Chapter 2
REGULATION OF THE INDUSTRY

Regulation of a public utility is its inseparable adjunct.

Public utility industry is characterised by the essential nature of the demand for its product or service on the one side, and the monopoly control over the supply of its product or service on the other. The inelastic demand for the product or service strengthens the monopoly power of the supplier. The industry involves huge capital investment and the bigger it is, the more economical and efficient it becomes by obtaining economies of scale. Its physical requirements also make it impossible for more than one supplier to be in business in one locality. In electricity supply industry, for example, cables or overhead mains of rival suppliers cannot be accommodated. In view of these circumstances, the industry is legally vested with monopoly powers.

Like any other monopoly, a public utility is likely to abuse its power. The abuse of power may take the forms of low quality of product/service or stoppage of supply, exploitative prices, and discrimination among consumers. A word of explanation need be added about discrimination—its use and misuse, with reference to electricity supply. Discrimination is useful in that each class of consumers can be charged what it can bear.
This by itself is equitable. Furthermore, if a lower charge to any class of consumers leads to a large increase in demand which in its turn leads to economies of large scale, the benefit accrues to all. If, thus, discrimination helps a nation-building service, it can be made even an instrument of public policy. If, for example, low electricity charges in rural areas are likely to promote use of power in agriculture or to popularise use of lights so as to make villages attractive, this kind of discriminatory policy may be made obligatory upon the supplier by the government rather than suppress it. On the other hand, other forms of discrimination between a buyer and a buyer in similar conditions must be suppressed.

In view of the possible abuses of its power the industry has to be regulated. The government can do this as a condition of vesting the industry with monopoly powers. Regulation which is thus essential can also be utilised for certain additional social purposes. Regulation can be used, for example, to avoid damage to the larger interests of the society and to achieve planned development of community's resources. Further, the industry of electricity generation and distribution has its own hazards. Regulation is needed to prevent these hazards.

Regulation, on the other hand, must be such that it does not hamper the normal growth of the public utility
industry. There should be no undue interference with the conduct of its business and also with supply of resources which in general interest should have been drawn into this industry. As supply of resources depends on returns, public regulation must not jeopardise fair returns.

In the light of these considerations, we have to review the regulation of electricity supply industry in this country. As said in the previous chapter, the industry is regulated under the Indian Electricity Act, 1910, the Electricity Supply Act, 1948 and the Indian Electricity Rules. The provisions of the ES Act are in addition to, and not in derogation of IE Act unless it is otherwise provided in the former. Where provisions of the ES Act are inconsistent with any provisions of the IE Act, the former prevail.

I

The Indian Electricity Act, 1910

The IE Act of 1910 was amended in 1922, 1923, 1937 and 1959. The last amendment was more substantial than the earlier ones. After the ES Act of 1948, it was necessary to make changes in the IE Act, not only because the two Acts were to be coordinated but also, and more importantly, to enable the State Electricity Boards to exercise stricter control over licensees and to take powers to regulate the distribution, supply, consumption and use of energy in certain circumstances.
We will proceed to consider only such provisions of the ES Act as are relevant for this study.

Grant of a Licence (Section 3)

The State Government is authorised to grant to any person a licence to supply energy in a specified area, on application from the person in a prescribed form. In the Electric Lighting Act, 1882, in England, one of the conditions of the grant of a licence is the consent of the local authority. This gave a specially advantageous position to the local authority, a fillip to municipal undertakings of electricity supply. In India no consent by the local authority is necessary for the State Government’s grant of a licence. The State Government has to consult the Electricity Board before granting the licence. Under Section 28 of the ES Act the Electricity Board prepares its own scheme of supply of energy and also under Section 55 and other sections of this Act the Board has powers to control the licensee. Hence it is an obligation of the Government to see that the licence to be issued fits into the scheme and policy of the Board.

Contents of a licence (Section 3 & Schedule & Rule 13)

The principal contents of the licence are the limits of the area in which energy is to be supplied, nature of the supply, rates allowed to be charged for the supply, the first and subsequent periods on the expiry of which the option to purchase the undertaking by the local
authority or the State Government may be exercised, and the terms and conditions of purchase. The area of supply may be classed into the area where supply is compulsory and the area where it is permissive. This may be done at the desire either of the licensee or the State Government. Unless the State Government waived, under Clause (b), Section 10 of the Act, its option to purchase the licensee's undertaking, it will specify in the licence the period on the expiration of which it may exercise the option for the first time and subsequently. The right to purchase vested in the local and the State Governments prior to the amendment of 1959 and it vests in the Electricity Board after the amendment as will be explained below.

The Schedule to the IE Act is deemed to be incorporated in the licence, with the additions, variations and exceptions that the State Government may expressly state. These additions, variations and exceptions or the provisions of the Schedule with these changes have to be stated in the licence itself. The provisions of the Schedule pertain to security and accounts, conditions for the execution of compulsory work and supply, safety of the consumers and the public, and continuous supply, method of charging, maximum charges, minimum charges and charges for public lamps. The provisions regarding tariff stood annulled on the application of the ES Act, VI Schedule as the latter dealt with this.¹

¹ This was decided by the CEA in 1956 in an appeal of the Ahmedabad Electricity Co. against the Bombay Electricity Board.
Revocation of a licence (Sections 4 & 5)

The State Government may revoke the licence if in its opinion the public interest so requires. The requirement of public interest in government action is too obvious to need comment. That it is the opinion of the Government is the crucial point. The Government is under no obligation to appoint a committee - an expert committee or a judicial committee - to enquire into the grounds of revocation. Nor is the Government's opinion or satisfaction justiciable. In some cases the Government is required to consider "any cause shown by the licensee against the proposed revocation". In cases where the revocation is done on the application or with the consent of the licensee, the Government takes the action upon such terms and conditions as "it thinks fit", after consulting the Electricity Board, and Central Government if it is interested and the local authority (if it itself is not the licensee).

The grounds of revocation are, in brief, that (i) the Government is not satisfied that the licensee is in a position fully and efficiently to discharge the duties and obligation; (ii) wilful and prolonged default in the duties by the licensee; (iii) default in complying with the directions issued by the State Government under Section 22A of the IE Act; (iv) financial position of the licensee being such that he is unable fully and efficiently to discharge the duties and obligations, and (v) an application of the licensee to the effect that the licence
may be revoked. The licensee is likely to apply for cancellation of his licence if he is in financial stringency or if he thinks that his business is not paying adequately. Several restrictions under the Sixth Schedule of the ES Act have, as will be shown later, a bearing on this state.

Electricity supply is a highly capital-intensive industry, and adequacy and efficiency of supply greatly depend upon the capital investment. Hence the Government must see that the industry does not remain in the hands of licensees who are financially weak parties. This ground for the revocation of the licence was substituted by the amendment of 1959 for another which invoked this action of the Government in case of insolvency of licensee. The present provision is broader than the one it replaces. 'Insolvency' has also a legal connotation (e.g., it is adjudged insolvency) which is avoided in the present provision.

After the licence is revoked the licensee is required to sell the undertaking to different parties in this order: (1) the Electricity Board, (2) the State Government, (3) the local authority and (4) any other person. The price to be paid by these parties is governed by Section 7 of the ES Act. If the licensee is not required to sell his undertaking thus, then only he has the option of disposing of it in such manner as he may think fit.
He must exercise this option in six months from the date fixed for the revocation taking place, failing which the Government would get the works of the licensee removed. These stipulations in respect of the sale are likely to affect the licensee adversely.

