

**CAVEAT**

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**BACKGROUND**

Pursuant to the Composite Scheme of Arrangement including Amalgamation of Torrent Power AEC Limited (TPAL), Torrent Power SEC Limited (TPSL) and Torrent Power Generation Limited (TPGL) (transferor companies) with the Company and the reorganisation of capital of the Company (the Scheme), the undertakings of the transferor companies as going concerns are transferred to and vested in the Company with effect from the Appointed Date, i.e., 1st April, 2005. This is the maiden report of the Company representing the collective operations of the power business of Torrent Group. Prior to the amalgamation, the transferor Companies had their independent operation with the erstwhile TPAL being engaged in generation and distribution of power, TPSL in distribution of power and TPGL in implementation of 1100 MW SUGEN CCPP. Simultaneously, the Company had extended the Financial Year (FY) 2005-06 to end on 30th September 2006 after obtaining necessary approvals in this regard.

The data presented hereinafter for FY 2004-05, wherever required for comparison, is the aggregate of the data of the transferor companies. In order to bring parity, the data for FY 2005-06 (18-months) has been annualised, wherever appropriate, for the purpose of comparison with FY 2004-05 (12-months). However, the annualised data of FY 2005-06 is not exactly comparable because of the seasonal impact on parameters like Sales, Plant Load Factor, Purchase of Power, T&D Loss, etc.

## OVERVIEW

### Sector:

Based on the current trends it is estimated that the Indian economy will grow at around 8%. There is no disputing the premise that robust infrastructure is a prerequisite for sustaining and enhancing GDP growth. Of the various elements of infrastructure, power would appear to be the most critical and any shortcoming in the sector would have an almost immediate impact on the output and hence, GDP. Although there has been quantum increase in investment in the Indian power sector, there is still an overall peak shortage of about 12 per cent in the country. The following table presents the power supply scenario during 2005-06:

	Peak Demand	Peak Met	Peak Deficit/ Surplus	Peak Deficit/ Surplus	Energy Requirement	Energy Availability	Energy Deficit/ Surplus	Energy Deficit/ Surplus
	MW	MW	MW	%	MU	MU	MU	%
Gujarat	9783	7610	-2173	-22.2	57137	52436	-4701	-8.2
India	93255	81792	-11463	-12.3	631757	578819	-52938	-8.4

Viewed against this backdrop, the state of Gujarat and Indian power sector generally, provides investment opportunities on all the aspects like adding generation capacity, strengthening transmission, reforming and intensifying distribution etc., for the private sector.

### Company:

Torrent Power Limited (TPL) is an integrated power company engaged in the generation and distribution of electricity in the cities of Ahmedabad, Gandhinagar and Surat in the state of Gujarat. TPL has a distribution area admeasuring 408 sq. kms. The Company serves about 1.85 million consumers in these cities. The operational generating capacity of the Company is 500 MW, comprising 400 MW coal based thermal power plant at Sabarmati and 100 MW dual fuel gas based combined cycle power plant at Vatva, Ahmedabad. The Company is also implementing a 1100 MW SUGEN gas based combined cycle mega power plant at village Akhakhhol near Surat. The first block of 367 MW of the project is scheduled to go on stream in the third quarter of year 2007.

### Performance:

The overall performance of the Company during the financial period 2005-06 has been good. The Company generated 5943 MUs of electricity while the purchase of power stood at 5711 MUs. The units of electricity billed to consumers were at

10037 MUs excluding an export of 73 MUs of power, showing an increase of 12.82% on annualised basis. The peak system demand in the areas of supply was 1333 MW, showing an increase of 13.93%. The net sales of electricity of the Company stood at Rs. 3,783 crores and net profit was Rs. 179 crores.

The operations in the Surat distribution area were significantly affected by unprecedented floods during August, 2006. More than 85% of the area was submerged in water, requiring the Company to proactively switch off 1720 out of 2003 distribution substations, affecting 3.83 lacs consumers for few days. The estimated expenditure to be incurred for the replacement of the transformers and consumer services apparatus such as meters, cut outs etc. after the Surat floods is approximately Rs. 35 crores. The revenue expenditure for restoring the services, repairs etc. is estimated to be approximately Rs. 15 crores, of which an amount of Rs. 8.7 crores has already been incurred till 30th September 2006.

## FINANCIAL AND OPERATIONAL REVIEW AND ANALYSIS

### Financial Review:

A summary of financial results for the financial period 2005-06 (18 months) is presented hereunder:

Particulars	Amount (Rs. crores)	% of net sales
<b>Net Sales</b>	<b>3,783</b>	<b>100.00</b>
Cost of Electrical energy purchased	1,657	43.80
Cost of Fuel	1,019	26.93
<b>Contribution</b>	<b>1,107</b>	<b>29.27</b>
<b>Operating Profit (PBDIT) - including Other Income</b>	<b>714</b>	<b>18.88</b>
Interest & Finance Charges	63	1.67
Depreciation	291	7.69
<b>Profit before Tax</b>	<b>360</b>	<b>9.52</b>
Provision for Taxes	181	4.78
<b>Net Profit before Contingency Reserve</b>	<b>179</b>	<b>4.74</b>
Equity EPS (in Rupees) – not annualised	3.79	–
Equity Dividend (%) – proposed	12	–
ROCE%	7.83	–
Debt – Equity Ratio	0.23	–

