Kerala State Electricity Regulatory Commission
Thiruvananthapuram

In the matter of application for truing up of accounts of KSEB Ltd for the financial year 2014-15

Proceedings of the Chairperson

Present : T.M. Manoharan

<u>Order dated 27.04.2017</u>

1. KSEB Ltd had, on 16.11.2016 filed the application No. OA 4/2017 for truing up of the accounts of its predecessor in interest namely, Kerala State Electricity Board (KSEB) for the financial year 2014-15. After preliminary scrutiny of the application and after getting necessary clarifications, public hearing was conducted on 15.03.2017. The undersigned had also participated in the public hearing. On examination of the files relating to the said application, it is noticed that verification of the documents and data has not been completed by the officers of the finance and tariff wing and of the technical wing. The learned Members in charge of the financial and technical matters have also not completed their scrutiny of records and data. Therefore final order in the said application could not be issued so far. Being the Chairperson of the Commission, who participated in the public hearing, the undersigned has to express his views on the matters dealt with in the application and on the further course of action. Hence this order.
2. The Commission had, on 20.03.2017, issued its order in OA 10/2016, which was the application dated 21.04.2015 filed by KSEB Ltd for truing up of the accounts of the predecessor in interest namely KSEB. The said order dated 20.03.2017 was a majority order issued by the learned Members Shri. K.Vikraman Nair and Shri. S.Venugopal. In the said order the undersigned had issued a minority order expressing difference of views on the following grounds.

    a) The decision of the learned Members to approve expenditure in respect of controllable items, was not in accordance with the scheme of law relating to determination of tariff,
    b) The decision of the learned Members to approve expenditure in respect of controllable items not in the interest of consumers, and
    c) The decision of the learned Members to approve expenditure in respect of controllable items not in the long term interest of KSEB Ltd, which should function more economically and efficiently to withstand and survive the impending tough competition in power sector.

d) The licensee could have realized excess expenditure for generation and for purchase of power in accordance with the provisions of KSERC (Fuel Surcharge Formula) Regulations, 2009.

e) The re-organization of KSEB into functionally and financially independent units namely, strategic business unit-generation (SBU-G), strategic business unit-transmission(SBU-T) and strategic business unit-distribution(SBU-D), preparation of separate accounts and balance sheets for such SBUs, constitution of Master Trust for payment of pension and such other provisions in the Second Transfer Scheme (notified by Government as per GO (P) No. 46/2013/PD dated 31.10.2013 and published as Statutory Rules and Orders (SRO) No 871/2013 in Kerala Gazette Extra Ordinary No.3103 dated 31.10.2013) have to be implemented without delay.

f) As held concurrently by the Hon'ble Supreme Court and by the Hon'ble APTEL, the Commission is also bound by the regulations issued by it and therefore truing up process should invariably done in accordance with the provisions of the following regulations,-

   (i) Kerala State Electricity Regulatory Commission (Terms and Conditions of Tariff for Retail Sale of Electricity) Regulations, 2006 (hereinafter referred to as Tariff Regulations, 2006)

   (ii) Kerala State Electricity Regulatory Commission (Terms and Conditions for Determination of Tariff for Distribution and Retail Sale of Electricity under MYT Framework) Regulations, 2006 (hereinafter referred to as MYT Regulations, 2006)

   (iii) Kerala State Electricity Regulatory Commission (Fuel Surcharge formula) Regulations, 2009 (hereinafter referred to as Fuel Surcharge Regulations, 2009)

g) The cost of power purchase and taxes on income are uncontrollable items of expenditure, whereas interest on capital liabilities, interest on working capital and O&M expenses which consist of employee cost, repairs and maintenance charges and administrative and general expenses are controllable items of expenditure. Therefore O&M expenses, have to be regulated in accordance with the provisions of the Tariff Regulations, 2006, which is quoted hereunder,-

> ***15. O&M Expenditure.-*** *(1) The component of revenue requirement consists of employee cost, administration and general expenses, repairs and maintenance expenses and other miscellaneous expenses.*
> *(2) These costs are to be taken at actuals or as allowed by the Commission whichever is lower and should be taken as base value.*
> *(3) The approved base value may be indexed to predetermined indices such as Consumer Price Index, Wholesale Price Index or*

a combination of both indices for subsequent years. Base value of O&M can be indexed to 70% of CPI and 30% of WPI.

