

**IN THE APPELLATE TRIBUNAL FOR ELECTRICITY
(Appellate Jurisdiction)**

APPEAL No. 37 of 2017

Dated: 03.07.2025

**Present: Hon'ble Mr. Sandesh Kumar Sharma, Technical Member
Hon'ble Mr. Virender Bhat, Judicial Member**

IN THE MATTER OF:

Transmission Corporation of Andhra Pradesh Ltd.
Vidyut Soudha, Khairatabad,
Hyderabad – 500082.

...Appellant(s)

Versus

Andhra Pradesh Electricity Regulatory Commission
Through its Secretary
4th Floor, Singareni Bhavan,
Red Hills, Lakadi-ka-pul,
Hyderabad – 500004.

...Respondent(s)

Counsel for the Appellant(s) : Mr. Udit Gupta
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JUDGEMENT

PER HON'BLE MR. SANDESH KUMAR SHARMA, TECHNICAL MEMBER

1. The captioned appeal has been filed by. M/s. Transmission Corporation of Andhra Pradesh Limited assailing the Impugned Order dated 07.11.2015 passed by the Andhra Pradesh Electricity Regulatory Commission (in short “APERC” or “Commission”) in O.P. No. 13 of 2015.

Factual Matrix of the Case

2. The Appellant Transmission Corporation of Andhra Pradesh Limited (in short “APTRANSCO” or “Licensee”) is the Transmission Licensee inter alia vested with the function of bulk supply of electricity in the erstwhile undivided Andhra Pradesh State on 31.01.2000 by the Andhra Pradesh Electricity Regulatory Commission under the Andhra Pradesh Electricity Reform Act, 1998. Pursuant to various reforms and the Electricity Act, 2003, the Appellant evolved to become the State Transmission Utility (STU) in the erstwhile State of Andhra Pradesh with effect from 09.06.2005.

3. The erstwhile APERC issued the APERC (Terms and Conditions for Determination of Tariff for Transmission of Electricity) Regulations, 2005, i.e., Regulation No. 5 of 2005 (in short “2005 Regulations”), thereby introducing the Multi-Year Tariff (in short “MYT”) framework to govern the activity of transmission. As per this framework, the transmission licensee, i.e., the Appellant, files the Aggregate Revenue Requirement (ARR) and the proposed tariff for each year of the control period for the approval of the APERC.

4. Clause No. 10 of the 2005 Regulations is the relevant Regulation for the dispute at hand:

“10.1 The multi-year tariff framework shall be based on the following approach, for calculation of ARR and expected revenue from tariff and charges.

10.2 Base Year- Values for the Base Year of the Control Period will be determined based on the audited accounts available, best estimate for the relevant years and other factors considered appropriate by the Commission, and after applying the tests for determining the controllable or uncontrollable nature of various items. The Commission will normally not revisit the performance targets are fixed on the basis of base values of un-audited accounts.

10.3 Targets- Targets will be set for items that are deemed by the Commission as “controllable”. Trajectory for specific variables may be stipulated by the Commission where the performance of the applicant is sought to be improved upon through incentives and disincentives.

10.4 Controllable and Uncontrollable items of ARR:- The expenditure of the Transmission Licensee considered as “controllable” and “uncontrollable” shall be as follows:

TRANSMISSION BUSINESS

ARR Item	“Controllable”/ “Uncontrollable”
<i>Operation & Maintenance expenses</i>	<i>Controllable</i>
<i>Return on Capital Employed</i>	<i>Controllable</i>
<i>Depreciation</i>	<i>Controllable</i>

<i>Taxes on Income</i>	<i>Uncontrollable</i>
<i>Non-tariff income</i>	<i>Controllable</i>

10.5 Pass-through of gains and losses on variations in “uncontrollable” items of ARR:- The Transmission Licensee shall be eligible to claim variations in “uncontrollable” items in the ARR for a Control Period in the filings for the subsequent Control Period depending on the availability of data as per actuals with respect to effect of uncontrollable items:

Provided that the Commission shall allow the financing cost on account of the time gap between the time when the true-up becomes due and when it is actually allowed and the corrections shall not be normally revisited.

10.6 Gains and losses on variations in “controllable” items of ARR:- The Transmission Licensee in its filing for a Control Period shall present a statement of gains and losses for each controllable item of the ARR for the previous control period. The gains and losses for each item shall be presented after adjusting for any variations, if any, on account of uncontrollable factors with details thereof.

10.7 For the purpose of sharing gains and losses with the users, only aggregate gains or losses for the Control Period as a whole will be considered. The Commission will review the gains and losses for each item of ARR and make appropriate adjustments wherever required.

10.8 Notwithstanding anything contained in this Regulation, the gains or losses in the controllable items of ARR on account of force majeure factors shall be passed on as an additional charge or rebate in ARR

over such period as may be specified in the Order of the Commission.”

5. Clause no. 16 of the 2005 Regulations deals with the Taxes on Income and how they will impact the calculation of the ARR and states as follows:

“16.1 Taxes on Income, if any, on the income stream of the licensed business of the Transmission Licensee shall be treated as an expense and shall be recoverable through ARR.

16.2 Taxes on Income actually payable and paid shall be included in the ARR, limited, however, to tax on Return on Equity component of the Return on Capital Employed, and excluding tax on profit, if any, in excess of such return (arising out of any reason, including efficiency of the Transmission Licensee or any explicit incentive provided in the ARR), penalties, interest on delayed payment of tax, etc. , and duly adjusted for any refunds, etc. received for the previous periods.”