There is however, no redress for the licensee under the Constitution. In the 'Narayanam Shankaran V. State of Kerala' (1966) it was decided that the provision of revocation did not violate Article 14 of the Constitution. In 'Silchar Electricity Supply Co. v. Secretary' (1969) it was declared that the act of revoking or amending the licence is administrative and not judicial.

Amendment of a Licence (Sections 4 and 4A)

A licence may be amended on the initiative of the Government or on an application of the licensee. An amendment presumes that the licensee is capable of conforming to the changes made in the licence (i.e. increased obligations of the licensee) and that the inadequacies are such as can be remedied by these changes. Not infrequently amendment of a licence becomes a prelude to revocation.

Amendment of a licence may be indicated in the more normal way. The licensee, for example, may ask for extension of his area. The Government, for example, may in public interest ask the licensee to take further obligation. In helping extension of facilities and rationalisation of the industry. The Government has many
occasions to amend licences granted a long time ago, particularly before the passing of the BS Act of 1948. Amendments of this type can be done not without consent of the licensee and after consulting the Electricity Board and the local authority (if it is not itself the licensee). To forestall unreasonable resistance of the licensee it is provided that the consent of the licensee is not a condition if it "has in the opinion of the State Government, been unreasonably withheld". Here again the opinion of the State Government is final.

Purchase of undertakings (Section 6)

The Electricity Board is vested with powers to purchase the undertaking of a licensee other than a local authority under Section 6 of IE Act as amended in 1959. This purchase is a "compulsory purchase" as distinguished from the purchase arising out of revocation of a licence. This section is substituted for the earlier one by the Amendment of 1969. The purchase can be made in the case of a licence granted before the commencement of the said amendment on the expiration of the period specified in the licence; in the case of a licence granted on or after the above date, on the expiration of a period not exceeding twenty years and every subsequent period not exceeding ten years.2

2. The period operates from the date of commencement of the licence. Is it the date of issue of the licence or the date of its publication in the Gazette? Rule 18 said that it was the latter. However, the Supreme Court ruled that it was the former in the Godhra Electricity and Another V. The State of Gujarat and Another (1973). Now the Maharashtra Ordinance No.XVIII of 1974 specified it as the date of publication in the Gazette.
The purchase will be made by public authorities in the following order: first the Board, second the State Government and third the local authority. It may be noted that the local authority is clearly distinguished from other licensees and it as a licensee has been kept out of the purview of this section. Also the local authority is made competent to take over the undertaking of another licensee.

**Purchase Price (Section 7A)**

Whether an undertaking is purchased under Section 6 (as a sequel to revocation of a licence) or under Section 6 (as a sequel to expiration of the period of a licence) the purchase price to be paid to the licensee other than a local authority is "the market value of the undertaking" at the time of purchase (or delivery if it is effected before purchase). Dispute regarding the price shall be determined by arbitration. In respect of the licensee being a local authority, the State Government will determine the purchase price having regard to the market value.

It is specifically laid down in the SE Act that the market value will be "without any addition in respect of compulsory purchase or of goodwill or of any profits which may be or might have been made from the undertaking or of any similar consideration". Only in case of compulsory purchase under Section 6, however, "there shall be added
to such value such percentage, if any, not exceeding twenty percentum of that value as may be specified in the licence on account of compulsory purchase". This consideration does not arise when the licence is revoked either for default etc. or an application on the part of the licensee.

Goodwill of an enterprise in a competitive industry is a thing different from the goodwill of a monopoly enterprise like an electricity undertaking. In a competitive industry, an enterprise creates goodwill about itself, distinguishes itself from others and thus partly creates new demand and partly draws it from other enterprises. Goodwill involves a high cost of creating it under competition. In a monopoly enterprise creation of goodwill does not necessitate such a high 'selling cost'.

Besides, in the case of electricity enterprise it may be added that the industry is subject to very rapid decline in cost if the load increases. Though load building involves a high cost it is a necessary part of the cost of running the industry and gain from utilising the surplus installed capacity is likely to outweigh the increment in cost (inclusive of selling cost) to a greater extent than in a competitive enterprise. In the case of electricity and other public utilities goodwill may also be regarded partly as a product of the franchise, not a creation of the concern. Regarding equity in excluding goodwill, it is observed by D.J.Bolton, "No question of
justice or equity here arises, since the terms were known from the outset and the company has operated throughout on this understanding.\(^3\)

Under Section 5, revocation of a licence being a punitive measure the question of paying indemnity does not arise. Under Section 7 too the question of indemnity does not arise because the compulsory purchase after the expiry of a certain number of years is a condition of the grant of a licence; it is a part of the contract between the licensee and the Government.

It is curious to note that the only difference made to the provision about purchase price by the Amendment of 1959 is the substitution of the words 'market value' in place of 'fair market value'. The description of the value, however, in the statute both before and after the amendment is the same. It is the value of lands, buildings, materials and plant less than that of the generating station if it was declared in the licence as no part of the undertaking for the purpose of purchase, less the value of service lines etc. constructed out of expenses to consumers, due regard being had to the condition of the assets and their usefulness for immediate working. It seems that the intent of the IB Act in this behalf both before and after the amendment is the same. The word 'fair' qualifying market value is dropped to avoid

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complexity and vagueness in the concept. In economic literature, the two concepts are different. However, in his classic study James Bonbright has pointed out that even if the statute refers merely to market value, the courts have held that the attribute of fairness must be impoorted into the term. 4

There can never be fully satisfactory a position in respect of purchase price of an undertaking. The Advisory Board5 had suggested "book value less depreciation". Of all valuations this is the minimum. The Federation of Electrical Undertakings objected to this principle. It is worth quoting. "The accounting fiction whereby the value of an asset is deemed to decline at a certain rate till it becomes nil, or nearly so, at the end of an arbitrarily fixed period of years is only a convenient device for purposes of annual book-keeping. It does not necessarily follow that such a device could or should be used to determine the true value of the asset at any time. Indeed the asset may have reached e.g. the end of its 'accounting' life, but by reasons of such factors as the quality of maintenance afforded to it and its general utility etc., it may have more years of actual life remaining to it." 6

5. This was appointed under section 35 of IE Act and it recommended amendments to be made to this Act.
6. Quoted from its Memorandum made available to the present writer by the Secretary of the Federation.
This view is strengthened by the Supreme Court judgement in the 'State of Bengal v. Mrs. Bella Banerjee and others' (1952). To quote, "What is determined as payable must be compensation, that is, just equivalent of what the owner has been deprived of". Under the Constitution, the legislature lays down the principles of compensation. "Whether such principles take into account all the elements which make up the true value of property appropriated and exclude matters which are to be neglected, is a justiciable issue to be adjudged by the court."

The Amendment of 1959 added that "......The licensee shall deliver the undertaking to the State Electricity Board, the State Government or the local authority, as the case may be, on the expiration of the relevant period .......pending the determination and payment of the purchase price". Thus the undertaking can be acquired without the licensee getting the price quite for some time! In the Godhra Electricity Co. case mentioned earlier the Supreme Court declared that the non-determination of price etc. contravened the licensee's right under Section 19, Clauses (f) and (g), of the Constitution. Hence some States (among them Maharashtra, Gujarat, Tamil Nadu and Assam) have passed legislation to fix the price and mode of payment. The mode of payment includes payment in bonds, payment in instalments, and payment of interest on the price payable during the period between
take-over and actual payment. The Maharashtra State, for example, will pay interest equal to the Bank Rate plus one per centum.