h) Truing up of accounts is a process of prudence check done by the Commission on the audited accounts of the licensee to evaluate its financial and operational performance compared to the approved forecast in the order on aggregate revenue requirements and expected revenue from charges. It has been held by the Hon’ble Supreme Court and Hon'ble APTEL that, auditing of accounts by the Comptroller and Auditor General (C&AG) and prudence check done by the Commission in the truing up process are totally different with different objective. The auditors examine the expenses of the licensee to ascertain whether or not there were any irregularities or non-compliance of rules and regulations relating to finance and accounting of the licensee. Prudence check is done by the Commission to examine the reasonableness of expenses incurred by the licensee and to ascertain how much of such expenditure can be passed on to the consumers by way of tariff. Prudence check in truing up process is the most effective step to safeguard consumer interest and therefore the Commission has the duty to perform it with utmost care and caution. Prior to the Tariff Regulations, 2014, in respect of controllable items, the actual amount of expenditure or the amount of expenditure in ARR whichever is less, had to be approved in the truing up process as per the regulations. In this process, if the licensee achieved some efficiency gains and reduced its expenditure below the level approved in ARR, the benefit was not made available to the licensee, since in the truing up process, the actual amount incurred or the amount approved in ARR, whichever is less, was being allowed. Thus the entire benefit of efficiency gains achieved by the licensee was made available to the consumer and therefore such system was not encouraging the licensee to make efficiency gains. It was in view of the above facts, the mechanism for sharing gains or losses on account of controllable factors was specified in regulation 15 of the Tariff Regulations, 2014.

i) There is no provision in the regulations to approve in truing up process, any excess expenditure over and above the amount approved in ARR in respect of controllable items of expenditure.

j) Truing up is invariably based on the audited accounts of expenditure actually incurred by the licensee. The expenditure incurred by the licensee should also be supported by authentic records. Therefore the relevant regulations do not permit the Commission to approve in truing up process any expenditure in excess of the amount approved in ARR in respect of controllable items of expenditure. This is all the more true in view of the judgments of the Hon'ble APTEL and of the Hon’ble Supreme Court to the effect that, the regulations issued by the Commission are subordinate legislations and therefore they are binding not only on the consumers, the licensees and the generators, but also on the Commissions which issued such regulations.

k) KSEB Ltd had filed before the Hon’ble Supreme Court, the Civil Appeal No. 5473 and 5474 of 2015 from the order dated 10.11.2014 of the Hon'ble APTEL in appeal Nos. 1/2013 and 19/2013. The Commission had, in the counter affidavit filed in the above appeals, submitted certain important questions of law before the Hon’ble Supreme Court, which are now pending before the Apex Court.
l) KSEB Ltd has not produced necessary and sufficient authentic documents or records to substantiate its claims for higher employee cost pertaining to the 27175 employees who were in the service of KSEB Ltd in 2008-09.
m) The Commission has no authority or responsibility to fix the pay and allowances of the employees of KSEB Ltd. It is the prerogative of the management of KSEB Ltd to determine the pay and allowances and service conditions of its employees, after following due procedures and after obtaining concurrence of the Government. KSEB Ltd may incur any expenditure for giving service benefits to its employees. The Commission has to fix only the reasonable limit of such expenditure under the head O&M expenditure, which can be passed on to the consumers by way of tariff. Within the normative maximum limit for the O&M expenditure, as fixed by the Commission in accordance with the regulations, the licensee has the freedom and latitude to regulate its expenditure under various sub heads.
n) In truing up process, the Commission has to conduct prudence check on the actual expenditure as per audited accounts of the licensee to evaluate its physical and financial performance as well as the efficiency gains, if any, achieved. The truing up process is based on actual expenses as evidenced by authentic accounts and records. In the absence of the details of actual expenses supported by authentic records, excess expenditure cannot be approved by the Commission in the truing up process.
o) KSEB Ltd has either failed to or refused to submit such details and records, even though it claims to have computerized all the matters relating to the management of human resources. When KSEB Ltd has failed or refused to submit such details and records which should be in its possession, the normal course of action in accordance with Section 114 of The Indian Evidence Act, 1872 is to draw adverse inference and to conclude that KSEB Ltd has failed to or refused to submit such details and records since they would disprove the claim for approval of excess employee cost in the guise of the order dated 10.11.2014 of the Hon'ble APTEL. Section 114 of The Indian Evidence Act, 1872 and clause (g) of

the illustrations thereunder which are relevant for the purpose, are quoted hereunder.