6. Accordingly, three control periods were determined for the Appellant, for which MYT orders were passed by the erstwhile APERC, which were:

- Financial year 2006-07 to 2008-09 was the 1st Control period
- Financial year 2009-10 to 2013-14 was the 2nd Control period
- Financial year 2014-15 to 2018-19 was the 3rd Control period

7. On 20.03.2009, based on the ARR filings of the Appellant, the Tariff order was passed by the erstwhile APERC for the 2nd control period, i.e., 2009-10 to 2013-14, approving an ARR of Rs. 6038 crores, and after reducing the NTI of Rs. 126.30 crores, the net ARR was Rs. 5911.66 cr.

8. In 2014, the erstwhile State of Andhra Pradesh was bifurcated into the new States of Andhra Pradesh and Telangana. Accordingly, a new APERC was constituted for the new State of Andhra Pradesh, and all the regulations, orders, etc., issued by the erstwhile APERC were adopted by the new APERC. The jurisdiction of the Appellant was also limited to the thirteen districts falling within the new state of Andhra Pradesh.

9. On 16.03.2015, the Appellant filed its true up petition for the 2nd control period before the APERC stating that the total revenue accrued during the said period was Rs. 6,266 crores against the Gross ARR of Rs.6885 crores, thus leaving a deficit of INR 619 crores and that out of the total revenue, Rs. 625 crores were from the non-tariff Income (NTI) and this deficit would have to be collected from the distribution companies.

10. Pursuant to the filing of the above-mentioned true-up petition, the APERC directed the Appellant to publish a public notice in one English and one Telugu newspaper. Accordingly, on 05.05.2015, the Appellant got the public notice published as per the direction of the APERC. The date of hearing was fixed as 09.10.2015 by the APERC, and various objections/suggestions with respect to the true-up order filed by the Appellant were received by the APERC.

11. During the course of the public hearing, the issue of NTI was argued in detail. With regard to the NTI, it was explained that as per Regulation 5 of 2005 of the erstwhile APERC, the NTI is passed on to the Consumers, however as per Clause No. 16 of the 2005 Regulations, for the determination of the ARR, the taxes on Income payable and paid shall be included limited to tax on the Return on Equity component of the Return on Capital Employed and it was argued that either NTI net

of other expenses should be passed on to consumers or the whole tax should be allowed for determining the ARR.

12. By way of the impugned order dated 07.11.2015 passed in O.P. No. 13 of 2015, the contentions raised by the Appellant in its True Up Order were not considered by the APERC, and its contention that there was a deficit was rejected. In fact, it was held that the true down amount for the new state of Andhra Pradesh for the 2nd control period was Rs. 271.34 crores and the same was payable by the Appellant to the two distribution companies in the new State of Andhra Pradesh i.e. the Andhra Pradesh Eastern Power Distribution Company Ltd. and the Andhra Pradesh Southern Power Distribution Company Ltd.

13. Aggrieved by the above order passed by the APERC, the Appellant filed a Review Petition on 04.02.2016 being R.P. No. 2 of 2016 in O.P. No. 13 of 2015 before the APERC, on the ground that there was an error apparent in the computation of the amounts pertaining to the Cost of Debt as a part of Return on Capital Employed (RoCE), the Income Tax and the Carrying Cost. The Appellant thus prayed for a relaxation of Rs. 187 crores under the abovementioned heads.

14. It was pointed out that the RoCE, which is a controlled item as per the 2005 Regulations, is defined as the product of the Regulated Rate Base (RRB) and the Weighted Average Cost of Capital (WACC), which is undisputedly a variable since it depends on the interest rate on debt and as such the same could not be taken to be fixed and had to be considered while pronouncing the true up order. Meanwhile, as per the order of the APERC dated 7.11.2015, the Appellant has passed the true-down of Rs. 271.34 crores to the two distribution companies in the new state of Andhra Pradesh, i.e., the Andhra Pradesh Eastern Power Distribution Company Ltd. and the Andhra Pradesh Southern Power Distribution Company Ltd.

15. By way of its order dated 26.08.2016 passed in R.P. No. 2 of 2016 in O.P. No. 13 of 2015, the APERC dismissed the Review Petition of the Appellant, holding that no grounds for review were made out.

16. Thus, being aggrieved by the Impugned Order dated 07.11.2015 passed by the APERC in OP No. 13 of 2015, the Appellant has preferred the present Appeal.

Written Submissions of the Appellant

17. The present Appeal has been filed by the Transmission Corporation of Andhra Pradesh challenging the Order dated 07.11.2015 passed by the Andhra Pradesh Electricity Regulatory Commission in O.P. No. 13 of 2015. The Appellant contends that the Commission erroneously determined the true-up amount for the second control period (2009-10 to 2013-14) as Rs. 271.34 crores, directing the Appellant to pay the said amount to Andhra Pradesh Eastern Power Distribution Company Limited (APEPDC)L and Andhra Pradesh Southern Power Distribution Company Limited (APSPDCL), despite the Appellant's submissions indicating a deficit position.

18. The Appeal also challenges the rejection of the Appellant's claims under three specific heads:

- (i) an increase of Rs. 59 crores towards Return on Capital Employed,
- (ii) treatment of tax on Non-Tariff Income, which the Appellant submits should either be passed on to consumers or fully considered in the ARR in accordance with Regulation 5 of 2005 and Clause 16 thereof, and

- (iii) the differential Return on Equity, wherein the Appellant sought a rate of 15.5% as per the CERC's Tariff Order dated 19.01.2009, instead of 14% as considered by the Commission.

