

Legal Aspects of Power Projects in India

Preface:

Energy is one of the essentials to our life and the quantity of energy consumed per capita can be used as an indicator of a country's development level. The growth of population is one of the major force driving towards the increase in energy demand globally and India, being the second most populous country in the world, the demand for energy has increased in manifold.

It is been estimated that by 2022, India would require 327 GW of power generation capacity. In India, power projects present a promising business opportunity which has not been tapped with full potential in India.

With the liberalization of market, private players have also marked their presence alone or in conjunction with the Government. The general framework governing the implementation of power projects by private participation depends upon:

- (a) The segment of the power sector that the project intends to develop;
- (b) The main fuel for the power project, if the project involves the establishment of a generating station;
- (c) The nature of the power project; and
- (d) The classification of the developer.

Nature of Private Participation:

Power projects by private developers can relate to either:

- (a) The generation segment; or
- (b) The transmission segment; or
- (c) The distribution and supply segment.

Within each of these segments, the scale of the project can be:

- (a) That of captive project for a specific identified group of consumers; or
- (b) An interstate project, within a specific state, or
- (c) An interstate, for the benefit or more than one state.

Applicable Laws and Governing Bodies:

This sector has highly developed legal framework for regulating private participation.

Applicable Laws:

The Electricity Act, 2003 is the Central Law governing the electricity sector. Electricity Act, 2003 gives a framework for restructuring of the state Electricity Boards.

Governing Bodies:

Under Electricity Act, 2003 following are the authorities:

Regulatory authorities:

- i) Central Electricity Regulatory Commission
- ii) State Electricity Regulatory Commission
- iii) Joint Commission
- iv) Appellate Tribunal

Monitoring agencies:

- i) Investigating Authority
- ii) Assessing Officer
- iii) Adjudicating Officer
- iv) Chief Electricity Inspector
- v) Electricity Inspector

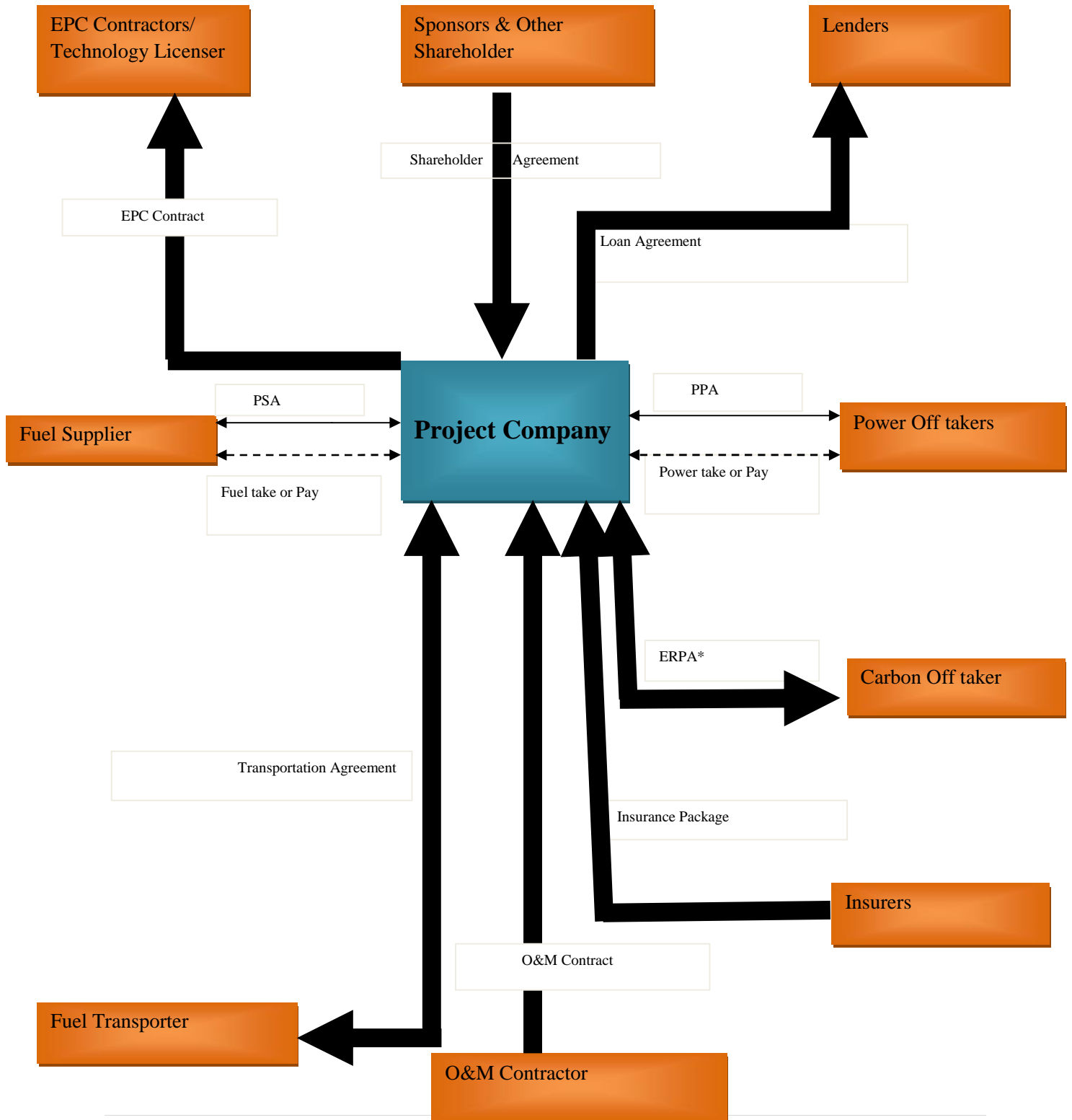
Advisory bodies:

- i) Central Advisory Committee
- ii) Selection Committee
- iii) State Advisory Committee
- iv) Coordination Forums

Operational authorities:

- i) Central Electricity Authority
- ii) National Load Dispatch Centre
- iii) Regional Load Dispatch Centre
- iv) State Load Dispatch Centre
- v) Central Transmission Utility
- vi) State Transmission Utility

Contractual Structure of a Power Project:



The diagram above illustrates the basic contractual structure of a simple project financed, which vary from project to project. However, most projects will have the basic structure illustrated above.

- (1) A Project Company which will construct and own the process plant facility and will be responsible for the relationship with Government, customers, contractors and suppliers.
- (2) Many developers of Project Company select to finance from their balance sheet but in many cases they seek finance from lenders. In these cases, Engineering, Procurement and Construction (EPC) Contractor is required to be a large, experienced participant in the industry on which lenders have confidence on the success of the project. In these cases the EPC Contractor should be one who can successfully deliver the project and is large enough to cope with losses if it does not.
- (3) There are a number of contractual approaches that can be taken to construct a process plant facility, and EPC Contract is one among them. The other option is to have a supply contract, a design agreement and construction contract with or without a project management agreement. The major advantage of the EPC Contract over the other possible approaches is that it provides for a single point of responsibility, a fixed contract price with fixed completion date.
- (4) Operating and Maintenance (O&M) Agreement with an operator for the operation and maintenance of the facility. The term of the O&M Agreement varies from project to project.
- (5) A Supply Agreement governing the supply of feedstock/fuel supply to the process plant. On most projects for the supply of feedstock/fuel supply, construction of infrastructure is done by a separate contractor to design and construct this infrastructure.
- (6) Off take agreements govern the sale of the output of the project. For process plant projects these agreements are crucial to the developing proceedings. Lenders will not lend the funds and boards will not approve the project if there are no customers locked in to take the product. The impact of the off take agreement is on practical completion. If there are take or pay agreements it is vital that the project is ready to deliver product from the inception date of the off take agreements. It may even have to buy product on

the open market to meet its obligations which can be a costly exercise if those markets are thinly traded or demand for these products is high.

- (7) Financing and security agreements with lenders and shareholder agreement to finance the development of the project.

Financing Trends for Power Projects:

Sl. No.	Existing Approach	Evolving Trends
1.	Conventional lending through Debt and Promoter's Equity	Financing from investors with varying risk profile: i) Subordinated debt. ii) PE Funds iii) Insurance Companies
2.	Debt: Primarily through Rupee Term Loans (RTL)	Increasing inflows through: i) External Commercial Borrowings. ii) External Credit Agencies iii) Multi-lateral Agencies
3.	Limited Exit Options for Lenders.	Being Addressed through 'Buy-out' clauses in Concession Agreement in sectors like Road, Power, etc.
4.	Inappropriate risk mitigation mechanism.	Innovative Project structuring through Financial Engineering to mitigate risks.

Concluding Remarks:

The Government has gone for a massive increase in power capacity through projects, which are open for both the private sector and foreign investors. However, controversies surrounding the contract awarding procedures, bureaucratic delays, counter guarantee problems and problems in signing fuel supply agreements have resulted in significant delays in most of these.

The government is sparing no effort to garner the requisite funds for the cause. For any country to develop, power plays a key role in the industrial growth. The future of the power sector thus depends on the Government's policies but there is no mistake in the immense potential of this sector.

Disclaimer

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