A word may be added about the solatium to be paid. It is likely that as the next option of purchase is nearing, the licensee may make unnecessary or unduly large investment so that he would earn a percentage (stipulated in his licence) on that as solatium. To forestall this there is a provision in Schedule VI of the ES Act. This provision requires that where at any time within three years before the next option of purchase the licensee proposes to make capital expenditure which exceeds in any year an amount of 25 thousand rupees or two per centum of the Capital Base, whichever is more, the licensee shall, before giving effect to such proposal, apply to the Electricity Board for its concurrence. Whether this provision applies to stores also is not clear.

Nationalisation

Above sections regarding revocation of a licence and purchase of an undertaking fade into the background as powers are acquired recently by the Government under section 39 of the Constitution to take over private property.

The Tamil Nadu Electricity Supply Undertakings (Acquisition) Act of 1964 provided for nationalisation of the undertakings of licensees including local authorities on payment of compensation and with four months' notice. In respect of private licensees it is replaced by Tamil
Nadu Private Electricity Supply Undertakings (Acquisition) Act of 1973. In the latter there is no reference to notice period and also the rate of compensation has been reduced. The compensation would be twelve times the average net profit of the undertaking as during a period of five years at the option of the licensee during the preceding seven years or it would be the net book value of assets in use. In the latter case there is a solatium added at specified rates and the licensee has the option between the two bases of calculation.

This Tamil Nadu legislation is a different type from the rest. It is 'acquisition' legislation. Other legislation provides for regulation in the normal conduct of the undertaking with further measures (1) to cancel their licence for their failure to fulfill their obligations and (2) to take over enterprise after the expiration of the licence. Tamil Nadu legislation is in exercise of the Constitutional provision under Section 39 and it is the type that is likely to be practised in the future, though the scale of this practice is uncertain.7

Restriction on Transfers and Mergers (Section 9)

Regulation includes restriction on transfers and mergers etc. The Act requires that without the consent

7. A Committee under the chairmanship of B.N. Kureel (Dy. Minister of Irrigation and Power of the Government of India) recommended acquisition of private undertakings in order to frustrate any malpractices by the licensees. The Report of the Committee is not published. See Weekly Commerce, July 16, 1972. We understand that the Planning Commission has expressed itself against nationalisation.
of the State Government the licensee shall not acquire the licence or undertaking of another licensee. Nor will he associate himself with another licensee so far as the business of supply of energy is concerned. He will also not assign, without the consent of the Government, his licence or undertaking or any part of it, by sale, mortgage, lease, exchange or otherwise.

Partnership and investment by a licensee in the shares of another licensee also come under the purview of this section.  

II

The Electricity Supply Act of 1948

This Act was a distinct landmark in the regulation and the development of electricity supply industry in this country. Whereas the earlier legislation of 1910 was for regulation this Act was mainly for development of the industry. The object of this statute as stated by the Central Government may be quoted herein extenso.

"The coordinated development of electricity on a regional basis is a matter of increasingly urgent importance for reconstruction and development. The absence of coordinated system, in which generation is concentrated in the most efficient units and
bulk supply of energy centralised under the direction and control of one authority is one of factors that impedes the healthy and economical growth of electrical development in this country. Besides, it is becoming more and more apparent that if the benefits of electricity are to be extended to semi-urban and rural areas in the more efficient and economical manner consistent with the needs of an entire region, the area of development must transcend the geographical limits of a Municipality, a Cantonment Board or a Notified Area Committee, as the case may be. It has, therefore, become necessary that the appropriate Governments should be vested with the necessary legislative powers to link together under one control electrical development in contiguous areas by the establishment of what is generally known as the 'Grid System'. In the circumstances of this country such a system need not necessarily involve inter-connection throughout the length and breadth of a Province; regional coordination inclusive of some measure of inter-connection may be all that is needed. An essential prerequisite is, however, the acquisition of necessary legislative power not only to facilitate the establishment of this system in newly licensed areas but also to control the operations of existing licensees so as to secure fully coordinated development.9

The Act declares its object to be "to provide for rationalisation of the production and supply of electricity and for taking measures conducive to electrical development and for matters incidental thereto." In the original Act electrical development of the "Provinces of India" was mentioned. By an order of 1950 the words "Provinces of India" were deleted. With the deletion of these words the Grid that may be visualised is not only provincial but extended to the country as a whole. The object as stated by the Central Government in the words quoted above (viz., "Such a system need not necessarily involve interconnection throughout the length and breadth of a province; regional coordination inclusive of some measure of inter-connection may be all that is needed.") may now look a little tame.

Development would mean extension of supply throughout the country including rural areas. Development would also mean increase of supply over any given area. From the statistics of supply in this country in the previous Chapter it is obvious that much has to be done in respect of development in both the senses. In this development, public sector would be given a big role to play.

Rationalisation would mean coordination of public and private sectors; regulation of private sector with a view to maximising efficiency and safeguarding interests
of the public; coordination of power policy of the
country with the needs of economic development; coordi-
nating power policy with the energy policy of the country;
coordination of the programme of generating electricity
from water, oil, gas, coal and non-fossil fuels; appro-
priation of hydro-power consistent with the requirements
of irrigation, navigation and flood control, and adop-
tion of measures to raise general efficiency of the
industry including, in particular, measures of expansion
of scale of production, full utilization of plant capac-
ity, removal of regional shortages and surpluses, and
adoption of most up-to-date techniques of manufacturing.

We will have to examine the SE Act in regard to
these purposes. The three authorities that are respon-
sible under this Act are, the Government, the CEA, and
the State Electricity Boards. Powers of each differ in
deepth and in extent in respect of regulation, planning
and development. Powers of the Government are mentioned
below while citing those of the latter too.

Duties of the Central Electricity Authority

The most important of the functions of the CEA is
making investigations and framing policy. The CEA has
no regulatory function even indirectly. In regard to
investigations and policy-making the relations of the
CEA with the State Boards will be crucial.
The Board from time to time prepares its schemes of generation, transmission etc. with a view to rationalising the production and supply of electricity in any area. If capital expenditure on such schemes exceeds one crore rupees they shall not be sanctioned by the Board without prior consultation with the Authority and until any recommendations which the Authority may make upon such consultation have received due consideration by the Board (Section 29). If the recommendations of the CEA are not accepted, the Board shall not sanction the schemes without the previous consent of the State Government. From this account it is clear that in planning of power development and of rationalisation of power supply the CEA is not likely to be very effective. Before the Amendment of 1956 schemes exceeding capital expenditure of Rs. 15 lakhs had to be referred to the CEA. Now it is to be consulted on larger schemes (involving over Rs 1 crore) only and its recommendations can be superseded by the consent of the State Government. This is particularly a serious drawback in planning on a national basis.

Coordination between the Board's schemes and multi-purpose river valley schemes is provided. This coordination is necessary for two reasons: (1) Board's electricity scheme and a multi-purpose scheme of a Corporation or Government for the same area must be harmonised, (2) The multi-purpose scheme may involve more than one State.
The Board which plans its scheme on the State-basis must dovetail its activities with the authority that plans its activities on the region-basis, or nation-basis.