In re: Return on Equity

19. It is submitted that Appellant filed MYT petition for the 2nd Control period on 29.11.2008 and assumed Return of Equity of 14% as per the then CERC Tariff Regulations for the 1st control period. CERC later issued the Tariff order for the 2nd control period on 19.01.2009 in which RoE was revised to 15.5%. The relevant extract of the said Central Electricity Regulatory Commission (Terms and Conditions of Tariff) Regulations, 2009 dated 19.01.2009 is reproduced as follows:

"15. Return on Equity.

(1) Return on equity shall be computed in rupee terms, on the equity base determined in accordance with regulation 12.

*(2) Return on equity shall be computed on **pre-tax basis at the base rate of 15.5%** to be grossed up as per clause (3) of this regulation..."*

20. It is pertinent to note that it is this rate at which the RoE should have been determined by the APERC when it issued the MYT Order on 20.03.2009 for the second control period as the RoE has to be fixed as per the CERC norms, as stated in Regulation 5 of 2005.

In re: An increase of Rs. 59 crores under RoCE due to the increase in the interest

21. The Appellant submits that although Return on Capital Employed (RoCE) is classified as a controlled parameter under the APERC Tariff Regulations, 2005 (Regulation 5 of 2005), it effectively becomes an uncontrolled item since it depends on the Regulated Rate Base and the Weighted Average Cost of Capital, with the cost of debt being a fluctuating variable.

22. It is further contended that during the second control period (2009-10 to 2013-14), the State Bank of India's base rate increased from 7.5% to 10%, and as corporate borrowings typically exceed the base rate, the Appellant procured debt at approximately 10% in the earlier years and up to 12% in the later years of the period.

23. The Appellant further submits that the Central Electricity Regulatory Commission, in its Order dated 30.12.2015 in Petition No. 216/TT/2014, allowed the actual interest cost while determining the true-up of Power Grid Corporation of India Limited for the MYT period 2009-10 to 2013-14, based on similar grounds.

24. Accordingly, the Appellant prays that the increase of Rs. 59 crores under RoCE, arising from the rise in Weighted Average Cost of Capital and debt cost, be permitted, as its disallowance would cause serious prejudice and would not withstand legal scrutiny.

In re: Tax on the Non-Tariff Income (NTI)

25. The Appellant contends that under Regulation 5 of 2005, Non-Tariff Income (NTI) is to be passed on to consumers. However, Clause 16 of the same regulations restricts the inclusion of tax expenses in the ARR to only those payable on the Return on Equity component of RoCE. This, the Appellant submits, is unjust, as it has actually paid Rs. 160 crores as tax on NTI.

26. Accordingly, it is prayed that either the tax on NTI be passed on to consumers or the entire tax amount be factored into the ARR. In light of the foregoing, the Appellant seeks appropriate relief as set out in the Appeal.

Written Submissions of the Respondent No. 1, APERC

27. The Respondent, Andhra Pradesh Electricity Regulatory Commission, passed the Impugned Order dated 07.11.2015 in O.P. No. 13 of 2015 after considering the views and objections of all stakeholders and in exercise of its powers under Regulation No. 5 of 2005, the Electricity Act, 2003, and the Andhra Pradesh Electricity Reform Act, 1998.

28. The matter pertains to a True-up Application filed by the Appellant under Clause 17 of Regulation 5 of 2005, following the completion of the second control period and prior to the start of the third. Under the Multi-Year Tariff framework, the Appellant (APTRANSCO) is mandated to file its ARR and proposed tariff prior to each control period, and to submit a true-up application at the end of the period to account for variations in uncontrollable items. The Commission then assesses whether these variations are justified and, if so, incorporates the true-up charges into the ARR for the next control period for recovery from consumers through the DISCOMs.

29. Pursuant to this, the Appellant filed its true-up application after the second control period, showing an increase in the approved Gross ARR from Rs. 6037.86 crores to Rs. 6888.05 crores, and in approved Revenue from Rs. 6037.96 crores to Rs. 6266.15 crores, resulting in a revenue gap of Rs. 621.90 crores. After bifurcation

of the State, the Appellant claimed Rs. 287 crores (46.11%) of the total shortfall as its share, to be recovered from consumers via the two DISCOMs.

30. It is submitted that the Respondent Commission has considered the true-up application filed by the Appellant strictly in accordance with Regulation 5 of 2005 by examining every component and item of Aggregate Revenue Requirement, Net Expenditure, and the Revenue as follows;

AGGREGATE REVENUE REQUIREMENT (ARR)

31. The Appellant submits that under Clause 10 of Regulation No. 5 of 2005, the Aggregate Revenue Requirement (ARR) includes components such as Return on Capital Employed (RoCE), Operation and Maintenance expenses, depreciation, taxes on income, and Non-Tariff Income. While examining the True-up Application, the Respondent Commission classified the ARR into two main categories: RoCE and Net Expenditure of the Appellant–TRANSCO.

ROCE

32. The Respondent Commission, in the Impugned Order, examined the Return on Capital Employed (RoCE) in detail from Paragraphs 23 to 35. It evaluated all components, including Regulated Rate Base (RRB), Original Cost of Fixed Assets, and Depreciation calculated in accordance with Clause 15.2 of Regulation 5 of 2005 using the depreciation rates notified by CERC, and also considered the Weighted Average Cost of Capital (WACC).

33. Based on this assessment, the Commission concluded in Paragraph 34 that RoCE, as per Clause 10.4 of Regulation 5 of 2005, is a controllable component of the ARR and found no justification to treat it as uncontrollable.

34. Additionally, the Commission noted that the Appellant had not provided adequate reasons for deviations in the cost of debt from approved benchmarks across the control period.