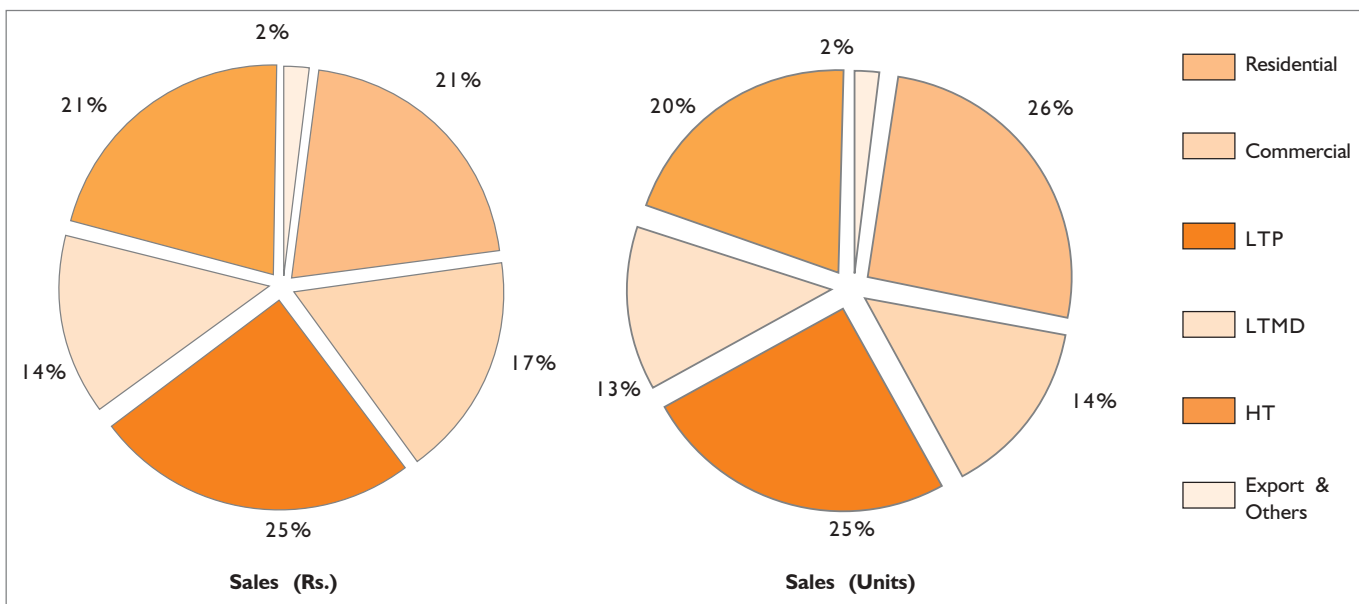
In FY 2005-06, the total revenues of the Company stood at Rs. 3,940 crores while the total expenditure was Rs. 3,580 crores.

## I. Revenue

The revenue of the Company comprises primarily sale of electricity, which is sourced from its own generation as well as purchase from Gujarat Urja Vikas Nigam Limited (GUVNL), erstwhile Gujarat Electricity Board. The Company also derives revenue from related services namely hire of meters, street light maintenance contracts, contract/ consultancy services, etc. and interest/dividend earned on investments.

### I.1 Sale of Electricity

The net revenue from sale of electricity for the financial period 2005-06 was Rs. 3,783 crores, which constituted about 96% of the total revenue. The Company witnessed demand growth from all major categories of the consumers. The sales of the Company are seasonal in nature. The charges for electricity are based on tariff approved by the Gujarat Electricity Regulatory Commission. Other major factor contributing to the net sales is the lower T&D loss of 9.67% witnessed during this financial period as against 11.99% during FY 2004-05. The Company also exports power to GUVNL in case power generated is more than system demand. The average revenue realisation per unit sold during the financial period was Rs. 3.74. The revenue composition and units sold to each category of consumers are shown in graphs hereinafter:



### I.2 Power/Contract Services Division

The Company earned Rs. 4 crores from the activities of the Division. This division undertakes activities such as Electrical Construction Jobs and Operation and Maintenance Jobs. The range of activities of the division also includes Thermal Imaging, Energy Audit, Demand Side Management etc.

### 1.3 Other Income

Other Income of Rs. 135 crores for the period under review comprises revenues from related business activities like hire of meters – Rs. 33 crores, Street Lighting Maintenance contracts - Rs. 19 crores besides other recurring items like interest & dividend on investments & deposits, sale of scrap, bad debts recovery etc.

## 2. Expenditure

The expenditure incurred is on purchase of power, fuel used for power generation and other generation, distribution, administration & other expenses including employees' costs, insurance etc.

### 2.1 Power Purchase

The total power purchase cost accounts for about 44% of net sales and 46% of the total expenditure. For power supplies in Ahmedabad and Gandhinagar, demand of power is met through own generation capacity of 500 MW and purchase of power from GUVNL. The higher efficiency achieved on generation front, represented by 10.24% growth in generation over FY 2004-05 on an annualised basis, has provided a cushion towards power purchased from GUVNL. For the supply of power to Surat, the entire requirement is sourced from GUVNL. The rates for power purchase from GUVNL are approved by GERC.