It is required that the Board will make regulation in regard to "principles governing the fixing of Grid Tariff" and "principles governing the making of agreements with licensees under section 49" with "the concurrence of the Authority" (Section 78).

Powers and Duties of the State Electricity Board

The State Government shall form State Electricity Board. The Board shall be charged with the general duty of promoting the coordinated development of the generation, supply and distribution of electricity within the State in the most efficient and economical manner, with particular reference to such development in areas not for the time being served or adequately served by any licensee. (Section 13). This involves supply of electricity, particularly to rural areas, by the Board itself and also the Board's control on the establishment, extension and operation of power stations by licensees. To this end the Board must also be vested with certain general powers or functions.

A) General powers of the Board

1) The Board may take such measures as in the opinion of the Board are calculated to advance the development
of water-power in the State, and may organise and carry out power and hydrometric survey work and cause to be made such maps, plans, sections and estimates as are necessary for this purpose (Section 21).

ii) In regard to water-power, the Board may at its own expense conduct such investigations, experiments, and trials as it thinks fit for the improvement of the methods of transmission, distribution and supply of electricity or the utilisation of fuel, water-power or other means of generating electricity, and may establish and maintain laboratories for the testing and standardisation of electrical instruments and equipment (Section 22).

iii) The Board may at any time by notice in writing require any licensee or person supplying electricity for public or private purposes or generating electricity for his own use to furnish it with such information and accounts relating to such supply or generation and in such form and manner as the notice may specify.

B) Powers in regard to generation, supply and distribution of electricity in the Scheme area

"With a view to rationalising the production and supply of electricity in any area the Board may from time to time prepare a scheme for any area which will provide for the following,

(a) the establishment of the Board's own generating stations;
(b) the designation of generating stations, whether existing station or new stations, as controlled stations at which electricity shall be generated for the purposes of the Board;

(c) the inter-connection, by means of main transmission lines to be constructed or acquired by the Board, of any generating stations with any others and with any systems of licensees;

(d) where a scheme relates to specified area, the inter-connection of the system of the Board in that area with the system of the Board in any other area with respect to which a scheme is in being or may subsequently be made;

(e) the construction or acquisition of such other main transmission lines as the scheme may require;

(f) the use by the Board of any transmission lines or main transmission lines of any licensee;

(g) such supplemental, incidental and consequential provisions as may appear necessary or expedient for any of the purposes aforesaid (Section 28).

This planning will be obviously on State basis.

Schemes with capital expenditure exceeding fifteen lakhs of rupees cannot be prepared by the Board without prior consultation with the State Government. Schemes with capital expenditure exceeding twentyfive lakhs of rupees have to be published in official Gazette so that
representations may be received from licensees and other interested persons.

In the Scheme area the Board has the following powers and duties.

1) In this area the Board itself will establish a new generating station but with the sanction of the State Government. It may make arrangements with any licensee or other person for the establishment of a new generating station, if in the opinion of the Board it is desirable to do so (Section 38).

ii) The Board may at any time declare to a licensee owning a generating station, other than a controlled station, that it is ready to make a supply of electricity available to the licensee for the purpose of his undertaking and may do so (Section 38).

iii) The Board may at any time declare to a licensee owning a generating station that the station shall be permanently closed down and the licensee will be a distributing licensee (Section 38).

iv) The Board can purchase controlled stations under Schedule I of the Act.

C) The Board's powers in regard to licensees and persons in the whole of the State

1) The Board may enter into arrangements with any person producing electricity within the State for the purchase by the Board of any surplus electricity which that person may be able to dispose of (Section 43).
(ii) It shall not be lawful for a licensee or any person, not being the Central Government or any Corporation created by a Central Act, except with the previous consent in writing of the Board, to establish or acquire a new generating station to extend or replace any major unit of plant or works pertaining to the generation of electricity in a generating station (Section 44).

(iii) The Board may grant loans and advances to any licensee for the purpose of his undertaking.

In the discharge of its functions it may call upon a licensee to expand his undertaking and offer to advance to him a loan on such terms and conditions as it may deem proper for such expansion, and if the licensee refuses, fails or neglects to accept the loan from the Board or to raise a loan from other sources or to employ his own funds on terms similar to those offered by the Board, the Board may purchase his undertaking (Section 23).

(iv) Unless otherwise agreed between them, the licensee will not purchase electricity from the Board at an average Power Factor below 0.86 (Section 52).

(v) No licensee shall, except with the previous approval in writing of the Board and subject to any conditions which the Board may think fit to impose, enter into any arrangement whereby any generating station is to be let or held on lease by him (Section 56).

(vi) Every licensee shall comply with such directions as the Board may from time to time give him for the
purpose of achieving the maximum of economy and efficiency in the operation of his undertaking or any part thereof (Section 58). Before the Amendment of 1956 these directives were limited to the operation of the station. The scope of the directives is now extended to the undertaking.

vi) The Board shall have the power to direct the amortisation and tariff policies of any licensee, being a local authority. The local authority shall give effect to such directions (Section 5).

A commentary on Powers and Duties of the Board

All these powers and duties of the Board which we have divided above into three categories (A, B, C) are aimed at effecting planned development of electricity industry and, also protecting the interests of licensees and persons interested in the industry on the one hand and those of the consumers on the other. Protection of consumers' interests does involve a curb on the powers of licensees and persons supplying electricity. The Board, however, must see that in the control of the industry the licensees and persons concerned are given a voice in the determination of controls and also certain rights of theirs are not violated. The licensees and persons in their own turn also must not claim to possess rights which amount to instruments of exploitation of the community.
There is no doubt that powers A above will facilitate development of electricity industry. Hydro-metric surveys etc. will show the possibilities of water-power in the State. Investigation and experimentation in methods of generation, transmission and distribution, so also manufacture and popularising of instruments used in generation etc. and of electrical appliances are calculated to advance the industry. The information which the Board receives can be utilised by it for formulating a proper policy and control the individual units in such respects.

For planned development of the industry it is essential that the Board should control the establishment or extension of generating stations, and start its own stations. For efficient and economic conduct of the industry the Board must have powers of inter-connections of stations and station systems. For the same purpose it must have the right of closing down stations, control of stations and of transmission lines. The provision that the Board may give loans for extension of plant is a positive help. Board's sale to and purchase of electricity from licensees and persons both help coordinated and economic conduct of the industry, and protect the interests of those to whom sale is effected and those from whom purchase is made. The Board's control of lease will prevent concentration of the control of the industry
in a few hands. The board will give directions to the licensees mainly for efficient running of their undertakings. Board's control of licensees' charges aims at protection of consumers. It is to be seen later whether the principles of control are fair to licensees and investors. We do not see a valid reason for not treating the local authorities that supply electricity in the same manner as other licensees in fixing their charges.

In giving directives to local authorities, under the Amendment of 1956, prior approval of the State Government has to be obtained. This suggests that the only reason for distinguishing local authorities from other licensees is political, viz., they form a part of the Government and cannot be submitted to the control of a non-government authority.