35. Subsequently, in Paragraph 35 and Table 7 of the Impugned Order, the Commission recalculated the RoCE using RRB and WACC and marginally increased it by Rs. 3.19 crores, determining it as Rs. 1950.04 crores compared to Rs. 1946.84 crores claimed in the Appellant's True-up Application.

NET EXPENDITURE

36. The Respondent Commission analyzed the net expenditure of the Appellant for the second control period from Paragraph 36 onwards of the Impugned Order, with final findings provided at Paragraph 44 and Table 10. The examination was conducted under the following heads:

- a) Operation and Maintenance (O&M) Expenses: The Commission allowed the actual wage cost under Clauses 25.1 and 25.2 of Regulation No. 5 of 2005, resulting in an increase of Rs. 238.4 crores. However, it treated Repair & Maintenance (R&M) and Administration & General (A&G) expenses amounting to Rs. 109.14 crores as controllable, due to lack of supporting data. The Appellant claimed Rs. 1938.64 crores, whereas the Commission approved Rs. 1829.5 crores.

- b) Depreciation: The Commission followed CERC-approved rates under Clause 15.2 of the Regulations and allowed depreciation lower by Rs. 203 crores than the Appellant's claim.
- c) Taxes: In line with Clause 16 of the Regulations, the Commission restricted allowable tax to the amount payable on the equity portion of the Regulated Rate Base. Accordingly, it approved Rs. 207.05 crores, which is Rs. 289.53 crores less than the Rs. 496.58 crores claimed by the Appellant.
- d) One-Time Expenditure: The Commission rejected the Appellant's proposed one-time pension fund contribution of Rs. 650.82 crores, stating that no justification was provided for including such a large amount in the current revenue requirement, which could result in tariff shocks. These adjustments reflect the Commission's application of relevant regulatory clauses in reassessing the true-up claims.

37. The Respondent Commission, after detailed examination, determined the Net Expenditure for the second control period to be Rs. 3686.22 crores, which is Rs. 1254.99 crores less than the Rs. 4941.21 crores claimed by the Appellant in its true-up application.

38. Based on its assessment of RoCE and Net Expenditure, the Commission computed the total ARR for the second control period as Rs. 5636.26 crores. This is lower than both the Rs. 6037.99 crores earlier approved in the original Tariff Order and the Rs. 6888.05 crores claimed by the Appellant in its true-up application, resulting in a total downward variation of Rs. 1251.79 crores.

REVENUE

39. The Appellant's true-up application reflected total revenue of Rs. 6266.15 crores, which matches the amount approved by the Respondent Commission, resulting in no revenue variation in the true-up process. However, when compared to the originally approved revenue in the Tariff Order, there is an increase of Rs. 228.19 crores in revenue variation.

REVENUE SURPLUS

40. As per the Appellant's true-up filing, a revenue deficit of Rs. 621.9 crores was projected for the second control period. However, the Respondent Commission, upon assessment, determined a revenue surplus of Rs. 629.88 crores, based on an approved ARR of Rs. 5636.26 crores and revenue of Rs. 6266.15 crores. Following the bifurcation of Andhra Pradesh and Telangana, a power-sharing ratio of 46.11% was applied.

41. Accordingly, the Appellant was directed to pay Rs. 271.34 crores being its share of the surplus to the two DISCOMs by way of adjustment towards transmission charges during FY 2016-17.

REPLY TO THE 3 KEY ISSUES RAISED/CONTENDED BY THE APPELLANT IN WRITTEN SUBMISSION:

Return on Equity (ROE)

42. It is submitted that the Appellant has raised the issue that the Appellant is entitled 15.5% Return of Equity as per the CERC (Terms and Conditions of Tariff) Regulations, 2009 dated 19.01.2009, however, this issue was never raised before

the Respondent Commission and has been raised for the first time before this Tribunal.

43. Admittedly, as per Para 33 Table 6, pleading has been recorded that the Appellant has claimed only 14% Return of Equity in its true-up application. This fact is also evident on perusal of Para 3 of the Written Submission wherein the Appellant admits “...Appellant filed MYT petition for the 2nd Control period on 29.11.2008 and assumed Return of Equity of 14% as per the then CERC Tariff Regulations...”

44. Hence, the Respondent Commission is bound by the pleadings and prayer in the Application and does not have the jurisdiction to go beyond the pleadings and prayer.

Return on Capital Employed (ROCE)

45. The Respondent Commission noted that Clause 10.4 of Regulation No. 5 of 2005 classifies Return on Capital Employed (RoCE) as a controlled item. However, since the Appellant claimed RoCE to be an uncontrolled item, the Commission examined this contention from Paragraph 24 onward of the Impugned Order.

46. Upon analysis, the Commission concluded at Paragraph 34 that there was no valid basis to treat RoCE as an uncontrolled item and accordingly did not accept the Weighted Average Cost of Capital (WACC) as computed and filed by the Appellant in its true-up application for the second control period.

Taxes on Non-Tariff Income

47. As per Clause 10.4 of Regulation 5 of 2005, taxes on income are treated as uncontrollable items, whereas non-tariff income is considered controllable. In the true-up proceedings, the Respondent Commission allowed tax variation of Rs. 207.05 crores for the second control period.

48. However, the Appellant claimed a total tax expenditure of Rs. 496.58 crores, including tax on income arising from non-tariff income linked to lift irrigation schemes. Applying Clause 16 of the Regulations, the Commission held that the Appellant is not entitled to claim tax on non-tariff income and limited the allowable tax expense to that attributable to the equity portion of the Regulated Rate Base for each year.

49. The Commission noted that the Appellant failed to provide sufficient justification for treating tax on non-tariff income as a recoverable expense, apart from asserting in its written submissions that non-application of Clause 16 would result in a grave injustice.