### 2.2 Fuel

The primary fuel used in power generation is coal and natural gas. Expenditure on fuel constituted over 28% of the total expenditure. The usage of fuel is also linked with the higher generation achieved by the Company. The coal used by the Company is procured both indigenously as well as imported. The Company makes conscious efforts to monitor the availability as well as optimise the sources of different fuel.

### 2.3 Operating Costs

The Operating Costs (Generation, distribution, administration and other expenses) other than fuel consist primarily of repair and maintenance of buildings, plant and machinery, employees' remuneration & benefit expenses, insurance, etc. These expenses, excluding fuel, represent a little over 15% of the total expenditure.

### 2.4 Depreciation

The depreciation charged to the profit and loss account during the year is Rs. 299 crores. A proportionate amount of Service Line Contribution and APDRP Grant attributable to depreciation on assets created against such Service Line Contribution and APDRP Grant is adjusted against depreciation for the period. The net depreciation after such transfer from Service line contribution and APDRP Grant is Rs. 291 crores. Depreciation on assets relating to 1100 MW SUGEN CCPP is treated as pre-operative expenses pending capitalisation.

### 2.5 Interest and Finance Charges

The interest charges consist primarily of interest expense on Term Loans and interest on security deposits placed by consumers of electricity. Borrowing costs amounting to Rs. 23 crores related to 1100 MW SUGEN CCPP are capitalised and shown as capital work-in-progress.

## 2.6 Taxation

The Company has provided for Rs. 160 crores in respect of Current Tax and Rs. 16 crores towards Deferred Tax. This financial period also saw introduction of Fringe Benefits Tax, payable on certain items of expenditure. The Company has provided Rs. One crore as liability computed as per the provisions of Income Tax Act towards Fringe Benefit Tax. An amount of Rs. 4 crores being the short provision made for earlier years in respect of the liability of transferor companies has also been debited to the Profit and Loss Account.

## 3. Net Profit after Tax

The net margin of the Company is 4.74% of the net sales for the period under review.

## 4. Term Loans

The term loans outstanding as at 30th September, 2006 stood at Rs. 623 crores. During the year an amount of Rs. 392 crores has been drawn for the 1100 MW SUGEN CCPP and soft loans have been received to the tune of Rs. 65 crores under the APDRP Scheme, Government of India. The Company has repaid an amount of Rs. 73 crores towards term loans including loan under APDRP. The repayments with respect to the term loans availed for the 1100 MW SUGEN CCPP will commence from year 2008 onwards.

## 5. Net Worth

The net worth of the Company at the end of financial period was Rs. 2,632 crores.

## 6. Appropriation to Reserves & Surplus

Out of the profits for the year an amount of Rs. 17.90 crores has been transferred to the General Reserve.

## Business Review – Generation:

### OPERATIONS

The power plants of the Company performed well during the year. The installed capacity and generation of power are as follows:

Particulars	Units	2005-06	2004-05	Annualised Growth %
		(18 months)	(12 months)	
Installed Capacity	MW	500	500	–
Gross Generation	MUs	5943	3594	10.24
Auxiliary Consumption	%	7.89	7.92	–
Less: Units used on auxiliary and transformation	MUs	469	301	3.88
Net Generation	MUs	5474	3293	10.82
PAF	%	95.46	91.61	–
PLF	%	90.37	82.06	–

The operating efficiency of power plants in general has improved during the year. The coal based Sabarmati Thermal Power plant consists of four Stations C, D, E and F built in different phases with capacity of 60 MW, 120 MW, 110 MW and 110 MW respectively. The availability factor (which is a measure of how much time a plant is available to generate power) of these stations improved to 94.91% from 92.32% in FY 2004-05 and the average PLF (which is a measure of capacity utilisation) increased to 93.25% from 86.69% in FY 2004-05. During the financial period, the Sabarmati plant generated 4906 MUs. The other highlights of the Sabarmati Power Plant are highest utilisation of Ash (94.71%) and continuous 198 “Accident free days work” constituting 3.5 million accident free man-hours work. The PAF for 100 MW Vatva Power Plant, consisting two gas turbines and a steam turbine, was 97.67% up from 88.74% in FY 2004-05 and PLF was 78.87% up from 63.55% in FY 2004-05. During the financial period, the Vatva plant generated 1037 MUs. It crossed 4009 days accident free work.

Further in order to increase the operational efficiency of the coal based generating plant, the Company has awarded a contract for revamping the coal handling facility at the Sabarmati Power Plant, which is about 30 years old. The project is likely to be completed by mid 2007. This will help in debottlenecking coal handling within the plant area facilitating continuous generation by increasing coal crushing and conveyor belt capacity.

With the intra-state Availability Based Tariff (ABT) to be implemented shortly in Gujarat, the Company has already installed ABT based Metering system at various power import and generating points. For the purpose state of art control rooms have been established at Ahmedabad and Surat.

