresentations to either the GoNCTD or this Commission.

Query b) Based on the audited accounts and report of the Credit Rating Agency, the correct Debt Equity Ratio (hereinafter “DER”) and Debt Service Coverage Ratio (hereinafter “DSCR”) as have already been mentioned in the Commission’s letter dated 28.05.2010 being letter No. F.11 (570)/DERC/2010-11/2492 (hereinafter “Letter 1”), which shows very clearly that both DER and DSCR shown by the Licensee in its representation to GoNCTD were not correct at all.

The Licensee reiterates that its audited accounts and Credit Rating Report have to be read in proper perspective. The Licensee submits that the Licensee had in its **Response 1**, at pages 8-10, clearly demonstrated in a tabular form the impact of the Regulatory Assets, which clearly indicated that on the exclusion of the said Regulatory Assets, the position for FY 2009-10 would be entirely different.

The Licensee fails to understand why the Commission overlooked its own orders wherein it had indicated that entitlements of the Licensee would be given through tariff in future/at the time of truing up, which fact was considered by the Licensee whilst giving its DER and DSCR to its lenders. Non-consideration of its own orders is also evident from the fact that this Commission in the letter under reply has indicated that no Regulatory Assets have been created by it in its past tariff orders despite the fact that this Commission in its order dated May 28, 2009 had clearly deferred the revenue requirement of the Licensee and had indicated that

the same would be recoverable through tariff over a period of 2 years along with carrying cost of 9%. The Licensee submits that this is nothing but a Regulatory Asset as defined under the MYT Regulations as well as the National Tariff Policy. Therefore, this Commission's disregard of its own orders coupled with the constant deferment of recovery through tariff of reasonable, prudent and legitimate expenses and return of the Licensee has put the Licensee in the dire financial unsustainable position.

Therefore, the Licensee states and submits that recovery has been deferred by the Commission repeatedly and ostensibly on the ground of imaginary surpluses or not-giving effect to legal entitlements adjudicated by this Commission itself or by the Hon'ble Appellate Tribunal for Electricity. This has resulted in the Licensee being entitled and accordingly rightly making accounting entries to show such entitlements as required in the Accrual based accounting. This is evident from the entry of Income recoverable from future tariffs amounting to Rs. 827 crs and thereby resulting into a book profit whilst the Licensee have yet to realize the said amount in cash through tariff. This is also evident from the fact that the Licensee has admittedly over achieved its loss reduction targets despite not getting the statutorily promised over achievement benefit. Finally, this is evident from the fact that the Commission has determined the tariff on the basis of surpluses for three years in the MYT period wherein in each year, instead of a surplus there has actually been a deficit on account of the constant overestimation of revenue by the Commission, despite the Licensee having exceeded its AT & C targets as specified in the MYT Order.

In view of the above, the Licensee denies having given incorrect figures for its DER or DSCR to the GoNCTD. The Licensee has calculated its DSCR in accordance with the generally accepted formula. In fact, the DSCR calculated by this Commission and as has been demonstrated subsequently, is premised on an erroneous reading of the accounts of the Licensee. Therefore, the Licensee denies having misled either the GoNCTD or the Hon'ble Commission.

Query c) The loan sanction letters issued to the Licensee by several Banks also support the abovementioned facts wherein the Banks have mentioned the method and formula of calculating DER and DSCR also and based on this the financial health of the Licensee is seen as excellent, completely negating the Licensee's representation regarding breach of financial covenants.

The Licensee submits that whilst applying the formulae prescribed by one of the Bank, the Licensee has calculated the adjusted DSCR which, as per the audited accounts for FY 2009-10 of the Licensee works out to 1.18. However, the Commission whilst calculating the DSCR for the Licensee has clearly erred as evident from the following tabular representation:

			Rs. (In Crores)
Particulars	Calculation as per the formula specified by one of the Company's Banks	DERC calculation as per letter dated 21.06.2010	Difference
Inflow			
PAT	186.61	186.61	-
Depreciation	132.55	132.55	-
Loss on sale / discarding of Assets	0.22	-	0.22
Interest	275.46	275.46	(1.00)
Income Recoverable from future tariff	(827.79)	-	(827.79)
Debt drawdown	890.00	890.08	(0.08)
Equity infusion	-	-	-
Capex	(304.82)	(298.51)	(6.31)
Decrease / (Increase) in WC	10.79	(153.49)	164.28
Investments	0.48	-	0.48
Opening cash balance	27.23	27.23	-
Consumer contribution for capital works	92.37	386.49	(294.12)
Consumer security deposits	44.84	311.12	(266.28)
Proceeds from sale / discarding of assets	1.08	-	1.08
Cash credit (WC loan)	153.49	294.67	(141.18)
Movement in general reserve	-	(0.91)	0.91
Movement in Service Line Deposits	(2.61)	-	(2.61)
Total cash available (A)	679.90	2,052.30	(1,372.40)
Outflow on account of Debt Servicing Obligations			
Interest	275.46	275.46	
Debt repayment	301.92	302.00	
Total Cash Outflow (B)	577.38	577.46	
Adjusted DSCR (A/B)	1.18	3.55	

