Over the past 11 years, some of the stated objectives of the Electricity Act, 2003 have been achieved, but much ground still remains to be covered on aspects that are constraining India's economic growth and its citizens' well-being. That should define the reform agenda for addressing these issues.

Manifestations of the problem

In spite of an installed capacity of over 254,000 MW, our average output remains below 150,000 MW (below 60 per cent) primarily due to the endemic fuel crisis; the inadequacies of our grid development; and operational inefficiencies. The self-inflicted nature of the problem becomes evident when we contrast our average national losses of around 30 per cent with the 10-12 per cent aggregate technical and commercial losses of a well-functioning system. We have 40,000 MW to 60,000 MW of installed generation capacity lying idle due to fuel shortages. Instead of getting supply at Rs 4 per unit from such plants, our marginal supplies include 25,000 MW of diesel gensets supplying at Rs 16-Rs 20 per unit. Despite having the fifth largest proven coal reserves in the world, we are the third largest importers of coal on account of our persistent refusal to allow entrepreneurship to end the state monopoly of coal. This situation hangs in a delicate balance today as the government seeks to prevent any adverse effect of the recent Supreme Court judgments cancelling the allocation of 294 coal blocks with a cumulative capacity of 45,000 million tonnes.

The nation's financial ill-health continues to be aggravated by vote-bank politics and state interference with market and tariff/subsidy games aided by compliant regulators. From the accumulated dues of Rs 425 billion owed by the state electricity boards in 2001 to central sector undertakings, we are now set to reach a staggering Rs 2.5 trillion. As of May 31, 2014, financial institutions are stated to have around Rs 5.5 trillion to Rs 6.3 trillion of stranded and stressed power generation assets, which are primarily attributable to this growing financial sickness. Consequently, the honest taxpayer bears the burden of this revenue shortfall while the honest consumer suffers because of poor quality and an unreliable and constrained supply.

Emergent agenda for effective change

The government must take a holistic review of the sector's problems to ensure that there is enough investment to deliver reliable and adequate power supply at fair and viable prices.

The need for a complete separation of the wires business from generation, supply and trade has been often discussed with the aim of rectifying the situation. Bundling the distribution and supply functions has enabled the incumbents to create barriers to competition and to frustrate the statutory goal of non-discriminatory open access to the network, which secures competitive neutrality to various generators and choice to consumers. This would require several intermediary steps over a transition period.

Another significant challenge remains in the management and structural bundling of the transmission system planner operator with the transmission licensee. We need complete independence (administrative, management, financial, etc.) of system operators and transmission licensees to ensure accountability and competitive neutrality of the network infrastructure. Perhaps listing the system operators on the stock exchange and giving board seats to stakeholders like banks, representatives of private generators and consumers would help.

Section 11 of the act has often been misused to prevent deregulated generators from selling power as per their power purchase agreements or in the open market—forcing them to sell to...
local discoms at government-dictated prices. This power must be limited by statutory guidelines in terms of when it can be invoked, the duration for which it can be put in place, and the limits on the kind of arrangements that can be ordered. The objective of exercising such power must be stated, and a compensatory mechanism put in place to offset the undeserved burden cast on a party on a real-time basis.

Section 42 has been exploited by "captured" state regulators to impose such high levels of wheeling charges, cross-subsidy surcharge and additional surcharge on a third-party supplier that local discoms have effectively been given an unbreakable monopoly. This mechanism has also been used by states to transfer their own subsidy burden to other states. There is a need to specify guidelines and limits for regulators to exercise this power.

State regulators have been captured by the state governments and state utilities. We need to strengthen them and make them more accountable by consolidating four or five state regulators into a regional regulator. Also, each regulator must in reality be a multidisciplinary expert body with legal, technical and financial expertise that justifies the deference to its expertise that the courts have accorded in the past. Electricity regulatory commissions must be made to evolve into energy regulators to include renewable energy and coal in their domain. As regards coal, the domain may be defined to cover productivity/output, technology, capital cost and tariffs.

The Electricity Act also does not appear to have provided for time-bound disposal, except for Section 64 (procedure for tariff order), where 120 days' time has been stipulated. Some pending cases, dating back 5-10 years, still await a hearing, often leaving private and non-state parties at the mercy of state utilities. This must be remedied.

The fifth proviso to Section 14 of the act is often read to mandate that a second distribution licensee must have its own distribution network to supply in an area. It has been given a meaningful interpretation by the Tribunal in the Mumbai "cherry-picking case" to enhance access in unserved areas or constrained areas by removing bottlenecks and congestion or to enable parallel systems. The provision needs clarity to enable the electricity regulatory commission, in consultation with the system planner, to remove bottlenecks in the local network while securing the systematic time-bound augmentation of the network to give access to unserved areas.

The ballooning accumulated dues not serviced by tariff need to be tackled with an effective transition financing with a road map for their discharge – seeking suitable accommodation from the banks. We need to ensure decisions like real-time fuel cost pass-through in retail tariffs, an identical regime of right-of-way permissions for all transmission licenses, and financial restructuring and transition financing with reforms and tariff hikes.

Trading was defined and accepted as a distinct licensed activity, primarily for the stated objective of promoting competition and efficiency, and ensuring that the market evolves. However, certain regulatory decisions (such as a trading margin cap at 4 paise per unit to backstop credit risk where the marginal cost is Rs 3-4 per unit with no protection on the downside) have reduced the trader from an independent reseller to a commission agent. This needs a relook: either define trader to work for brokerage or permit full play to secure the benefit of efficient portfolio management among competing traders. There is a need to support the creation of a merchant market for intermediate and peak power while adding futures trade in power and coal (domestic and imported) to the power exchanges.

To address fuel risks, there is a need for effective reforms in the coal sector with increased accountability of Coal India Limited (CIL) through higher penalties for the non-delivery of MoU coal (as against fuel supply agreement-linked coal). The denationalisation or even the splitting up of CIL into separate companies, of which some could be privatised, should be taken up. The coal mine auctions post the Supreme Court judgment should be accompanied by a credible regulatory mechanism that establishes the real cost of efficiently mined and delivered coal.

When the stated policy aims to rapidly build capacities and implement projects, an effective single-window clearance mechanism that cuts across all central and state agencies can surely be implemented. While keeping our focus on building up capacities, it is critical to allot first priority to installed capacities that are lying idle as well as significantly completed capacities that are facing financial challenges. In this context, there is a need to evolve a framework to deal with and salvage productive assets and valuable investments in a time-bound manner. The solutions could subsume all dimensions of insolvency remedial action like the takeover of the asset by lenders exercising their step-in rights, buy-outs by procurement re-auctions, financial restructuring or regulatory interventions.

Perhaps there is a need to rethink whether it would help to shift "electricity" to the Union List from the Concurrent List. This will help in ensuring uniformity across the nation, particularly when the political economy overtures viability needing periodic redressal from union budgetary allocations, etc.