## DEVELOPMENT

### **1100 MW SUGEN Power Project – A Mega Strategic Initiative:**

The Company is implementing 1100 MW SUGEN gas based combined cycle power plant at an estimated project cost of Rs. 3,096 crores at village Akhakhhol, near Surat following Government of Gujarat’s direction to set up its own generation facilities for the Surat Distribution Area as well as a backward integration move to secure a long term reliable source of supply for its Ahmedabad Distribution Area.

The project achieved financial closure in September 2004 by tying up the entire debt requirement of Rs. 2,167 crores with a consortium led by IDFC. Government of India has accorded Mega Power Project status to the project, which shall bring attached fiscal incentives. Central Electricity Regulatory Commission has accorded its in principle approval to the project cost.

The project will have 3 power blocks, each of 367 MW comprising advanced class gas turbines SGT5 4000F, steam turbines and common generators connected in single shaft configuration along with HRSGs. The Engineering, Procurement and Construction (EPC) Contract was awarded to the consortium of Siemens AG and Siemens Ltd. in June 2005 after following a rigorous and transparent ICB route for the evaluation of technology and suppliers, aided by third party supervisors for monitoring the process.

The design and implementation of this project also take into account the environmental protection and clean environment objectives of the Company. The Environment Impact Assessment of the project has been completed and a complete environment management system is in place.

The Company has already tied up the substantial part of the fuel requirement for the project and discussions are on for the balance with various suppliers. The Gas Transportation Agreement has been executed with Gujarat State Petronet Limited. A joint venture has been formed with Siemens for providing Operations and Maintenance services to the project.

The Project has achieved considerable progress and about 56 per cent of the EPC work has been completed. All essential Non-EPC works viz. intact well, water pipe line, reservoir, compound wall, roads and site office have been completed. The first block is scheduled to commission by the third quarter of 2007.

### **Power Evacuation Arrangements**

#### ***Joint Venture with PGCIL***

The Company has also entered into a Joint Venture with Power Grid Corporation of India Limited (PGCIL) for setting up dedicated transmission lines of 440 KV for evacuation of power from 1100 MW SUGEN project to Ahmedabad distribution area and to the National Grid through connectivity with PGCIL at Dehgam and Loop In Loop Out of Gandhar- Vapi line. This will be implemented under the aegis of Torrent Power Transmission Private Limited (TPTPL), which has already applied for the grant of the transmission license to Central Electricity Regulatory Commission. The Company will own 74% of the equity of TPTPL while PGCIL will have the balance. The estimated project cost is Rs. 550 crores and is expected to start soon.

#### **220 KV Transmission Project:**

The Company is creating power evacuation facilities for taking the power from the project to Surat distribution area by implementing a 220 KV Transmission Project. The project entails setting up of three 220 KV substations near Surat distribution area and connecting them to 1100 MW SUGEN project through installation of three double circuit 220 KV lines. The detailed engineering for the project is complete and orders for procurement of the major equipments have been placed.

### **Business Review – Distribution:**

#### **OPERATIONS**

Pursuant to the Scheme, the Company has been vested with the power distribution business of erstwhile Torrent Power AEC Limited and Torrent Power SEC Limited. Torrent Power AEC Ltd. was generating and distributing electricity in cities of Ahmedabad & Gandhinagar with a distribution area admeasuring 356 sq. kms. while Torrent Power SEC Limited had distribution area admeasuring 52 sq. kms. in Surat.

**Consumers:**

The number of consumers at the end of current financial period was 18.45 lacs. The Company added 1.04 lacs new consumers during the current financial period, which represents a growth of 5.96% over the consumer base at the end of FY 2004-05.

The consumer mix of the Company at the end of FY 2004-05 and 2005-06 is presented in the table below. There has not been any significant shift in consumer mix of the Company vis-à-vis FY 2004-05.

Consumer Category	2005-06	% of total consumers	2004-05	% of total consumers
Residential	1357346	73.56	1286669	73.89
Commercial	346571	18.78	319075	18.32
LTP/LTMD	136291	7.39	130107	7.47
HT	805	0.04	748	0.04
Others	4128	0.23	4689	0.28
Total	1845141	100.00	1741288	100.00