The licensees and persons generating electricity are not deprived of their say or certain legitimate rights. When the Board takes measures for development of water-power, the licensee whose source of water power is affected by these are to be given notice of the measures and an opportunity to be heard. In respect of the controlled stations, closing of stations, purchase of stations and transmission lines, and supply by the Board to the licensees having generating stations, the Board may make arrangements with licensees (under section 47 and regulations in that behalf under Section 79) and the
licences can press their legitimate claims. In doing this they will not be deterred by their licences etc. (Section 49). If the generating station belongs to a person other than a licensee, his station will not be designated as a controlled station, and if a transmission line belongs to a person other than a licensee it will not be used or acquired without the prior consent of the owner. The main transmission line of a licensee will not be acquired without the prior consent of the licensee (Section 37). The Board will not supply in the area in which a sanctioned Scheme is in force electricity to a distributing licensee without the consent of the bulk-licensee, unless the licensee to be supplied has an absolute right of veto on any right of the bulk-licensee to supply electricity for such purpose, or unless the bulk-licensee is unable or unwilling to supply electricity for such purpose on reasonable terms and conditions and within a reasonable time (Section 19). The Board will not supply electricity to a person within the area of supply of a licensee without the consent of the licensee, unless the actual effective capacity of the licensee's generating station at the time when supply was required was less than twice the maximum demand asked for by any such person, or the maximum demand of the licensee, being a distributing licensee is, at the time of the request, less than twice the maximum demand asked for by
any person, or the licensee is unable or unwilling to supply electricity for such purpose on reasonable terms and conditions and within a reasonable time (Section 19). The circumstances under which the licensee's refusal to give consent may be set aside are quite just and fair.

In regard to consent of the Board to establish or acquire a new generating station or to extend or replace any major unit of plant or works pertaining to the generation of electricity, it will not be withheld except for reasons (Section 44) which are reasonable. The only ground on which the licensee may complain is that the Board may withhold consent, giving an undertaking that it itself would make him a supply sufficient for his requirement. This the Board is not likely to do unless such a supply is included in the Schemes of the Board. Schemes are not made to meet ad hoc exigencies. If, however, Schemes which are already made include the supply to a licensee, they are made not to penalise the licensee but because they are called for on sound considerations. Lastly, even in an area in which the Board is to establish a generating station as per a sanctioned Scheme it may make arrangements with a licensee or a person for the establishment of the station. The possibility of a licensee or a person being allowed to start a generating station in this area is not ruled out. Even when the Board establishes or acquires a generating station, it may make arrangement with a licensee or any other person for its operation.
Any commentary on the powers and duties of the Board is inadequate without a reference to its control of the rates and finances of the licensees. We will deal with them separately because of their importance.

Rate Control

(A) Licensees' Rates

Control of rates charged by a public utility is an essential function of the regulatory authority. Prior to the 1950 Act, the licensees were free to vary their charges between the minimum and the maximum stated in the licence. Under this Act the rates are governed by the Sixth Schedule of the Act (Section 57). Any provision in the licence inconsistent with the Sixth Schedule is void according to 'Jindes Oil Mills v. Godhra Electricity Co.' (1963). This Schedule is explained and discussed in Section III of this Chapter.

The Board, or where no Board is constituted under (Section 57A) this Act, the State Government, may appoint a Rating Committee if it is satisfied that the licensee has failed to comply with any of the provisions of the Sixth Schedule. The Rating Committee must be appointed when so requested by the licensee. The Rating Committee is to report to the State Government and the latter is to publish the report in the official gazette with an order fixing licensee's charges for a period not exceeding three years. The licensee can charge less but not more than these.
The composition of the Rating Committee leaves little to be desired. If it is appointed by the Board, it includes a judicial member not below the rank of a District Judge, a member of the Board having experience of accounting and financial matters and a representative of the association of licensees. If the Rating Committee is appointed by the Government, it consists of five members as these: one judicial officer as above, one Chartered Accountant of not less than ten years' experience and one member having administrative experience, all these three being appointed by the Government; one member nominated by the licensees; and one member nominated by the association referred to above.

(B) Board's Rates

There are two specific Sections (46 and 49) in the Act about the Board's tariffs.

A tariff to be known as Grid Tariff will be fixed from time to time by the Board in accordance to regulations made in this behalf for its Scheme area. For all Scheme areas there may be one tariff or there may be different tariffs for different areas. These tariffs are applicable to controlled stations, licensees to which the Board supplies power (under Section 35), licensees whose stations are closed down and other licensees.

(1) Tariffs so fixed may also be uniform. In fixing the uniform tariffs the Board shall have regard to all or any of the following factors.
(a) the nature of supply and the purposes for which it is required;
(b) the co-ordinated development of supply and distribution of electricity within the State in the most efficient and economical manner, with particular reference to such development in areas not for the time being served or adequately served by the licensee;
(c) the simplification and standardisation of methods and rates of charge for such supplies;
(d) the extension and cheapening of supplies of electricity to sparsely developed areas.

(2) If the Board considers it necessary to fix different tariffs for any person other than a licensee it can do so having regard to the geographical position of any area, the nature of supply, the purpose for which supply is required or any other relevant factors.

(3) In fixing the tariffs and terms and conditions for the supply, the Board shall not show undue preference to any person.

From these provisions it can be seen that the Board, as compared to the licensee, has a great latitude in fixing its charges. This latitude is greater in supply to licensees than in supply to persons who are not licensees. Such latitude is necessary if the social objectives of electricity supply are to be served; however, it may also be used in enhancing charges to consumers. Though it was
stressed in 'Kanganunda Industrial Works V, Andhra Pradesh State Electricity Board' (1968) that the Board is not given arbitrary powers to fix tariffs and has to work on certain guiding principles, there is no doubt about the latitude and the possibility of abuse of the powers against general consumers. The element of arbitrariness is reduced by the guiding principles stated above and also by the principles to be laid down by the Board under its regulations to be made under Section 79. But these regulations, unlike certain other regulations, do not have to be made with the approval of the State Government. Only the regulations regarding the principles of Grid Tariff have to be made with the concurrence of the CEA.

III

The Sixth Schedule of the Electricity Supply Act

In respect of the regulation of the conduct of the licensees the most important part of the ES Act is the Sixth Schedule. As mentioned above, the licensees' rates are regulated by this Schedule. It also regulates Reasonable Return to the licensees, reserves and a few elements of cost. The Schedule is a complicated piece and needs elaboration.

Rates and Return

1. The licensee shall so adjust his charges for the sale of electricity that his Clear Profit in any year shall not, as far as possible, exceed the amount of Reasonable Return.
2. The licensee will be excused for having not adjusted the charges downward in any one year if his Clear Profit has exceeded Reasonable Return by not more than 20% of the latter.

3. The above provision does not prevent the licensee from levying a minimum charge with the previous approval of the Government.

4. Charges can be changed only once in the year.

5. If Clear Profits exceed Reasonable Return, one-third of the excess but not exceeding 5% of the Reasonable Return will be at the disposal of the undertaking. Half of the balance shall be carried to the Tariff and Dividends Control Reserve and the other half shall be distributed among the consumers in the future.

I. Clear Profit

Clear Profit is defined as difference between income and the sum of expenditure and specific appropriations together on the other hand, each being derived as under.

Income is derived from gross receipts from sale of energy exclusive of discount, from rent of meters and apparatus hired to consumers, from sale of lamps and apparatus, from interest on investments and bank balances.

Expenditure is that which is properly incurred on generation/purchase of energy, on distribution and sale
of energy, on rent, rates and taxes, on interest on
loans from the Board and Government approved institutions,
on interest from debentures and security deposits, on legal
charges, on bad debts, on auditors' fees, on management
including Managing Agent's remuneration, on depreciation,
on contribution to provident fund, pensions and gratuity
and on payment of bonus. Bad debts also are included.