The Licensee submits that the erroneous approach adopted by the Commission is self explanatory from the above table. A bare perusal of the above table would indicate that the Commission has not taken into consideration/erroneously considered the following:

- a. The figure for Profit after Tax for the year 2009-10 of Rs. 186.61 includes an amount of Rs. 827.79 crores accrued by the licensee against 'Income Recoverable from future Tariff'. The Commission has taken the figure of Rs. 827.79 crores as the cash generation of the Licensee whereas the same is clearly a cash item yet to be realized from future tariffs as shown in Profit & Loss account. The recognition of this receivable is by means of an accounting entry only without any associated cash flows. Therefore, the Commission has clearly erred by taking an item as a cash receipt, which will be converted into cash through future tariff orders only and since the same is not readily available cash with the Licensee. Accordingly in the cash availability statement, since the figure of PAT is inclusive of this credit, a deduction has to be made in arriving at net cash inflow to reflect the fact that the aforesaid credit is a non-cash item. The cash flows resulting from the said receivables would be recognized in the cash availability statement only if and when they occur in future.
- b. The Commission has considered an increase in Working Capital at Rs. 153.49 crores whereas the same actually works out to a decrease of Rs. 10.79 crores. The Licensee is at a loss to understand as to how the Commission has arrived at the figure of Rs. (153.49) crores, which amount is actually Rs. 10.79 crores. The workings for the decrease in working capital is tabulated below:

Movement in working capital				
	2008-09		2009-10	
Current Assets				
Inventories		137.42		127.23
Sundry Debtors	257.42		1,319.87	
Less: Tariff Adjustment Account	-	257.42	827.79	492.08
Sundry Debtors for bulk power sale		117.00		238.15
Other Current assets		0.57		0.57
Loans & Advances		119.54		109.55
		631.95		967.59
Current Liabilities				
Current Liabilities		485.98		812.84
Provisions		11.18		30.75
		497.16		843.59
Net Current Assets		134.79		124.00
Decrease in WC				(10.79)

c. Further, the Licensee submits that the Commission has erred whilst arriving at the following amounts:

- i. **Consumer Contribution for Capital Works:** The Commission has overstated the amount to the tune of Rs. 294.12 crores. It is submitted that the amount of consumer contribution for FY 2009-10 is actually the increase in consumer contribution for the relevant financial year. The Commission has erred by taking into consideration the accumulated figure, which is an accumulation of consumer contribution over a period time. For example, the Consumer Contribution for Capital Works as at the end of a year comprise the contributions received till the previous year end and contributions received during the year. The Commission has erred whilst taking this accumulated amount since the consumer contribution for a particular financial year is actually the contribution by consumers in that particular financial year. Therefore, for FY 2009-10, the net increase in consumer contribution is actually Rs. 92.37 cr. whereas the Commission has

taken a cumulative figure of Rs. 386.49 cr. thereby unduly accounting for Rs. 294.12 crores as cash accumulation for FY 2009-10.

- ii. **Cash Credit/WC Loan:** It is submitted that the similar erroneous approach has been adopted by the Commission for the head Cash Credit/WC loan, by taking the accumulated figure. The impact on account of such an erroneous calculation is to the tune of Rs. 141.18 crores.
 - iii. **Consumer security deposits:** The Commission has once again adopted the same erroneous approach for the head Consumer security deposits of which the impact is to the tune of Rs. 266.28 crores.
 - iv. **Service Line Deposits:** The Commission hasn't considered the amount of Rs. (-)2.61 crores on account of Service Line Deposit as is clear from the above tabular representation.
- d. Further, the Commission has taken the amount of Capex as Rs. 298.51 crores whereas the actual amount expended by the Company on Capex for FY 09-10 is Rs. 304.82 crores. The amount of Capex considered by the Commission is net of the value of assets sold / discarded during the year amounting to Rs. 6.31 crores whereas the actual amount spent by the Company on Capex needs to be considered without adjusting for the value of assets disposed off. The cash impact of disposal of assets has been considered separately in the table above as loss on disposal of assets amounting to Rs. 0.22 crores and proceeds from disposal of assets amounting to Rs. 1.08 crores.
- e. The Commission has taken the figure of Rs. (-)0.91 crores in the above table as the movement in general reserve. This amount of Rs. (-)0.91 crores is an adjustment of depreciation on assets created out of grant-in-aid and has already been reduced from the amount of depreciation on the assets for the year as shown in the Profit & Loss A/c for the FY 2009-10.

As such the amount of Rs. 0.91 crore as movement in general reserve should not again be considered.

The Licensee submits that the total difference in the Commission's calculation as compared to the Licensee's calculation with respect to the available cash accrual to service the debt obligations is Rs. 1372.38 crores. Hence, the adjusted DSCR, which is represented by total cash available divided by the total debt obligations for the financial year, is at variance from what has been calculated by the Licensee with what has been considered by the Commission.