**Power Purchase and Sales:**

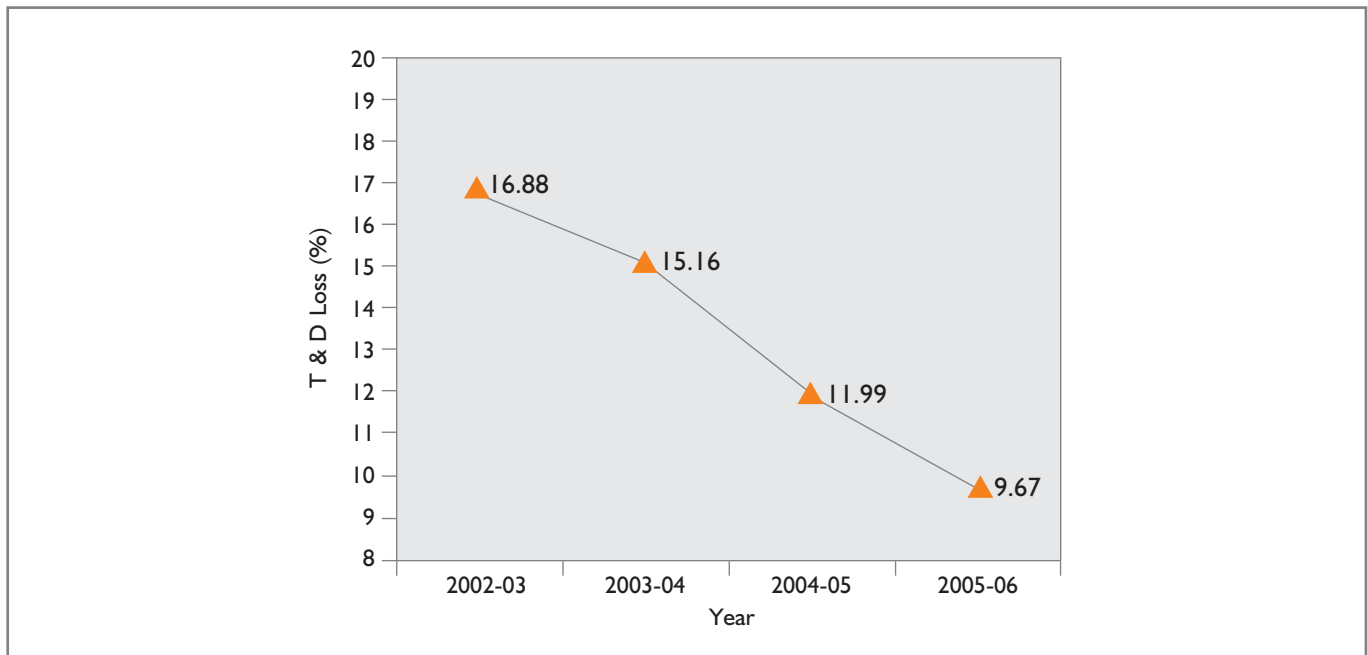
The system peak demand went up from last year's level of 1170 MW to 1333 MW showing an increase of 13.93%. The details of purchase and sale of power are as follows:

Particulars	Units	2005-06 (18 months)	2004-05 (12 months)	Annualised Growth %
Net Generation	MUs	5474	3293	10.82
Add: Purchase of power	MUs	5711	3494	8.97
Less: Units exported	MUs	73	5	873.33
Units Sent Out	MUs	11112	6782	9.23
Sales	MUs	10037	5969	12.10

**Transmission and Distribution (T&D) Loss**

The dedicated efforts of the Company on various fronts including detection of thefts, replacement of defective/stopped meters, Slum Electrification, consumer awareness initiatives etc. as well as strengthening and augmentation of distribution network have brought down the T&D loss to 9.67%, from 11.99% during 2004-05. This is amongst the lowest in the country.

The relentless efforts made by the Company to curb the T&D loss can be visualised by the reduction in the T&D loss achieved during past few years in the power distribution areas.



Well planned and organized efforts for the theft detection were made to minimize the commercial losses on account of theft of energy. The Company conducted about 12.50 lacs inspections and during the period under review, over 37,488 theft cases were detected. The recoveries from theft stood around Rs. 35 crores.

The massive drive for Slum Electrification in Ahmedabad continued vigorously. The Company released 29,255 new connections under Slum Electrification Programme.

#### **System Network:**

As at 30th September 2006, the system had a High Tension (HT) mains length of more than 4400 Kms. and Low Tension (LT) mains of more than 16000 Kms. while length of Extra High Voltage mains was more than 290 Kms. The number of EHV Sub-stations was 26, the number of power transformers was 140 and the number of distribution transformers was 6783.

The highlights as regards up-gradation of the system network are:

- Enhancement of power transformation capacity by about 200 MVA by commissioning of a 220 KV sub-station, a 66 KV substation and capacity addition at existing substations taking the total power transformation capacity to about 2554 MVA.
- Enhancement of distribution transformation capacity by about 174 MVA by addition of 594 new distribution transformers and replacement of existing transformers taking the total distribution transformation capacity to about 2780 MVA.

- Commissioning of three 33 KV Sub-stations at AUDA Garden, C. G. Road and Srinandnagar in Ahmedabad.
- 66 KV connectivity established between E and G Receiving Stations by laying 3 Single Core 66 XLPE cable in Surat.

The efforts of the Company in strengthening and augmentation of the system network has helped in reducing the average number of interruptions per consumer to 16.35 hours compared to 19.19 during FY 2004-05. The number of consumer hours lost was 16.91 hours per consumer in FY 2005-06.

#### **Consumer Services:**

There is an underlying commitment from the Company to deliver the best service experience to its consumers.

The Company provides a well spread out network of bill payment facilities in its distribution areas including online payments through partner websites using convenient channels like direct debit facility tied up with prominent banks. In addition, Torrent Power Mobile links (m-links) are a special customer service initiative for the twin cities of Ahmedabad and Gandhinagar wherein the Company's fully computerised mobile vans visit and offer bill collection services at more than 150 locations across the two cities.