Specific appropriations are those sufficient to
cover previous losses, taxes on income and profits, written
down amount in respect of intangible assets, contribution
to Contingency Reserve, contribution to arrears of depre-
ciation, contribution to Development Reserve, and others
as approved as appropriation by the Government.

II. Reasonable Return
Reasonable Return consists of the following:
(a) Amount found by applying Standard Rate to Capital
Base at the end of the year;
(b) income from investments other than those included
in Capital Base;
(c) an amount equal to $ of one percent on loans from
the Board/Government-approved organisations;
(d) an amount equal to $ of one percent on capital
raised from issue of debentures;
(e) an amount equal to $ of one percent on accumula-
tions in the Development Reserve; and
(f) an amount allowed by the Central Government in
view of prevailing tax structure.
Provisions (d) to (f) were added by the Amendment of 1966 and 1966.

III. Standard Rate

(1) Standard Rate = 7% on that part of Capital Base which is equivalent to that on 31st March 1965.

(2) Standard Rate = on the remaining part of Capital Base; Reserve Bank rate at the beginning of the year plus two per cent.

These provisions are substituted for the provision of 5% in the original Act. Five per cent was criticised by the licensees as too low. It was only 1½ % higher than the Bank Rate at the time of the Amendment in 1966, though it was 2½% higher than at the time the principal Act was passed. The Amendment of 1966 introduced the arrangement of 2% percent being added to the Bank Rate. This automatic change as related to Bank Rate should have been there from the very beginning. This arrangement has one defect, viz., as the Bank Rate rises the licensees get undue benefit in respect of investment which was made when the interest rates were low. This defect was partly rectified by the Amendment of 1966 which distinguished between investments prior to the end of March 1965 and investments that followed.

IV. Capital Base

Capital Base consists of $a + b + c + d + e - (f + g + h + i + j + k + l)$, where these letters measure the following.
(a) Original costs of fixed assets in use and for purposes of the undertaking, less contributions made by consumers towards construction of service lines and also less written-off cost of assets which are obsolete, inadequate or superfluous.

(b) Costs of intangible assets.

(c) Costs of works in progress.

(d) Amount of investment in authorised securities made from Contingency Reserve and from depreciation account, and

(e) an amount on account of Working Capital equal to the following.

(i) 1/12th of the book cost of stores and materials,

(ii) 1/12th of bank balances (credit or debit) and call and short term deposits, not exceeding 4th of Operating Expenditure excluding some items, e.g. expenses of generation/purchase of energy, interest on loans from Government-approved organisations and the Board, interest on debentures and depreciation,

(iii) security deposits received from consumers,

(iv) credit balance of Tariffs and Dividend Control Reserve and Development Reserve,

(v) amount from Clear Profit appropriated for distribution to consumers,

(f) the amounts written off or set aside on account of depreciation of fixed assets and amount written off in respect of intangible assets.
(g) loans from the Board/Government-approved organisations and
(h) the amount of debentures.
(i) security deposits from consumers.
(j) amount in the Tariffs and Dividends Control Reserve at the beginning of the year.
(k) amount in the Development Reserve at the close of the year, and
(l) amount carried forward at the beginning of the year for distribution to consumers from the excess of Clear Profit over Reasonable Return.

It may be noted that the Capital Base is narrowed by the deductions from (g) to (l) under the Amendments of 1956 and 1966 as compared to that in the original Act. These are legitimate deductions from the Capital Base because expenses on these accounts are admitted for calculating Clear Profit. This must have escaped the attention of the framers of the original Act.

Original cost of assets includes the cost of delivery, erecting and bringing the assets in beneficial use. It also includes interest charges on capital expenditure incurred since the date of the grant of licence and the date of commencement of supply out of borrowed money. The interest chargeable is, however, not that exceeding the average Reserve Bank rate during that period plus one per centum only.
Intangible assets mean underwriters' commission and preliminary and promotional expenditure. It, however, excludes amount paid on account of good-will. This is affirmed by Government of Bombay and Suburban Electric Supply Co. Award of October 1966. Our remarks about good-will given above under (g) of Part I of this Chapter may be consulted.

V. Reserves

1. Tariff and Dividend Control Reserve shall be available for appropriation only to the extent by which Clear Profit is less than Reasonable Return in any year.

2. Contingency Reserve will be formed by carrying every year a sum between one-fourth and one-half of one percent of the original cost of fixed assets, the maximum of the Reserve being 6 percent of the said cost. Amount realised by sale of assets which are obsolete, inadequate or superfluous shall be credited to Contingency Reserve.

3. Sums in Contingency Reserve shall be invested in authorised securities.

Contingency Reserve will be available for appropriation only with the approval of the Government, to meet contingencies like loss of profits due to accidents and strikes, and expenses on maintenance and renewal of plant which are not normal expenditure and for payment of compensation under any law. It can under the judgement in 'U.P. Electricity Supply Co. v. R.K. Shukla' (1970) be used for paying compensation to retrenched employees.
Also written down cost of fixed assets will be charged against Contingency Reserve.

3. Development Reserve shall be created by carrying to it every year a sum calculated at the rates of income tax and super-tax on the amount of development rebate to which the licensee is entitled in the year.

VI. Depreciation

1. The licensee shall be allowed to set aside in each year, for depreciation of fixed assets, an amount in such a manner that the accumulated amount over the prescribed period together with compound interest of 4 percent will equal 90 percent of the book value of the assets. The licensee has the option of adopting within three months from the date these principles being enacted, the straight line method of depreciation accounting.

For the purposes of depreciation even the cost of service lines constructed out of contributions from consumers shall be considered.

All sums credited to depreciation amount shall be invested only in the business of electricity supply of the undertaking or, if this is not possible, as approved by the Government.

Depreciation will not be charged in respect of fixed assets described as obsolete, inadequate or superfluous.

Except with the previous consent of the Government no sums shall be carried to a reserve and no dividend
exceeding 3 per cent shall be paid on share capital and no other profit will be distributed to the shareholders in any year unless normal depreciation and equated installment of arrears of depreciation have been written off.

Arrears of depreciation may be written off by equated payments over the remainder of the prescribed period, the amount being treated as special appropriation for the purpose of calculating Clear Profit.

Age of assets for calculating depreciation is given in Seventh Schedule.

VII. Managing Agent

1. Managing Agent's ordinary remuneration and purchasing commissions, if any, shall be based on Net Profit (as under Section 349 of the Indian Companies Act of 1956) as under.

   (a) 10% in respect of first Rs 5 lakhs of Net Profit
   (b) 7% in respect of excess over Rs 5 lakhs.

2. Managing Agent's ordinary remuneration shall be subject to a minimum of two rupees per annum per thousand rupees of paid-up and debenture capital, the base being equated to Rs 5 lakhs if it is actually less than Rs 5 lakhs and being considered as Rs 1 crore if it is actually more than Rs 1 crore. Thus the annual minimum remuneration of Managing Agent will vary between Rs 1000 and Rs 10,000.

3. Office allowance of Managing Agent which shall include salaries and wages of persons employed in his office shall be based on percentages of (1) Operating
Expenditure and (2) capital expenditure. It will not exceed:

(1) 5% in respect of first Rs 1 lakh of Operating Expenditure,
6% in respect of next Rs 2 lakhs,
9% in respect of next Rs 7 lakhs, and
14% in respect of excess over first Rs 10 lakhs,

plus (2) 4% in respect of first Rs 1 lakh of capital expenditure,
3% in respect of next Rs 2 lakhs,
1% in respect of Rs 7 lakhs, and
1% in respect of excess over first Rs 10 lakhs.