50. Accordingly, the Commission passed the Impugned Order dated 07.11.2015 in O.P. No. 13 of 2015 under Clause 17 of Regulation 5 of 2005, considering the pleadings and prayers of the Appellant.

51. Subsequently, the Commission also dismissed the Appellant's Review Petition No. 2 of 2016 by order dated 26.08.2016, rejecting the same grounds now raised in the present Appeal.

Analysis and Conclusion

52. After hearing the Learned Counsel for the Appellant and the Learned Counsel for the Respondents at length and carefully considering their respective submissions, we have also examined the written pleadings and relevant material on record. Upon due consideration of the arguments advanced and the documents placed before us, the following issue arises for determination in this Appeal:

Whether the APERC was justified in

- (i) treating Return on Capital Employed (RoCE) as a controllable item fixed at the beginning of the control period, despite its dependence on Weighted Average Cost of Capital (WACC) and the variable nature of interest on debt;***
- (ii) disallowing tax paid on Non-Tariff Income (NTI) for true-up purposes, despite Regulation 5 of 2005 mandating both tax paid and payable to be considered for ARR and NTI to be passed on to consumers; and***
- (iii) fixing the Return on Equity at 14% for the second control period, contrary to the CERC Tariff Regulations then in force, prescribing 15.5%?***

53. The Appellant herein has prayed for the following:

“a. The Appeal may be allowed and the Impugned Order dated 07.11.2015 passed by the Ld. APERC in O.P. No. 13 of 2015 be set aside;

And

b. Any other just and equitable relief in favour of the Appellant as deemed fit by the Hon'ble Tribunal.”

54. This Appeal has been preferred challenging the Order dated 07.11.2015 passed by the Andhra Pradesh Electricity Regulatory Commission (“APERC” or “the Commission”) in O.P. No. 13 of 2015, whereby the Commission undertook a truing up of expenses and revenues for the second control period (FY 2009-10 to 2013-14) under the Multi Year Tariff (MYT) framework pursuant to Regulation 5 of 2005.

55. The impugned order, *inter alia*, determined that there was a surplus of ₹271.34 crores to be refunded by the Appellant to the distribution companies in the residual State of Andhra Pradesh, contrary to the Appellant’s claim of a revenue deficit.

56. The Appellant has raised a challenge to how certain crucial regulatory determinations were made by the Commission in the impugned order.

On Return on Capital Employed (RoCE):

57. The Appellant submitted that RoCE should not have been treated as a “controllable” item under Clause 10.4 of Regulation 5 of 2005 because it is determined by two fluctuating elements: the Regulated Rate Base (RRB) and the Weighted Average Cost of Capital (WACC), wherein the cost of debt, a key component, is subject to market volatility.

58. The base rate of the State Bank of India increased from 7.5% to 10% during the control period, and the Appellant was forced to borrow at rates as high as 12%.

59. It was argued that this external economic factor rendered the cost of debt and, by extension, the RoCE uncontrollable. The Appellant contended that CERC itself,

in analogous circumstances in Petition No. 216/TT/2014, allowed Power Grid Corporation of India to recover actual interest costs.

60. The Commission contended that RoCE is a controllable item under Clause 10.4 of Regulation 5 of 2005. The mere fluctuation of interest rates does not render the item “uncontrollable”, especially since the Appellant made no specific representation for variance during the control period. The Commission noted that the Appellant neither substantiated the change in WACC with material evidence nor justified deviation from approved cost assumptions. The Commission therefore recomputed RoCE based on the originally approved Weighted Average Cost of Capital (WACC) and did not accept the Appellant’s plea for a higher WACC reflective of actual interest rates incurred during the control period.

On Tax on Non-Tariff Income (NTI):

61. The Appellant argued that Regulation 5 of 2005 mandates all taxes paid and payable to be accounted for in determining the Aggregate Revenue Requirement (ARR). The tax on NTI, amounting to ₹160 crores, had already been paid by the Appellant.

62. Since NTI itself is passed through to consumers, the tax incidence on such income should equally be pass-through or else included in ARR.

63. Denying this would impose an undue burden on the Appellant, contrary to the principles of fairness embedded in the regulatory framework.

64. The Commission stated that while taxes on income are an uncontrollable item as per the Regulation, the tax liability must relate only to the equity portion of RRB

and not to income derived from NTI, especially where such income stems from consumer-funded or government-subsidized assets like Lift Irrigation Schemes.

65. Accordingly, only ₹207.05 crores were allowed under taxes, and the balance ₹289.53 crores was disallowed.

On Return on Equity (RoE):

66. The Appellant submitted that while it originally assumed a return of 14% RoE based on the CERC norms applicable to the first control period at the time of filing its petition (29.11.2008), the CERC subsequently revised the RoE to 15.5% via the 2009 Tariff Regulations issued on 19.01.2009, prior to the issuance of the MYT Order on 20.03.2009.

67. It was submitted that APERC was statutorily required to align with CERC norms under Regulation 5 of 2005, and hence ought to have adopted the revised RoE of 15.5%. The continued use of the outdated rate of 14% by the Commission was not only inconsistent with binding norms but also caused financial prejudice.

68. It was contended by the Commission that the Appellant had itself claimed only 14% RoE in its true-up filings and that no prayer for adoption of 15.5% was made before the Commission. As per settled principles, the Commission cannot grant relief beyond the pleadings and prayers of the Applicant. The Commission argued that this issue had been raised for the first time in the appeal and was barred for want of a foundational pleading.

69. The issues that arise for our determination lie at the intersection of regulatory interpretation, economic realities, and principles of fairness.