> *“**114 Court may presume existence of certain facts:-** The Court may presume the existence of any fact which it thinks likely to have happened, regard being had to the common course of natural events, human conduct and public and private business, in their relation to the facts of the particular case.*
> *<u>Illustrations</u>*
> *The Court may presume-*
> *X X*
> *(g) That evidence which could be and is not produced would, if produced, be unfavourable to the person who withholds it”*

p) Since KSEB Ltd has failed to or refused to produce such records, it has to be reasonably presumed that, if the authentic record are produced, they would prove that the amount approved by the Commission was sufficient to meet the pay and allowances, gratuity, pay revision, pension etc in respect of the 27175 employees in the service of KSEB Ltd in 2008-09. The Hon'ble APTEL has, in its order dated 10.11.2014, directed only to allow in truing up process the amount required to meet the pay and allowances, increase in DA, payment of gratuity, payment of pension, etc., in respect of the 27175 employees. Truing up has to be based on accounts of actual expenditure and authentic records to substantiate the claims of the licensee. Approval of excess expenditure under employee cost as per calculations based on assumptions and conclusions without authentic records, is not in accordance with the spirit of the order of the Hon'ble APTEL dated 10.11.2014. On the other hand it is only approving excess employee cost in the guise of implementation of the order of the Hon'ble APTEL.

q) According to the undersigned, the Commission has no duty or responsibility to ‘calculate the employee cost’ in a truing up process, basing on extrapolations or interpolations or assumptions or conclusions. After having availed the benefit of such excess employee cost approved basing on such extrapolations or interpolations or assumptions or conclusions, the licensee can always challenge their veracity and validity.

r) The approval of excess employee cost, as claimed by KSEB Ltd, beyond the scope of the scheme of law and regulations and without substantiating authentic records, is not at all in the interest of the consumers.

s) The employee cost of KSEB Ltd, per unit of electricity sold is very much on the higher side. The Commission has been giving directions to KSEB Ltd to improve efficiency gains by adopting information technology in billing and revenue collection, meter reading, disbursement of pay and allowances and pension, keeping accounts of PF, etc. The Commission has also given direction to assess the requirement of employees in various divisions, re-skill and re-deploy the excess employees and to re-define the job content of different posts. In spite of repeated directions, the licensee is not seen to have taken such directions seriously and implemented them earnestly with a view to improving the performance and enhancing the efficiency gains.

t) It is desirable in the interest of the licensee and of the consumers, to insist on efficiency gains and to regulate employee cost in accordance with the relevant regulations, instead of approving the excessively high employee cost which was increasing due to increase in number of employees and increase in pay and allowances of employees.

u) It is absolutely necessary that KSEB Ltd, being one of the very large public sector undertakings of the Government, with its long tradition of service to the people of Kerala, should continue to function more efficiently to render better service to the people. If KSEB Ltd has to survive such tough competition and sustain as an efficient distribution licensee, it will have to improve the work norms, the efficiency gains and the service to people. The recent studies conducted by Indian Institute of Management, Kozhikode reveals that many measures are yet to be taken by the licensee for improving efficiency, improving utilization of available human resources and for optimizing employee cost.

v) Such other grounds and facts as explained in the minority order in the order dated 20.03.2017 in OA 10/2016.

3. Therefore the undersigned is of view that approval of excess employee cost beyond the scope of regulations without substantiating authentic document and allowing such excess employee cost to be passed on to the consumers, would not be desirable in the long term interest of the efficient functioning of KSEB Ltd. The above views expressed by the undersigned will hold good for processing the application for truing up of accounts for 2014-15.

4. KSEB Ltd shall take special note of the remarks dated 19.02.2016, given by the Additional Chief Secretary (Finance) on the proposal to approve the long term agreement (LTA) for pay revision. The said remarks were on the Note to the Board of Directors (No.CMD/102/P.R-Workmen and Officers/2/2016 dated 15.02.2016) on the 'Revision of Pay and Allowances of Workmen and Officers of KSEB Ltd', which was taken as agenda item No.OA1/2-2016. The Note to Board of Directors was to approve the pay revision of workmen with effect from 01.08.2013 and of the officers with effect from 01.07.2013. The additional financial commitment as per the said note was Rs.19.83 crore per month with an annual commitment of Rs.237.96 crore. The remarks of the Additional Chief Secretary dated 19.02.2016 are quoted hereunder.

"The following objection to the LTA may be recorded.

The terms of the agreement were not discussed in the Board at sufficient length. The fact that the settlement was done at the Government level even before the Board was consulted and apprised is highly objectionable and militates against the very concept of the organizations autonomy.

While, it is important to reward employee with a good compensation package, there are components in the package that should have been curtailed to reasonable levels. Distributing largesse based on such an LTA comes at a cost – as this translates into an extra burden for the consumers.

It is understood that both for Non-Technical and Technical Staff the scale of pay in Electricity Board has been fixed at 2 to 4 stages above what is enjoyed by persons holding corresponding posts in government. There is absolutely no justification for doing this. If the idea is to provide compensation for the extra risk exposure of an employee, the correct approach should have been to compensate this extra risk through an additional risk allowance as is being done in Government.

