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Distribution franchisees mushroom even as power discoms up base rate

JYOTI MUKUL
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In a sector fraught with challenges, if margins are to be determined by the pace of loss reduction, the business model can hardly be termed prudent. But this is exactly what power distribution franchisees are doing — some of them in more cities than one.

While a new set of players — India Power, Crompton Greaves, Torrent and Essel Utilities — have taken the job of distribution franchisees with much enthusiasm, industry players advise caution over distribution firms' modified bidding norms.

According to Shrirang Karandikar, chief executive officer, India Power Corporation, states have increased the base rate for companies to bid for distribution franchise contracts. This is meant to recover arrears. "The distribution-franchise business is a thin-margin one. The model will become unsustainable if the base rate continues to be high. Recovery of arrears could lead to a collapse of the entire business," he said.

SQUEEZING LOSSES

	Franchisee	Customer base
MAHARASHTRA		
Nagpur	Essel Utilities	400,000
Bhiwandi	Torrent	200,000
Aurangabad	GTL Urja*	178,000
Jalgaon	Crompton Greaves	115,000
BIHAR		
Bhagalpur	SPML Infra	160,000
Muzaffarpur	Essel Utilities	149,000
Gaya	India Power	100,000
MADHYA PRADESH		
Gwalior	Essel Utilities	202,000
Ujjain	Essel Utilities	101,000
Sagar	Essel Utilities	57,820

* Contract terminated in 2014

India Power is the distribution franchisee for Gaya in Bihar. It received the rights for the city after Essel Utilities did so for Muzaffarpur and SPML Infra for Bhagalpur, for 15-year contract periods. The distribution-franchise model was first tried in December 2006, when Maharashtra State Electricity Distribution Company Ltd (MSEDCL) gave Torrent Power the rights for the Bhiwandi circle. The textile hub, where 60 per cent of the demand comes from the power loom sector, has a customer base of about 200,000, spread over 721 square kilometres.

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Eight years on, Bhiwandi is not alone. There are more than a dozen cities, including Nagpur in Maharashtra; Sagar, Gwalior and Ujjain in Madhya Pradesh; Agra in Uttar Pradesh; and Muzaffarpur, Gaya and Bhagalpur in Bihar; that have adopted the distribution-franchise model.

State government-owned distribution companies adopt this model in areas where losses are high. Under Section 14 of Electricity Act, a power distribution company can appoint another entity to supply power in a particular area within its distribution territory without the requirement of a separate distribution licence. "The key difference between a distribution-franchise model and a privatised distribution company is that the capital expenditure is *not passed through to consumers* under the former, while a private discom recovers that expense from consumers. Besides, government discoms' employees are on deputation from the utility concerned; they go back to their parent company after the end of the franchisee period," explained Siddhartha Mehta, chief executive (power distribution), Essel Infra & Utilities. The company is the distribution franchisee for Muzaffarpur, Nagpur, Sagar, Ujjain and Gwalior.

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At the time of bidding for a contract, the private players quote a price above the base rate for power to be supplied by the distribution company. The bidder quoting the highest levelised tariff gets the contract. To make a margin, the franchisee has to minimise the gap between input and supply price; it incurs capital expenditure for that. The billing to consumers, however, is done on a rate approved by the regulator. The capital expenditure is serviced through loss reduction and the franchisee gets paid for the assets it created, when it transfers it to the distribution company, at a depreciated value.

According to RB Goenka, head (energy cell), Vidarbha Industries Association, after a distribution franchisee has been appointed in Nagpur, the consumer services have improved and corruption has come down. "Since the franchisee's profitability depends on the quantum of power it is purchasing and selling, the franchisee is trying to sanction new loads and increasing load of consumers within the time limit of SOP (standard of performance) regulations. The technical skill, experience and knowledge of employees, particularly the testing department, however, is not according to requirements," he said.

Goenka added the franchisee was responsive to consumer complaints, the attending time for which had reduced. It is not always, however, that the model has worked successfully. In November last year, MSEDCL had to take over the Aurangabad distribution business after early vacation by the franchisee, GTL Urja. The private company worked for a little more than three years but was unable to reduce losses. "The company did not make capital expenditure for loss reduction," said an industry player. The problem between MSEDCL and GTL started with non-payment of electricity purchase payment.

Karandikar said the distribution-franchise model should be workable and beneficial for all stakeholders; for that, distribution companies needed to stick to the original model, where arrears are not built into the base rate. Mehta, too, said the model was a performance-driven one and required a strong political will, along with hand-holding by distribution companies, for success. "The future could see coming up of an integrated utility business, offering combined services of water, broadband, power and waste management, on a single bill."