70. At the heart of the matter are three pivotal determinations made by the Andhra Pradesh Electricity Regulatory Commission in the impugned order; each of which has far-reaching implications for how tariff elements are treated under the Multi Year Tariff (MYT) framework. We will now consider each of the three impugned findings of the Commission in a detailed manner.

(i) Whether RoCE should be treated as a controllable or uncontrollable item under the MYT regime

71. Return on Capital Employed (RoCE) is a foundational component of Aggregate Revenue Requirement (ARR) under Regulation 5 of 2005. The Commission, relying on Clause 10.4 of the said Regulation, has treated RoCE as a “controllable” parameter. The Appellant disputes this treatment on the ground that RoCE, though formulaically derived as a product of the Regulated Rate Base (RRB) and the Weighted Average Cost of Capital (WACC), is susceptible to external market factors, particularly in relation to the cost of debt, and hence cannot be realistically classified as a controllable item.

72. In examining this contention, the Tribunal finds it imperative to first understand the architecture of RoCE under the Regulation. The Regulated Rate Base is composed of fixed assets less accumulated depreciation and normative working capital. The WACC, on the other hand, consists of the weighted average of the cost of equity and the cost of debt. While the cost of equity remains largely constant across the control period (subject to regulatory prescription), the cost of debt is highly sensitive to market fluctuations and macroeconomic policy shifts, including changes in central bank rates, liquidity conditions, and risk premiums imposed by lenders.

73. This Tribunal in ***Tata Power Delhi Distribution Limited vs. Delhi Electricity Regulatory Commission, Appeal No. 301 of 2015, Order dated 28.01.2015*** has held as follows:

“Issue No.8- Erroneous allowance of cost of debt for computation of WACC for the FY 2007-08 to FY 2011-12.

.....

Our View:

29. The issue pertains to the true-up of the cost of debt for the computation of WACC for the first MYT control period, i.e. FY 2007-08 to FY 2011-12 by the State Commission. It is the case of the Appellant that the State Commission has failed to true-up the cost of debt in terms of the judgments of this Tribunal.

30. It has been the stand of the State Commission that in case there is a deviation in SBI PLR rates by 1% (on either side) it would true up the interest rates for loans taken for capital investments and for working capital requirement. Therefore, the sole question which arises for our consideration is whether there was a deviation in the SBI PLR rates by 1% (on either side) during this control period to warrant a true up.

31. Upon consideration of the rival submissions made on behalf of the parties and taking note of the judgment of this Tribunal in Appeal No.36/2008 BSES Rajdhani Power Limited v. DERC decided on 06.10.2009, we do not find the approach of the Commission justified. We find it apposite to quote Para No.115 of the said judgment hereunder: -

“115. Further, the Commission has at the very outset said that it shall true up the interest rate for the new loans to be taken for capital investment and for working capital requirement if there is a deviation in the PLR of the scheduled commercial banks by more than 1 per cent on either side. Thus, there is sufficient safeguard for the Appellant and sufficient room to procure loans at the given market rate of interest. We are not inclined to interfere with the Commission’s decision on the approval of interest rate.”

32. Thus, it was the statement of the Commission itself given to this Tribunal, that if there is a deviation in the PLR of the scheduled commercial banks by more than 1% on either side, they shall true up the interest rate for the new loans to be taken for capital investment and for working capital requirement accordingly. In this case it is not disputed by the Commission that there has been variation of more than 1% in SBIPLR for the FY 2011- 12. In similar circumstances, the Commission has, vide its tariff order dated 29.09.2015 for BRPL and BYPL, revised the rate of interest to 11.29%. The relevant portion of the order is reproduced hereunder:

*“3.32 The Commission had provisionally allowed the actual rate of interest for FY 2011-12. **It is observed that the SBI PLR varied by 2.13% in FY 2011-12 over the previous year**, while the DISCOM was provisionally allowed the interest rate at 4.91% above the normative interest rate for FY 2010-11 in the Tariff Order dated July 2013. **The Commission has decided to revise the rate of interest***

applicable to FY 2011- 12 based on actual variation in average rate for SBI PLR from FY 2010- 11 to FY 2011-12 of 2.13% and revised rate of Interest is 11.29% (9.16% 2.13%). Further, in view of the Hon'ble APTEL's direction in Appeal No 36 of 2008 and Appeal No. 61 & 62 of 2012, the Commission has filed a Clarificatory Application before the Hon'ble APTEL, therefore a view in the matter will be taken, as deemed fit and appropriate, after receipt of the direction of the Hon'ble APTEL In the said application."

33. As, it is clear that SBI PLR varied by more than 1% during the period under consideration, thus requiring, true up of the interest rates for the Control Period. Hence, the State Commission, in accordance with its own submissions as recorded in the above judgment, was bound to true up the interest rate for the Control Period inasmuch as it was obligated to allow the actual rates qua the projections.

34. In this view of the matter, we find force in the contentions of the appellant and set aside the findings of the Commission on this issue. We direct the Commission to re-evaluate the WACC of the appellant for the FY 2007-08 to FY 2011-12 in terms of the statement given before this Tribunal in Appeal No.36/2008 considering the actual rate of interest for debt."

74. The Appellant has placed on record uncontested facts that during the second control period, **the base lending rate of the State Bank of India rose from 7.5% to 10%, and that commercial borrowings had to be secured at even higher rates up to 12% in the later years of the control period.** These variations in borrowing costs were neither within the control of the Appellant nor foreseeable at

the beginning of the control period. The Tribunal takes judicial notice of the fact that such fluctuations in interest rates are characteristic of economic cycles and cannot be reasonably locked in for a five-year control period.