The Company also runs a 24 × 7 state of the art in-house consumer call centre to handle all consumer complaints, queries and other information needs. The Company's website continues to be consumer friendly.

#### **DEVELOPMENT**

##### **Bhiwandi Distribution Franchisee:**

The Company has been selected as the Distribution Franchisee for Bhiwandi circle of Maharashtra State Electricity Distribution Company Limited (MSEDCL) in first such model in Indian Power Sector. Bhiwandi is a major textile hub of western India catering to 1.6 lacs consumers having an unrestricted demand of about 750 MVA. The agreement shall be valid for 10 years and during the validity of the agreement the Company would undertake all activities relating to distribution of power in the franchise area as an agent of MSEDCL. The Company would not take over any past liabilities.

The Company would commence its operations in Bhiwandi on signing of the Distribution Franchisee Agreement, which is under discussions.

#### **HUMAN RESOURCES**

The Company has a pool of capable and experienced personnel in all its areas of operations viz. technical, commercial, finance, human resources, information technology etc. To inculcate an orientation of high performance the employees are rewarded for their significant contribution and high performance under formal Scheme for the purpose. In house training programs on various technical, attitudinal and supervisory aspects with the help of internal as well as external faculty are conducted for

employees for developing their skills to meet with the changing technology, business practices and market requirements. The focus of the training has been to create high performance culture as well as bringing an improvement in the organisation for meeting consumer's need.

The industrial relations are cordial. The Company has resolved the long pending issue of wage settlement of its employees in Ahmedabad by entering into an agreement with their Union for the period 01-10-1992 to 31-03-2009. During the year, a wage settlement for employees in Surat was also concluded for the period from 01-01-2004 to 31-12-2006.

## **INTERNAL CONTROL SYSTEMS**

The Company has adequate internal control systems for achieving efficiency in operations, optimum utilization of resources, effective monitoring thereof and compliance with applicable laws and regulations. In order to ensure that all checks and balances are in place and all internal control system are in order, regular and exhaustive internal audits are conducted by the experienced professional firms based on an annual audit plan. The audit plan is made out with due weightage to the risk parameters associated with the business processes. The reviews are carried out to ensure follow-up on the audit observations.

Any significant observations are reported to the Audit Committee, which currently comprises three non-executive Directors including financial experts. The Audit Committee meeting is also attended by representatives of Statutory and Internal Auditors. The Company's auditors have also certified the existence of an adequate system of internal control in the Company.

Audit Committee regularly reviews the adequacy and effectiveness of the internal controls and suggests improvements for strengthening the same. The system of Internal Control is constantly improved through judicious use of technology.

## **INDUSTRY STRUCTURE AND DEVELOPMENTS**

Power is a critical requirement for economic development. Sustained socio-economic growth substantially hinges upon the availability of adequate and reliable power at reasonable rates.

### **Industry Structure**

Historically, the electricity business has been a monopolistic one. At the state level, the successor entities of the State Electricity Boards dominate generation, transmission and distribution of power. The central public sector companies such as NTPC, NHPC, PGCIL, etc. continue to be the major players in the power sector. But of late, private sector entities encouraged by the ongoing reforms in the power sector have made significant inroads in the industry. The Ministry of Power prescribes guidelines for all the technical and economic matters, duly assisted by the Central Electricity Authority for technical matters. The operations and activities of entities in the power sector are regulated by respective regulatory commissions. The Central Electricity Regulatory Commission is responsible for regulating the central sector generating plants and entities engaged in inter-state supply, transmission and trading of power while the State Electricity Regulatory Commissions are responsible for regulating the State level entities.

## Developments

Fully realizing the criticality of this sector, the Government has been taking, over the last few years, and is fully committed to take in the future, path-breaking initiatives for the rapid growth of the sector on the legal and regulatory front as well as the business environment front.

With the enactment of the Electricity Act, 2003 and the notification of the National Electricity Policy, the National Electricity Rules, the National Tariff policy and Competitive bidding Guidelines, the Government has created an enabling and investor friendly policy environment.

In January 2006, the Central Government notified the National Tariff Policy (NTP) for the power sector in compliance with Section 3 of the Electricity Act and in continuation of the National Electricity Policy (NEP) passed in February 2005. The tariff policy has set some objectives like ensuring availability of electricity to consumers at reasonable and competitive rates, ensuring financial viability of the sector and attracting investments, promoting transparency, consistency and predictability in regulatory approaches across jurisdictions and encouraging competition and efficiency.