In the Indian Companies Act the provisions were as under:

1. Total managerial remuneration to directors, managing agents, secretaries, treasurers and managers not to exceed 11% of Net Profit.
2. Payment to managing agent not to exceed 10% of Net Profit.
3. Managing Agent not to be paid any office allowance.

As compared to these provisions those in the ES Act were restrictive for large companies though they were more favourable to small licensees.

Now that the Managing Agency system is abolished since April 1970 we need not go further into this subject.

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10. Sections 198, 348 and 364 respectively of the Indian Companies Act.
The object of the ES Act as stated officially, contains no reference to regulation of the private sector of the industry. There is a reference to rationalization which, as was shown above, may be interpreted to include regulation. That regulation was one of the main objects is clear from the text of the Act taken with the Schedules and the history of this Act. In the IE Act of 1910 there were provisions like the fixation of maxima of rates and the revocation of licenses in cases of serious defaults. However, there was no continuous and sustained regulation with uniform principles. This lacuna was felt particularly in respect of finances of the licensees. Therefore, with a view to placing the finances of public electricity supply companies on a standard and firm basis the Electrical Commissioner to the Government of India outlined, in 1944, some principles. These were examined by an Advisory Board appointed by the Central Government on 15th November 1946. The recommendations of this Advisory Board form the base of the Sixth Schedule of the ES Act. Therefore explanation of the provisions of the Schedule may be found in the report of the Advisory Board.

The Advisory Board mentioned the following objects of its recommendations.

(a) To safeguard the interest of the consumer by limiting interest and dividends payable to the

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11. Only a typed copy of this Report was available to the present writer from the Federation of Electricity Undertakings of India, Bombay.
minimum necessary to ensure an adequate flow of development capital, and so effect a reduction in the selling price of electricity.

(b) To safeguard the interests of investors (and, in the long run of the consumers as well) by insistence on a properly devised system of compulsory depreciation and at the same time permit the earning of a "reasonable" or "fair" return on investment.

(c) To regulate the commission and expenses of Managing Agents within reasonable limits, having regard to the special circumstances of the industry.

The Advisory Board compared the Capital Base with the Rate Base in the U.S.A. The latter excluded some items because the system of accounting that was employed in the U.S.A. made that elimination possible. "It is admittedly desirable to effect all of the .... exclusion, but in practice it would mean an investigation into the accounts of every undertaking since its inception.... and this would be impracticable as being too formidable a task". On the admission of the Advisory Board, the Capital Base as defined in the Indian counterpart "will permit various undertakings who have indulged in the past in the capitalisation of revenue partly at the consumers' expense,

to retain the assets thus acquired in the Capital Base." ¹³
Once, however, the legislation comes into force capital-
isation from this source ceases to operate. Even in
the past only some companies which were making electrical
supply in big centres must have made huge profits by
setting the rates high and carried a large portion to
capital formation by not providing adequately for depre-
ciation and dividend payment. "As the time goes on the
tendency will be for the Capital Base to approximate
more and more to the paid-up ordinary share capital, any
excess in the long-run being represented by the effects
of efficient management." ¹⁴ The importance of the con-
trol of Reasonable Return by relating it to Capital
Base may be appreciated by the fact that 21 percent
licensees out of the sample of 148 ones taken by the
Advisory Board, which were responsible for 77 percent
of the capital employed, distributed dividends exceeding
7 per cent in the year 1945-46. The principles of
Capital Base and Reasonable Return result into reduction
of charges for the consumer. The Advisory Board does
not deny that "cases will arise, where an attempt will
be made to effect an artificial inflation of the Capital
Base. Other irregularities of internal accounting might
also be attempted with a view to avoiding the full effect
of certain provisions." The State Governments, however,

¹³ Ibid, paragraph 21.
¹⁴ Ibid, paragraph 36.
have adequate powers of supervision of the accounts of the licensees.

The Standard Rate as recommended by the Advisory Body was based on the “redemption yield of the longest dated terminable Central Government loans,” and it was different for different slabs in the Capital Base as under.

(a) 5.3% on that portion of Capital Base which is in excess of Rs 50 lakhs,
(b) 5.8% on that portion of Capital Base between Rs 10 lakhs and Rs 50 lakhs, and
(c) 6.3% on the first Rs 10 lakhs of Capital Base.

The redemption yield of Government loan was 2.8% and the Standard Rate was calculated on a sliding scale adding to it an increasing allowance with the diminishing base. In the view of the Advisory Board, the Reasonable Return based on these standard rates would not affect the flow of capital into this industry. Under the principles laid down by the Advisory Board (e.g. the provision of depreciation) financial standing of the industry would be strengthened and money would be available at cheaper rates. In his minute of dissent, however, the representative of the licensees, Mr. J.A. Macpherson suggested a rise of 2% above these rates.

Actually in the ES Act as it was passed in 1948, the differentiation in the size of Capital Base was not

15. Ibid, paragraph 25.
adopted. A uniform Standard Rate was taken and it was fixed at 8%. As the Advisory Board had pointed out, a uniform rate was inequitable. The smaller the licensee, more difficult it is for him to obtain capital and the higher is the Standard Rate that it deserves. It may further be noted that the Amendments to this Act related the Standard Rate to the Bank Rate to the Government security rate.

In respect of Managing Agent’s commission the Advisory Board suggested the maxima less than those stipulated under the Indian Companies Act then. The rates of commission would also be applied to Clear Profit and not to Net Profit as required under the Companies Act. These recommendations were made on the ground that electricity supply company was a monopoly industry and that it was desirable to reduce cost of electricity. On the other hand, the Advisory Board proposed additional payment to the Managing Agents as office allowance. As the Clear Profit of the electricity undertakings in the initial period would be small and inadequate the Advisory Board provided for certain minima too. The ES Act incorporated the recommendations of the Advisory Board except that the base of Clear Profit was substituted by that of Net Profit. Now that the Managing Agency system has been abolished the interest in the provisions regarding this system is merely academic.

16. Ibid, paragraph 27.
Michael Kidron made a remark that "Electricity generation and distribution strictly controlled under terms of the Electricity Supply Act 1948, regained considerable freedom with the Electricity (Supply) Amendment Act of 1956". This remark cannot be borne out on examining the Amendment. Relaxation of control is not in evidence. There is a new provision that a Rating Committee will not be appointed unless a show cause notice is sent to the licensee and if there is a dispute about interpretation of the Sixth Schedule. This is not a concession but an equitable provision. It is true that under the Amendment, the licensee won some benefits, at least two. Firstly, the Reasonable Return is stopped up. Secondly, a Development Reserve has been allowed to be instituted.

The Amendment, on the other hand, has tightened up conditions in a number of ways. Firstly, while requiring the licensee to conform to Reasonable Return he would be allowed a deviation from Clear Profit by only 20% in place of the provision of 30% in the original Act. Secondly, of the excess of Clear Profit only 5%, not 7½% as in the principal Act, can be at the disposal of the undertaking. Thirdly, payment of dividend in excess of 3% and distribution of other profits cannot be done without Government's permission so long as any arrears of depreciation or previous losses remain to be written off.

