Power Sector Reform in Orissa: Lessons for Other States in INDIA

Grant Activity Description

This PPIAF activity supported an independent consultancy to review experience in power sector restructuring and privatization in the Indian state of Orissa, which recently privatized its power distribution sector. The review was considered especially timely because other states in India are currently pursuing reform and are examining the lessons from the experience in Orissa.

Objectives

The focus of this review was to draw on international experience and evaluate the desirability and feasibility of different approaches to three key elements of Orissa’s reform package:

- The structure adopted for the reformed industry and the role of competition.
- The means and detail of private sector participation.
- The regulatory framework.

It is anticipated that the findings of this review will be used to:

- Inform the wider debate about power sector reform in India and South Asia.
- Influence the reform strategies of power sector reform in other Indian states and other national governments in the region.

Major Conclusions and Recommendations

The review produced a report capturing the main reform decisions in Orissa:

- **Industry restructuring model**: The sector structure adopted in Orissa (and chosen for implementation in other states) is based on the single-buyer model. Reform in Orissa continues to focus on non-competitive solutions, to protect the cross-subsidies necessary (in the absence of government support) to ensure the viability of the industry. In the next stage of reform the state is expected to implement a multi-buyer model, reallocating the contracts between the generators and the Grid Corporation of Orissa to the four distribution companies.

- **Privatization strategy**: Orissa privatized distribution through the sale of assets. Its experience shows the importance of undertaking financial restructuring at the beginning of reform, which may require using privatization revenues to pay down debt. Possible options for this financial restructuring include transferring debt to the private sector, transferring debt to the public sector, and writing off debt.

- **Regulatory framework**: Orissa’s experience has shown that price setting can be undertaken by an independent regulator. It has also shown the importance in India of adopting a transparent regulatory process for price setting. But there are major concerns relating to the qualifications of the members of the electricity regulatory commission and the lack of an explicit obligation for the regulator to ensure financial viability of regulated companies.
The reform in Orissa has shown that privatizing distribution through the sale of assets is a feasible option in India — an important message for power sector reformers throughout the country. Still, it is important to consider whether the privatization process could be improved. One widely recognized problem is that there were too few bidders, an aspect that needs to be improved in future privatizations. Two other key points emerged from the analysis:

- The distribution companies formed from the state electricity boards need to be larger than those in Orissa, to ensure financial viability and to meet the minimum size standard most international investors presently seem to require to participate in bidding.

- The price regulatory system needs to enable investors to form better estimates of likely revenue flows, particularly for the first five years or so. The process of annual tariff hearings is inconsistent with this. Reforming states could consider building into the initial legislation the price path for, say, the first five years.

Dissemination

A workshop held to prepare the final report State Power Sector Reform: A Review of the Orissa Experience, was attended by about 30 people in Virginia, USA, April 2000. A second workshop was held in New Delhi, India in June 2000 to disseminate the results of the Orissa power sector review.

This second workshop was targeted to national and state-level governments either involved in, or contemplating power sector reforms. A total of 74 participants attended, including officials from the central government ministries, state governments, and from central and state utilities. In addition, key private sector players associated with power sector reforms, and an NGO, were also invited. The workshop was chaired by the central government’s finance secretary.

Lessons from this review were also utilized in the South Asia Forum for Infrastructure Regulation (SAFIR) core training course (www.safir.teri.res.in).

Next Steps

Since this review was intended to provide useful information for the reforms underway in other Indian states, as well as for those being considered more generally at the national level, there is no obvious next step for this activity. Nevertheless, by providing information and promoting debate about the existing reforms this activity has helped focus the ongoing dialogue about electricity reform in India.