The salient features of the National Tariff Policy, 2006 are as follows:

- i) All future requirements of power by distribution licensees to be procured competitively, except in cases of expansion of existing projects.
- ii) Tariff of new public sector generation and transmission projects to be decided on the basis of competitive bidding after a period of five years.
- iii) The Central Commission to notify the rate of return on equity for generation and transmission projects. The rate of return for transmission may be adopted by the State Electricity Regulatory Commissions (SERCs) for distribution with appropriate modification taking into view the higher risks involved. Either of the two, Return on Equity approach or Return on Capital approach may be adopted by Central Commission.
- iv) Any cash resources available to the Company from its share premium account or from its internal resources that are used to fund the equity commitments of the project under consideration should be treated as equity.
- v) For financing of future capital cost of projects, a Debt: Equity ratio of 70:30 to be adopted.
- vi) The Central Commission to notify the rates of depreciation in respect of generation and transmission assets, which would also be applicable for distribution with appropriate modification as may be evolved by the Forum of Regulators. The rates to be applicable for the purpose of tariff as well as accounting.
- vii) The Central Commission, in consultation with the Central Electricity Authority (CEA), to notify operating norms for generation and transmission. The SERC to notify operating norms for distribution.
- viii) MYT framework to be adopted from April, 2006. The framework to have a five year control period, which can be relaxed to three years in case of transmission and distribution if considered necessary by regulatory commission.

- ix) For generation, a two part tariff structure to be adopted for all long term contracts to facilitate Merit Order Dispatch. Availability Based Tariff (ABT) to be introduced at State level by April, 2006 as per NEP. This framework to be extended to generating stations, including grid connected captive plants as determined by SERC.
- x) The national tariff framework for transmission to be developed by CERC taking into consideration the advice of the CEA and to be implemented by 1st April, 2006.
- xi) Central Commission to establish (within one year) norms for capital and operating costs, operating standards and performance indicators for transmission lines at different voltage levels.
- xii) Investment by transmission developer other than Central Transmission Utility or State Transmission Utility (CTU/STU) would be invited through competitive bids as per Central Government guidelines. Tariff for projects to be developed by CTU/STU after 5 years or as decided by Commission to be determined through competitive bids.
- xiii) For Distribution, the State Commission to notify the standards of performance of licensees with respect to quality, continuity and reliability of service for all consumers. The Forum of Regulators to determine basis frame work on service standards.
- xiv) Framework for revenue requirement, costs, regulatory asset and tariff design is provided.
- xv) Consumers having consumption below 30 units per month may receive a special support through cross subsidy and such tariff should be at least 50% of the average cost of supply.
- xvi) The method and formula of determination of cross-subsidy surcharge are indicated. The cross-subsidy surcharge to be brought down progressively so that by year 2010-11, tariffs are within +/- 20% of the average cost of supply.

## **OUTLOOK AND OPPORTUNITIES**

The enactment of the Electricity Act and subsequent introduction of various regulations have opened up myriad opportunities in the Indian Power Sector. Though presently, opportunities for private sector seem to be available mainly in power generation, but it will be more prudent to follow a synchronized approach to make transmission and distribution also easy investment destinations.

The Company plans to expand operations in the areas of power generation, transmission and distribution by taking advantage of opportunities created by regulatory and economic reforms. The Company is actively pursuing various generation projects as well as the distribution franchisees being offered in several states in the country. In order to obtain fuel security, the Company is also evaluating options for entering into agreements with various companies having experience in coal mining, which would be captive supplies for the generation projects with coal as fuel.

The total installed generation capacity in the country was around 1,26,994 MW at the end of August 2006. The private sector constitutes only 12% of the installed capacity. The existing peak shortage in the country stands around 12% and energy shortage is around 8%. With the peak demand expected to rise by 2012 to a level of 1,57,107 MW, in order to fully meet both energy and peak demand , there is a need to create adequate reserve capacity margin which would require a capacity

addition of over 1,00,000 MW. The transmission and distribution system also need to be correspondingly augmented to meet the increased demand. If the role of private sector is assumed at 20%, Rs. 90,000 crore investment by the private sector is envisaged in the 11th plan period.

The Government of India is proposing the setting up larged-sized power generation projects of 4000 MW each (called ultra mega projects) with a project cost of approximately Rs. 25,000 crores which are expected to provide economies of scale and faster capacity addition leading to less expensive power. Government of India has appointed Power Finance Corporation (PFC) as the Nodal Agency to award these projects to private sector players, on the basis of competitive bidding of tariff. The Company has qualified in the PFC invitation for Request for Qualification for these projects. The Company proposes to bid for two projects, one at Mundra in Gujarat based on imported coal and second at Sasan in Madhya Pradesh based on indigenous coal.

The participation of private sector in nuclear power generation may also see light of the day with the historic nuclear deal cooperation between India and the US.

In the transmission segment, the target is to create a robust National Grid by 2012 besides strengthening the existing network. In transmission, so far the role of the private sector has been limited. In accordance with the Electricity Act, as also with the National Electricity Policy, the private sector's role is expected to increase gradually. It is expected about 10-15 per cent of the transmission system to be developed through the private sector route in the next 10-15 years and the proportion may be more in the next 25 years. The CTU, PGCIL has invited private participation in various transmission projects through joint venture route wherein 74% equity will be owned by the private investors and PGCIL will have the balance.

Under the new environment, 'Open Access' in transmission and supply has become feasible and shall provide fillip to the Company to source power at competitive prices.

## **RISK AND CONCERNS**

The Company has systems and practices to help in identifying potential risks and taking measures to mitigate those risks. The Risk Management Policy of the Company addresses all potential risks including Fuel risks (availability & pricing), Regulatory Risks (Tariff Regulation, Environment Regulation etc.), Consumer Risks (Revenue Realisation, Transmission Risks), Assets Risks (Natural Calamity etc.), Human Resource Risks and IT Risks.