These facts will be brought to the notice of the Kerala State Electricity Regulatory Commission so that the unnecessary part of the expenditure on account of pay revision will not be passed on to the consumers while tariff are re-fixed.” .

5. Further, in the matter of creation of new electrical sections with additional posts, the Additional Chief Secretary (Finance) had, on 19.02.2016, recorded his remarks as follows,-

“The creation of the 27 new Electrical Section Offices in Kerala State Electricity Board Limited is strongly objected to. At a time when the efforts should be to reduce manpower through modernization and computerization, the Board is proposing to open 27 new offices at an estimate total outlay of approximately Rs.29 core.

This financial burden will finally be passed on to the people of Kerala who are its consumers.

Finance Department intends to bring this avoidable wastage of resources to the notice of the Kerala State Electricity Regulatory Commission, so that this additional expenditure will not be passed on the consumers of the Board.”.

The Additional Chief Secretary (Finance) has forwarded the above remarks for appropriate action by the Commission. KSEB Ltd shall take note of the above remarks of Additional Chief Secretary (Finance) and prepare and implement plans for optimizing the number of employees and the employee cost by improving efficiency. KSEB Ltd shall, on or before 30.09.2017, submit an action taken report on this issue.

6. KSEB Ltd shall improve and upgrade the skills/competencies of the workers and of the officers by implementing a well laid down training schedule with the

latest state of art technological innovations in the sector and shall optimize the staff strength and employee cost, taking into consideration the recommendations of IIM Kozhikode and the concerns of Government as expressed by the Additional Chief Secretary (Finance). An action plan in this regard shall be submitted to the Commission on or before 30.09.2017.

7. KSEB Ltd has, in WP No. 465/2015, challenged the validity of the KSERC (Terms and Conditions for Determination of Tariff) Regulations, 2014. KSEB Ltd has also filed petition in the said Writ Petition praying for upward revision of the O&M norms for the distribution business / licensees as specified by the Commission in Annexure IX to the KSERC (Terms and Conditions for Determination of Tariff) Regulations, 2014. The order of the Commission in the application for truing up of accounts for 2014-15 will have far reaching consequences. Therefore the Commission has to be extremely cautious while issuing orders after examining the claims and counter claims as well as the relevant documents and data.

8. Further, the Commission should also guard against the possible allegations of bias, impropriety and unfair judicial practices especially in view of the following facts,-

   (a) The learned Member Shri. K.Vikraman Nair had been the Director (Transmission) of KSEB Ltd till November 2014 and the learned Member Shri. S.Venugopal had been the Director (Finance) of KSEB Ltd till April 2015 and therefore they were the part of the management of KSEB Ltd which incurred the impugned expenditure.

   (b) The statutory time limit given as per sub-section (3) of Section 64 of the Electricity Act, 2003, for issuance of tariff order is 120 days from receipt of the tariff application. The application for truing up OA 4/2017 was received on 16.11.2016 and public hearing was conducted on 15.03.2017. The delay beyond 120 days for issuance of the final order can be depicted as an attempt to avoid minority order.

   (c) Additional details, which are obtained after the public hearing, are not made available to public and the comments thereon are not invited from public. Accepting such additional details without subjecting them to public scrutiny can be depicted as a dilution of the process of public hearing.

9. The Commission is an independent statutory body constituted under Section 82 of the Act with quasi-judicial and quasi-legislative functions. It has also been given functional and financial autonomy. Section 89 of the Act, stipulates the term of office and conditions of service of Members in such a way that the functional and financial independence are ensured to them. In this regard the following famous legal dicta relating to the principle of natural justice have to be adhered to by the Commission

   (i) "no-one should be a judge in his own cause."

   (ii) "Justice must not only be done, but must be seen to be done"

10. Therefore the undersigned is of the view that the learned Members will consider the following two options before taking a final decision in OA 4/2017.
    (i) Issuing order by the learned Members, without a fresh public hearing, citing the reason that the Chairperson who heard the case, has demitted the office.
    (ii) Present the case before the new Chairperson on assumption of office and take further course of action following due procedures in accordance with law, in consultation with him.

    If the learned Members adopt the first option, the views expressed by the undersigned in this order may also please be referred to in their order.
11. The Secretary to the Commission, the Director (F&T) and other staff are directed to submit this proceedings and relevant records to the Members for appropriate action in accordance with law. Copy of this proceedings may please be made available in public domain.

Sd/-
T.M.Manoharan
Chairman

Approved for issue,

Santhosh Kumar.K.B
Secretary