In view of the above, the adjusted DSCR calculated by the Commission works out to 3.55 (2052.30 / 577.46), whereas rightly, the adjusted DSCR calculated by the Licensee works out to 1.18 (679.90/577.38).

Therefore, the Licensee submits that the Licensee has in fact calculated its DSCR as per the formula suggested by one of our Bankers, which work out to 1.18 and not 3.55 as calculated by the Commission.

It may also be mentioned that there are various ways in which DSCR is computed and the method adopted by the Licensee is one of those methods as specified by one of its bankers. However, no matter which method is adopted to calculate the DSCR, the resultant figure would reflect the same acute position that the Licensee is in with respect to its ability to service its debt obligations.

It is submitted that a DSCR of 1.18, which is much lower than 3.55 and clearly reflects the inability of the Licensee to repay its debt obligations in a satisfactory manner. The DSCR for FY 2009-10 has not been significantly greater than 1, which means that the margin of safety available to lenders has been minimal. Further, the entire debt servicing during the FY 2009-10 has been out of fresh borrowings.

In view of the above, the Licensee denies having misled either the GoNCTD or the Hon'ble Commission whilst calculating its DSCR

Query d) No Bank or Financial Institution has ever recognized Revenue gap, proposed to be absorbed in the subsequent year as per the Tariff Order as a Regulatory Asset, for the purpose of DER or DSCR. That DSCR of 3.55, being more than required minimum of 1.10, shows that there is no financial emergency or cash crunch and financial covenants have been never breached.

The Licensee denies the allegation made by the Commission that no bank or financial institution has recognized the existence of a revenue gap in the form of regulatory assets. The Licensee submits that it has in fact procured Short Term Loan /general purpose loans from banks against cash mismatch which primarily is on account of deferment of cost reflective tariff. It is also pertinent to note that Commission itself has identified a revenue gap of Rs. 827 crores, which revenue gap has been created by the Commission itself in its Tariff Orders. The Licensee submits that the said revenue gap is currently unfunded due to lack of cost reflective tariff leading to the precarious financial condition that the Licensee finds itself in today.

It is also pertinent to note that the notes to the accounts of the Licensee for FY 2009-10 also indicate the existence of regulatory assets amounting to Rs. 827.79. Relevant extract of the said note is produced below for the sake of convenience:

“ ...

5. Regulatory Assets

The company has accounted for Regulatory Assets amounting to Rs. 827.79 crores, the details of which are given below:

a. Revenue Gap as per MYT Order dated 28th May 2009

The DERC, vide its Order dated 28th May 2009, has trued up the financials upto F.Y. 2007-08 and had identified Revenue Gap of Rs. 575 crores as on 31.3.08. As per the Order, the said Gap would be recovered through future tariff. Considering the above Order and the fact that the gap has not been recovered during FY 2008-09 and 2009-10 and based on legal opinion, the company has recognized Rs 683.15 crores being the revenue gap up to FY 2007-08 including carrying cost of Rs 108.15 crores up to 31st March 2010 as regulatory assets.

b. 6th Pay Commission Recommendations

The DERC, vide its Order dated 28th May 2009, and recognizing the uncontrollable nature of the 6th Pay Commission Recommendations has agreed to true-up the impact on account of 6th Pay Commission recommendations. Accordingly, an amount of Rs 144.64 crores, has been recognized as regulatory assets. The Company has also taken a legal opinion supporting the same.

....”

Query e) The good financial health of the Licensee is a matter of appreciation indicating the success of Power Sector Reforms in Delhi. In such a situation it is really surprising as to why there is a need for the Licensee to show its financial health in a bad light which is contrary to the factual position.

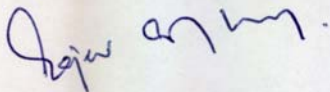
After inclusion of the “Income recoverable from future Tariff” amounting to Rs. 827 crores, the Licensee’s audited accounts reflects a book profit but the financial health of the Licensee has to be inferred from the overall analysis of all the components of financial statements. However as discussed above such income needs to be recovered through cost reflective tariff and the amount needs to be available in the hands of the Licensee after meeting all its expenses. Unfortunately, hard cash has still not reached the licensee in the absence of a suitable Tariff Order which provides for a cost reflective tariff as required by the Act and the Tariff Policy.

In the light of the above, the Licensee reiterates the contentions and concerns raised in its Representation to GoNCTD and the same may be treated as a part of the present

reply. The Licensee further states that there are no discrepancies in the figures in the audited accounts or the Report, nor are the same at variance with the representation for the reasons stated above. The Licensee trusts that the queries have been answered to the satisfaction of the Hon'ble Commission and in case any further clarifications are required, the Licensee will be pleased to provide the same.

Kindly acknowledge receipt of the present response.

Yours truly,
For **BSES Rajdhani Power Limited**,



Rajeev Chowdhury
Head (Regulatory)