75. It is further brought to our notice that the Central Electricity Regulatory Commission (CERC), in Petition No. 216/TT/2014, considered and approved the actual cost of debt incurred by Power Grid Corporation of India during the corresponding MYT period. This persuasive precedent by the regulatory body underlines the acceptability of accommodating market-driven debt variations within the true-up process.

76. The concept of controllability in RoCE needs to be understood properly. In a stable rate regime, RoCE measures the optimization of capital structure, which includes decisions regarding the mix of debt and equity, and securing debt at competitive interest rates, which can impact the overall cost of capital and thus RoCE.

77. However, when there are unprecedented changes in interest rates/debt market, while a utility can try to secure favorable rates, significant systemic shifts in the interest rate environment, the RoCE may become uncontrollable. In such a situation, Utilities have no options other than raising debt at prevailing rates and seeking reimbursement at the time of true-up. As the respondent has not raised any objection to the prudence of the appellant on debt management, the actual rate of debt needs to be made to pass through the modified WACC.

78. In M/s. TGV SRAAC Limited Vs. Andhra Pradesh Electricity Regulatory Commission & Anr., Appeal No. 413 of 2023 dated 25.09.2024 it was held that:

“43. Regulation 10.3 & 10.6 of Regulation No. 4 of 2015 allows..... the relevant extract is reproduced below :

“55. “Truing up” has been held by this Tribunal in **State Load Despatch Centre v. Gujarat Electricity Regulatory Commission** to mean the adjustment of actual amounts incurred by the licensee against the estimated/projected amounts determined under the ARR. Concept of “truing up” has been dealt with in much detail by this Tribunal in its judgment in **North Delhi Power Ltd. v. Delhi Electricity Regulatory Commission** (North Delhi Power case SCC OnLine APTEL para 60).

“60. Before parting with the judgment we are constrained to remark that the Commission has not properly understood the concept of truing up. While considering the Tariff Petition of the utility the Commission has to reasonably anticipate the Revenue required by a particular utility and such assessment should be based on practical considerations... **The truing up exercise is meant (sic) to fill the gap between the actual expenses at the end of the year and anticipated expenses in the beginning of the year.**”

79. To classify RoCE as “controllable” in such a rigid and unyielding manner, as the Commission has done, is to overlook the underlying economic logic of WACC and its inherently variable character. Clause 10.4 of the Regulation must be read purposively and in light of evolving jurisprudence around cost recovery and investment neutrality. If the regulatory framework is interpreted to penalize actual and prudent borrowing necessitated by macroeconomic changes, it disincentivizes

capital formation, undermines investor confidence, and leads to unsustainable regulatory risk.

80. We are of the view that while the structure of MYT seeks to minimize the impact of year-on-year cost volatility through normative benchmarking, it cannot become a straightjacket that ignores legitimate cost escalations which are demonstrably beyond the control of the utility. The classification of RoCE as “controllable” must therefore be applied with discernment. The Tribunal holds that in cases where the actual cost of debt diverges materially from the approved norms due to external economic factors, RoCE must be treated as an uncontrollable item for the purpose of true-up.

81. The Commission’s treatment of RoCE as a wholly controllable item overlooks the fundamental economic nature of the Weighted Average Cost of Capital (WACC), particularly the variable cost of debt, which is subject to market conditions beyond the licensee’s control. It is a well-recognized principle that while the MYT framework aims to foster efficiency through normative benchmarking, it must remain responsive to unforeseen economic conditions that lie beyond the control of the utility. The denial of a true-up for demonstrable and prudently incurred increases in interest costs defeats the very purpose of post facto reconciliation inherent in the true-up mechanism.

(ii) Whether the Commission erred in disallowing tax paid on Non-Tariff Income (NTI) from being recovered through ARR

82. The second issue pertains to the tax incidence on Non-Tariff Income. The Appellant’s case is that it paid ₹160 crores in taxes on NTI during the control period. The Commission, while allowing ₹207.05 crores of total income tax, disallowed the

portion relating to NTI on the ground that tax pass-through is restricted only to the equity portion of RRB, as per Clause 16 of Regulation 5 of 2005.

83. The Tribunal considers the principle underlying the treatment of NTI within the regulatory scheme. Non-Tariff Income comprises receipts such as interest income, supervision charges, income from rental of meters, and income from assets funded through consumer contributions or government grants (e.g., Lift Irrigation Schemes). Regulation 5 mandates that such income must be passed on to the consumers, thereby reducing the ARR.

84. This passing-on of NTI implies that such revenue is not retained by the licensee but credited to the consumer's benefit. However, when the licensee is nonetheless burdened with the corresponding tax liability, a distortion is created. The licensee is made to absorb the tax cost of an income stream that is not available to it for business use. The Tribunal finds such treatment contrary to principles of revenue neutrality and regulatory consistency.

85. Furthermore, Clause 16 of the Regulation uses the language *"tax on income actually payable and paid,"* which should be read broadly to include tax paid on any income that forms part of the ARR, whether tariff or non-tariff in character. If NTI is being deducted from the ARR, then the tax paid on such NTI must logically be added back; otherwise, the consumer reaps the benefit of the income but avoids responsibility for its tax consequence. This one-sided treatment is economically untenable and legally inequitable.

86. Clause No. 16 of the 2005 Regulations is as follows:

“Clause no. 16 of the 2005 Regulations deals with the Taxes on Income and how they will impact the calculation of the ARR and states as follows:

“16.1 Taxes on Income, if any, on the income stream of the licensed business of the Transmission Licensee shall be treated as an expense and shall be recoverable through ARR.

