AIDA Study | Dynamics of Tariff and True-up Mechanisms

Objective & Scope of the Study| Key Parameters & DISCOMs considered

This study has been conducted by AIDA, which led the study's design and strategic direction, under the expert supervision of Shri U.N. Behera, former Chairperson of the Odisha Electricity Regulatory Commission (OERC).

This study analyzes the tariff orders and true-up orders issued by SERCs for Distribution Companies (DISCOMs) to evaluate compliance with key provisions outlined in Tariff Policy 2016 and Electricity Rules and its amendments by the MoP.

- This study analyzes 7 parameters for 7 DISCOMs across 7 states.
- DISCOMs have been selected to represent all 5 regions (Northeast, North, South, East & West) and state and privately owned DISCOMs along with Union Territory representation.
- DISCOMs with higher ACS-ARR Gap compared to other DISCOMs within the same State/ UT iwith multiple discoms have been shortlisted for the study

Parameters Considered

1. **Power purchase costs-** Limit on short-term purchases, Disallowances due to higher distribution loss target and Sharing of losses on account of power purchase with the consumers
2. **Regulatory Assets (RA)-** Quantum of RA & trend and whether carrying cost is allowed
3. **Fuel and Power Purchase Adjustment Surcharge (FPPAS)-** Automatic pass on of FPPAS on monthly basis and whether carrying cost is allowed
4. **Tariff Subsidy-** Whether SERC has notified a Tariff Schedule without considering subsidy, as required by Tariff Policy
5. **O&M Norms-** whether in line with the CEA "Guidelines for Benchmarking of Operation & Maintenance (O&M) Norms for Distribution Utilities"
6. **Prior-period adjustments**- Adjustment of prior period gain/loss in ARR
7. **Cross-subsidy-** Whether it is within a band of 20%

DISCOMs Considered

Sr. No.	States	Name of DISCOM
1	Assam	APDCL
2	Delhi	BRPL
3	Jharkhand	JBVNL
4	Karnataka	MESCOM
5	Madhya Pradesh	MPMaKVVCL
6	Tamil Nadu	TANGEDCO
7	Uttar Pradesh	PuVVNL

Key Observations………(1/3)

Power Purchase Cost

- The Electricity Rules require SERCs to adopt AT&C loss trajectories aligned with the RDSS, yet most commissions continue to use distribution loss targets instead, often set below RDSS benchmarks.
- Most commissions disallow excess power purchase costs, when actual losses exceed these approved targets, though the basis for calculating disallowance varies by state—some use the Average Power Purchase Cost, while others apply alternative methodologies.
- Resource Adequacy regulations have been notified in most states (except Delhi & Uttar Pradesh), typically capping short-term contracts at 10–15% for meeting resource adequacy, with allowances for exigency purchases subject to post-facto submissions within 15–45 days. However, low caps and prior-approval requirements can impede the quick decision-making needed for short-term procurement.
- Overall, while SERCs follow their own regulations, most do not share losses with consumers—contrary to the Electricity Rules, which envisage a 2/3:1/3 split between licensees and consumers. These practices, combined with large disallowances, materially impact ARR and weaken DISCOM financial health.

Regulatory Assets (RA)

- All states except Karnataka have RA regulations, and most allow carrying costs.
- However, across states, approved carrying cost rates are below the base LPS rate, creating a financial shortfall for DISCOMs and liquidation timelines are often undefined, risking protracted recovery periods.
- Most commissions are not creating new gaps, aligning with Electricity Amendment Rules 2023. RAs are generally constant or declining except in Uttar Pradesh.

FPPAS Mechanisms

- Five of the seven states allow automatic FPPAS adjustments, with monthly or quarterly frequencies.
- Most states enable timely FPPAS recovery, but design and rigor vary.
- Assam and Madhya Pradesh are the most comprehensive; Tamil Nadu is the most restrictive; Uttar Pradesh follows a hybrid model with distinct caps.

Key Observations………(2/3)

Tariff Subsidy

- All reviewed states notify full-cost, subsidy-independent tariffs, as required, enabling governments to provide targeted support separately and improving transparency and cost reflectivity. However, not all states provide tariff subsidies in their tariff order.
- Some states like Assam and Uttar Pradesh have specified category wise subsidies within tariff orders to reduce disputes, others may also follow it.
- Assam, Tamil Nadu, Uttar Pradesh have high subsidy component as part of revenue which exposes DISCOMs to risk due to delays, contributing to national dues. While states like Karnataka face less risks as subsidy components are low.

O&M Norms

- The importance of robust O&M benchmarks, including CEA guidelines, is underscored. ed to balance adequate spending with efficiency improvements
- CEA recommend categorizing O&M expenses into the three heads (Employee, R&M, A&G), applying normative controls linked to operational metrics, and incorporating efficiency incentives like gain/ loss sharing. However, States like Delhi, Karnataka and Tamil Nadu has not provided the breakup of O&M expenses into the three heads.
- No state treats special schemes like RDSS separately, and only Delhi and Jharkhand share gains/ losses with consumers, missing CEA’s efficiency incentives and risking O&M cost overruns.
- States such as Delhi and Madhya Pradesh demonstrate greater alignment with the guidelines, while Assam and Tamil Nadu show more significant deviations. This variation reflects differing timelines in the adoption of guidelines across jurisdictions.

Key Observations………(3/3)

Prior-Period Adjustments

- Prior-period gains have not been explicitly adjusted in the approved ARR of the current year in any of the reviewed states. . Except Uttar Pradesh, no DISCOM has surplus in the previous years
- Although ARR shows no prior-period surplus adjustments, state commissions are still addressing prior-period items via true-ups, surplus pass-throughs, or pending regulatory decisions; disclosure is not always explicit in ARR lines.
- Assam has surplus in the current year which has been adjusted in the revenue from tariff and accordingly tariff and cross-subsidy has been reduced to pass through the surplus in the current year to consumers. This shows improving financials of distribution licensee APDCL and inclination of state commission toward tariff rationalization when surplus exists.
- Regular approval, publication and updation of tariff orders is essential, otherwise, risk of overstating/understating the present requirement arises, such as in the case of Delhi (BRPL) and Tamil Nadu (TNPDCL), and there is a high likelihood of changes since and hence these data may not represent true picture

Cross-Subsidy

- Cross-subsidy levels vary significantly across consumer categories. The analysis points to the need for progressive reduction of cross-subsidies and better targeting of subsidies.
- As a matter of policy, cross-subsidization should be reduced to a minimum (within +/- 20% of ACoS). If there is a need for subsidizing particular types of use or specific categories of consumers, government may provide targeted subsidies for those purposes.
- Despite repeated focus on reducing cross-subsidization, this continues to significantly distort the tariff structure. Industrial tariff being 28-35 % higher than the cost of supply acts as a serious impediment to industrial growth. Same is the case with commercial tariff being as high as 51% above the cost of supply.