The Growth of business is dependent on overall growth and development of the power distribution areas of the Company and in particular on the demand generated from the industrial and commercial consumers. However, the demand for energy has been rising at a high rate in Ahmedabad, Gandhinagar and Surat in past few years, which is in line with overall economic growth taking place in Gujarat. It is expected that the demand for energy in the power distribution areas would also grow in tandem.

The Company procures substantial quantity of power for supply from GUVNL. The demand supply gap in Gujarat may impact the availability of power from GUVNL. The upcoming 1100 MW SUGEN project shall help in bridging the demand supply gap in existing distribution businesses leaving potential of sale of power outside Gujarat.

The power generation plants use coal and gas as fuel. While domestic coal production has just kept pace with past demand, the requirement for coal is expected to increase significantly in the future, driven by significant capacity addition in the power sector. High dependence on domestic coal could therefore expose the Company to potential price and availability risks. In respect of imported coal, various domestic and international factors such as import duties, fluctuations in foreign exchange, volatility in international freight, adverse diplomatic development affecting relationship with Suppliers' Countries, changes in Government Policies etc. may affect the regularity and reliability of supplies.

The Electricity Act, 2003 makes possible introduction of competition through second licensee in the Company's existing license areas of operation. The Company has built a large and established distribution network that is difficult to replicate and with the track record of supply of reliable power at competitive costs with highest consumer orientation, is well equipped to meet the threat of competition.

The GERC has notified regulations, prescribing various norms and standards of performance for the licensees, and provided for penalties for deviating from the prescribed standards of performance. The Company has been able to improve its performance vis-à-vis GERC's prescribed standards of performance.

Power projects by nature of being capital intensive run the varied risks including delay in completion, performance risks and cost over-run. The Company is currently implementing 1100 MW SUGEN gas based power project near Surat, the past experience of the Torrent Group in implementing mega projects without any time/cost overruns provides confidence on the timely completion of the power project.

All the significant parameters concerning the commissioning of SUGEN Project have been already tied up and therefore no delay is expected in the technical commissioning of the entire project. The full capacity utilisation during the commercial operations of the project will require uninterrupted supply of fuel, i.e., Natural Gas (NG)/Regasified LNG (RLNG). At present in the world and in the country there is a mismatch of demand and supply of NG/RLNG, both in terms of quantity and seasonal variations. This results into higher cost of fuel besides interrupted supplies. The project enjoys partial certainty of availability of fuel at reasonable price. However, for the balance portion, if uninterrupted supplies are not available, to that extent the commercial operations will suffer from the utilization of full capacity. At the same time possibility of purchase of fuel on spot basis exists which may partially mitigate the risk. The power generated from the plant is proposed to be used in the Company's distribution areas and sold to Power Trading Corporation. The Company is yet to have firm commitment for the purchase of the balance power.

The Company has exposure in foreign currency for the upcoming 1100 MW SUGEN power project in addition to the regular procurement of imported coal as well as capital goods and spares. The depreciation of the Rupee against foreign currencies may affect the financial results of the Company. However the Company has partially reduced the susceptibility to foreign currency fluctuations by hedging part of the exposure with respect to the SUGEN project.

The operations of the Company are subject to certain risks generally associated with power generation, transmission and distribution businesses, and the related receipt, distribution, storage and transportation of fuels, feedstocks, products and wastes. The Company could be subject to substantial civil and criminal liability and other regulatory consequences in the event

that any environmental hazard were to be found at the site of any of its power plants, or if the operation of any power plants results in material contamination of the environment.

## SOCIAL CAPITAL

The Company has always appreciated its social responsibility as a part of its Corporate Governance philosophy as well as a utility. The Corporate Social Responsibility initiative “Sparsh” carried during the year saw many social and community activities like up-gradation of schools and hospital infrastructure, health camps, tree plantations, provision of various facilities for senior citizens etc.

The Company has been a significant contributor to the social capital of the cities and the state of power supply. A value added statement, particularly as regards society, is summarised below which details the contribution made by the Company towards the state exchequer, employment generation, creditors and lenders, and investors.

### Value Added Statement

(Rs. crore)

Particulars	Period ended 30th September, 2006
Gross Income	4642.60
Less: Cost of fuel & Electrical Energy Purchased	2675.74
Distribution, Administration & Other Expenses	276.94
Add: Net Income of Power / Contact and Fly-Ash Divisions	3.97
<b>Total Value Added</b>	<b>1693.89</b>
<b>Applied to Meet</b>	
Government Duty	707.07
Other Rates & Taxes	4.43
Employee Costs	275.74
Income Taxes (including short provisions of earlier years)	164.62
Provision for Deferred Taxation	16.41
Contingency Reserve	14.00
Dividend and Tax thereon	64.65
Interest Payments	63.10
Retained in Business	383.87
Total	1693.89

As seen from the above, your Company has added a value of Rs. 1,693.89 crores to the social capital during FY 2005-06.

For and On behalf of the Board of Directors

**Sudhir Mehta**

Chairman

Ahmedabad, 7th November 2006

## NOTES

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