The accounts of the licensees are subject to very close scrutiny and the expenses are seen to be proper or otherwise. Under the definition of Clear Profit what is allowed is "expenditure properly incurred" in place of expenditure incurred in the principal Act. The Government of Maharashtra has a special auditor for this scrutiny. He sends his remarks to the Government and the Electricity Board.

The main demands of the electricity undertakings were that the Standard Rate should be raised and a provision for Deferred Tax payment should be made. The case of Deferred Tax payment arose out the difference of provisions regarding depreciation between the ES Act and the Income Tax Act. The latter allows accelerated depreciation in the early life of the assets "so that funds would be provided for accelerated industrial development in the country's expansion plans", whereas the depreciation rates under the ES Act are lower. Under the Income Tax Act depreciation can be provided down to a fraction of the written-down value of assets while under the ES Act it can be provided down to 10% of the written-down value. Of these two points of difference the first has been attached great importance.\textsuperscript{18} The importance attached to

these provisions arises because the licence of the electrical undertaking expires or is terminated, and the licensee has to receive a value of assets from the Electricity Board. This value will depend on the written down value. The written down value under the ES Act is higher than that under the Income Tax Act. The excess will be liable for tax. Thus, it is alleged, this is a case of deferred tax, for which there is no provision under the ES Act. Such a provision is not so far made.

Our comments are these: (1) If the price of assets that is paid is high (due to whatever reasons, e.g. high written down value), it legitimately attracts tax. (2) That depreciation is charged to consumers need not mean that a tax arising out of the gains from methods of depreciation charges be also charged to the consumers.

Lastly, we turn to assess the provision of Reasonable Return, the provision which affects the profitability of this industry and the availability of finance to this industry. From the point of view of the industry, it is the most important measure of regulation. It must be said that the provision of admissibility of expenditure and profits has been liberalised under the two Amendments. This is done in three ways. Standard Rate to be applied to Capital Base has been stepped up; Clear Profit which must not exceed Reasonable Return is calculated after making allowance for expenditure on a broader base. This expenditure includes interest on
debentures and on loans from nationalised banks. Reasonable return itself is escalated by additions of certain charges mentioned above in the section on this subject. It should also be emphasized that from the very beginning specific appropriations have been allowed to be bracketed with expenses for deduction and they include taxes on income and on profits along with other items. Thus the appropriations precede profit calculation and not follow as is usual. Some profit is thus, in effect, concealed from our eyes in the specific appropriations.

On the other hand, there was some erosion of this benefit. Mr. Haushir Bharucha, an authority on electricity law, pointed out that from the Finance Act of 1959, the advantage of "grossing up" i.e. freeing the dividend receiver from tax on the company's profit has been abolished. This takes away the advantage from tax on income and on profit being considered admissible expenditure under the ES Act. 19

Then the question is whether rate of return that was admissible was fair to the industry. The U.S. Supreme Court gave a verdict in the Bluefield Case of 1921 that "the return should be reasonably sufficient to assure confidence in the financial soundness of the utility,

and should be adequate under efficient and economical management, to maintain and support it to raise the necessary money for proper discharge of its public duties

If the investor is to be assured of the soundness of the industry, he has to be assured on two counts: capital appreciation and income of his share. The Commerce 190 pointed out that because of the regulated nature of the industry there was little prospect of capital appreciation and income was the primary consideration. There were two extreme views about the fair income to the investor.

At the one end the 'Free Press Journal' (a daily paper which was reputed for its nationalist past) said that electricity consumption in India was lowest in the world, and to encourage it a return of 1½% above Bank Rate in the industry should be regarded as adequate. 21 On the other hand, spokesmen of the industry clamoured 22 before 1966 for a return of 1%. When by the Amendments the Standard Rate was raised by 2½% above the Bank Rate, there was demand from the industry for the abolition of the distinction between the part of Capital Base before 31st March 1965 and the part thereafter. 23 The distinction was made

21. This is quoted from memory by the Author.
by the authors of the provision to keep down/Reasonable Return in an era of rising Bank Rate in the interest of consumers. Actually from 1948, the Bank Rate has moved as under.

Bank Rate & Standard Rate

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<th>Date</th>
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<th>Standard Rate</th>
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<td>5%</td>
</tr>
<tr>
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<td>February 1965</td>
<td>6%</td>
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</tr>
<tr>
<td>April 1966</td>
<td>6%</td>
<td>* (7%) 8%</td>
</tr>
<tr>
<td>March 1968</td>
<td>5%</td>
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<tr>
<td>January 1971</td>
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<td>July 1974</td>
<td>3%</td>
<td>(7%) 11%</td>
</tr>
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</table>

Table 2.1 *Note: The two rates are given for the two parts of the Capital Base as before and after 31-3-1966.

Thus before 1966 Amendment the Standard Rate must have been hard on the industry but subsequently it was satisfactory.

In price fixation a certain fair return has to be assumed, though it is not guaranteed in all cases. In
Respect of other industries where price fixation has been adopted the Tariff Commission and ad hoc committees have from time to time recommended the fair return and the final price. In most cases the fair return was recommended to be 12% on the basis of net block plus Working Capital, 24 Returns included provision for bonus, interest on borrowed capital and debentures, Managing Agent's remuneration, taxes and dividend. Recently, the Supreme Court has passed a judgement on the prices of motor cars in 'Premier Automobiles V. Union of India' case. In this it has taken 16% return on capital employed as reasonable. 25 This would according to the Supreme Court leave 10% dividend to equity share holders. Compared with these standards, provisions for the electricity supply industry leave much to be desired. It may be said in defence of lower rates, return and dividend in this industry that this is a public utility industry par excellence and therefore, it cannot be on par with others in respect of return etc. On the other hand, the principle of optimum resource allocation would not uphold this distinction.

This discussion of Reasonable Return and particularly of Standard Rate is made with reference to equity

capital. The industry can take loans from the Government-approved institutions and security deposits and issue debentures. Interest on these has been admissible expenditure. In the original ES Act only interest on loans from the Boards and on security deposits was admissible. It was a debatable question whether interest on debentures and on loans from Government-approved institutions (like the LIC) could be admissible. There were two opposite opinions on this. One opinion was that interest on debentures etc. was covered under the provision "other expenses admissible under the law for the time being in force in the assessment of Indian Income-tax and arising from and ancillary or incidental to the business of electricity supply." The Amendment of 1965 confirmed this view by specifying as admissible interest on debentures and on loans from Government-approved institutions. With this Amendment and increase in the number of financial strength of these institutions (including the nationalised banks) the industry may be expected to depend on loans increasingly. Stringency of Standard Rate and Reasonable Return has, therefore, been relieved.

In conclusion, it may be said that under the IE Act of 1910 and ES Act of 1948 the control of the electricity supply industry is fairly close. To the extent that, because of the control and further acquisition or
nationalisation possibility, expansion of the industry is likely to be hampered, the Electricity Board may be ready to expand. In fact, the private enterprises, except the giants like Tata, play a very minor and subordinate role. They are mainly distributors and are also weak. In the ES Act the stress is more on planning and expansion of the industry, and on the organisation of the public sector than on regulation of private sector. In a few years' time regulation in the latter sense may be little to be done, the giant enterprises, though subordinate in law, being treated as coordinate suppliers. About the impact of regulation on rates and finance we will have more to say in Chapters 8 and 9 on these subjects.