***16.2 Taxes on Income actually payable and paid** shall be included in the ARR, limited, however, to tax on Return on Equity component of the Return on Capital Employed, and excluding tax on profit, if any, in excess of such return (arising out of any reason, including efficiency of the Transmission Licensee or any explicit incentive provided in the ARR), penalties, interest on delayed payment of tax, etc., and duly adjusted for any refunds, etc. received for the previous periods.”*

87. We find that the Commission committed an error in disallowing the tax burden on revenue, which was not retained by the Appellant but instead passed through to consumers. Such disallowance is not only inconsistent with the accounting logic of ARR formulation but also violates the fairness principle embedded in the regulatory compact.

88. Accordingly, the Tribunal holds that the Commission erred in denying recovery of tax paid on NTI. Once NTI is included in the regulatory revenue stack and passed on to consumers, the associated tax liability must be permitted as an ARR expense.

(iii) Whether the fixation of RoE at 14% was erroneous when the CERC Regulations of 2009 prescribed 15.5%

89. The final issue relates to the rate of Return on Equity (RoE) allowed by the Commission. The Appellant initially claimed 14% RoE in its MYT petition, consistent with the then-prevailing CERC norms for the first control period. However, **subsequent to that filing, the CERC notified its revised Tariff Regulations, 2009 (vide notification dated 19.01.2009)**, wherein the RoE was revised upwards to 15.5%. Despite this, the Commission persisted in applying the 14% figure in its determination.

90. The Commission has justified its action on the ground that the Appellant itself did not amend its prayer or petition to seek 15.5% and is, therefore, estopped from seeking such relief in appeal. It is contended that the Commission cannot suo motu go beyond the pleadings.

91. This Tribunal finds the Commission's approach procedurally correct, for the following reasons:

- (i) We agree with the Commission that the issue of ROE was not raised in the true-up petition before it, as the Commission cannot go beyond the prayer.
- (ii) As per APERC Tariff Regulation 2005, Regulation 10.5, true-up exercise has limited scope only in respect of uncontrollable parameters, and import parameters like ROE cannot be raised in true-up.
- (iii) As the parameters like ROE are decided after following the due process of public hearing, it can be changed only through the due process of amendment of Regulations or Tariff Petition.
- (iv) As per Tariff Regulation 2005, in the Filing procedure (Regulation 6), it is the responsibility of the licensee to propose ROE:

6.2 (c) “A proposal for appropriate capital structure and its cost of financing (interest cost and return on equity) for the purpose of computing Weighted Average Cost of Capital;”

(v) Thereafter, considering the following factors Commission would decide:

“13. Return on Capital Employed:

*re is the Return on Equity and shall be determined at the beginning of the Control Period after **considering CERC norms**, Transmission Licensee’s proposals, previous years’ D/E mix, risks associated with distribution & supply business, market conditions and other relevant factors.”*

92. Hence, it is clear that in addition to CERC norms, other factors would be considered, and the claim that CERC norms should be adopted is not correct.

93. Appellant in its filing dated 29.11.2008 prayed for 14% ROE in its ARR. The Central Commission’s Tariff Regulations were published on 4.1.2009, and APERC vide order dated 20.3.2009 issued the tariff order for the second control period. Appellant had the opportunity to revise its ARR filing or seek review of the order, having a considerable period. However, Appellant, till the filing of the appeal before this Tribunal, never raised this issue before the Commission either during the hearing of the Impugned Order dated 7.11.2015, nor when the review order was disposed of in 2016.

94. Accordingly, we do not agree to the claim of the appellant to allow a higher ROE at the stage of appeal, when no such prayer was made in the true-up petition before the Commission. This prayer, if accepted, will set a bad precedent.

Undoubtedly, the decision on such issues cannot be made without hearing all stakeholders, including the public.

Summary of Findings

95. RoCE can be treated as an uncontrollable item when actual WACC diverges materially from normative levels, considered at the time of tariff order, due to demonstrated market conditions; and there is no evidence of mismanagement of capital by the utility, and while raising debt, it followed the prudence.

96. Tax paid on NTI must be allowed as a recoverable expense within ARR if the NTI itself is passed on to consumers;

97. The prayer to modify ROE for the second control period is rejected.

Conclusion

98. In the considered opinion of this Tribunal, the regulatory determinations made by the Andhra Pradesh Electricity Regulatory Commission in its Order dated 07.11.2015, in O.P. No. 13 of 2015, suffer from material legal infirmities and regulatory misapplication in respect of two specific components of the Aggregate Revenue Requirement (ARR), namely: Return on Capital Employed (RoCE), and tax on Non-Tariff Income (NTI).

ORDER

For the foregoing reasons as stated above, we are of the considered view that the captioned Appeal No. 37 of 2017 has merit and is allowed to the extent indicated

hereinabove. The Impugned Order dated 07.11.2015 passed by the Andhra Pradesh Electricity Regulatory Commission in O.P. No. 13 of 2015 is set aside to the limited extent of:

- Re-computation of RoCE based on actual Weighted Average Cost of Capital incurred by the Appellant;
- Inclusion of tax paid on Non-Tariff Income in the Aggregate Revenue Requirement for the second control period;

The matter is remanded to the Commission for recalculating the true-up amount in accordance with this judgment and passing a fresh order within three months from the date of receipt of this judgment.

The Captioned Appeal and pending IAs, if any, are disposed of in the above terms.

PRONOUNCED IN THE OPEN COURT ON THIS 3rd DAY OF JULY, 2025.

(Virender Bhat)
Judicial Member

(Sandesh Kumar Sharma)
Technical Member

REPORTABLE / ~~NON-REPORTABLE~~

pr/mkj/kks