15.26 The ToR has identified four key public utility services and we have restricted our analysis to these, though other public services could, arguably, also be included in the broad categorisation of public utilities.Within public transport, we have looked at the pricing of services in both rail and road transport sectors. While examining each of these public utilities, we have been mindful, that except for the Railways, all of them fall within the domain of the States, and there are significant differences across States in the institutional mechanisms for the provision of these services.

Power

15.27 Between 2005 and 2011, there were few hikes in power tariff in the States.The consolidated financial position of all the state utilities deteriorated considerably and, in 2011-12, they incurred a combined loss of Rs. 92,845 crore (without taking into account the subsidy). Four states, which had not raised tariffs for six to eight years, accounted for 61 per cent of the combined loss. The distribution utilities of only two states showed profits in 2011-12.

15.28 Since State Governments are the sole owners of the overwhelming majority of power distribution entities, the financial health of these entities directly affects the fiscal position of the States. In this regard, it is noteworthy that the financial gap (the excess of the average cost of supply [ACS] over the average revenue realised [ARR]) at the national level has consistently increased over the last few years. This is partly due to the increase in the ACS, without a commensurate increase in tariffs. The financial gap can be segregated into two parts: one related to inadequate tariff increases and the other related to inefficiencies on the part of the distribution utilities, i.e., collection inefficiencies and technical losses. An analysis of the data for 2011-12 suggests that inefficiencies account for 59 per cent of the total financial gap at the national level, and inadequate increases in tariffs account for the rest. These inefficiencies can be addressed through a combination of full information and policies.

15.29 Metering is necessary for deriving the consumption details of the various consumer categories, as also for determining the subsidy element, estimating actual aggregate technical and commercial (AT&C) losses and, ultimately, for financial management. In the absence of metering, losses are sometimes determined based on the estimated consumption of the unmetered category, mainly in agriculture. The Electricity Act provides that no licensee shall supply electricity except through the installation of a correct meter in accordance with regulations. However, even eleven years after the enactment of the legislation, full metering has still not been achieved in most states. None of the States has been able to meter all their agricultural consumers.

15.30 Metering is also necessary as a basis for informed pricing decisions by the regulator. Unless there is universal metering, measuring losses becomes a notional exercise lacking credibility. **We, therefore, recommend that 100 per cent metering be achieved in a time-bound manner for all consumers as already prescribed statutorily.**

15.31 The Electricity Act provides for some insulation of pricing from the vagaries of policy fluctuations through Multi-Year Tariffs (MYTs). The MYT regulation provides an element of certainty on costs to all stakeholders, for which utilities can legitimately be held accountable. It also seeks to reduce the cost of regulation and regulatory intervention in routine utility matters. The MYT framework has been implemented in most States.

15.32 On the provision of subsidies by State Governments, Section 65 of the Electricity Act mandates that these need to be paid in advance to the utilities. The Section also stresses that no

direction of the State Government to subsidise a certain section of consumers will be operative, if payment is not made in accordance with tariffs fixed by the SERC. At present, the subsidy is not being paid in advance. The timely payment of subsidies is extremely important from the point of view of fiscal transparency perspective. **The Electricity Act, 2003, currently does not have any provision of penalties for delays in the payment of subsidies by State Governments. We, therefore, recommend that the Act be suitably amended to facilitate levy of such penalties**.

15.33 Though statutory provisions are in place, the experience of the last eleven years suggests that the mere enactment of the Electricity Act and the appointment of regulators have not necessarily led to the intended outcomes. In practice, it appears that SERCs have tended to be influenced to keep tariffs low, despite legitimate increases in expenses of the distribution companies. In some SERCs, this is done by classifying approved expenditures as "regulatory assets" and not factoring them into the tariff increase. These regulatory assets continue to remain on the books of the utilities even after the mandated three-year period. This suggests that SERCs need to be strengthened in order to effectively carry out their statutory responsibilities.

15.34 A key issue in the functioning of the SERCs is their financial independence and autonomy. The SERCs' primary sources of income include grant from State Governments and their own revenue generated through fees for annual licenses and the filing of applications. **In order to provide financial autonomy to the SERCs, Section 103 of the Electricity Act, 2003, provides for the establishment of a State Electricity Regulatory Commission Fund by State governments, to enable the SERCs to perform their responsibilities, as envisaged under the Act. We reiterate the importance of financial independence of the SERCs and urge all States to constitute a SERC Fund, as statutorily provided for.**

Railways

15.35 The tariff structure in the Railways is characterised by very low passenger fares and high freight charges. Indian passenger tariffs are one-fourth of those in China, one-ninth of those in Russia, and nearly one-twentieth of tariffs in Japan. In purchasing power parity terms, too, the tariffs reflect similar gaps. To remedy this, a regulatory framework for tariff setting is urgently required. This will enable costing of services and timely rate revisions along commercial principles for both passenger and freight traffic.

15.36 We note that the Union Government has recognised this need and recently approved the setting up of a RTA. Though this requires an amendment of the Railways Act, 1989, an interim RTA has been set up as an advisory body, pending the enactment of a comprehensive legislation. The primary function of the RTA would be to develop an integrated, transparent and dynamic pricing mechanism for the determination of tariffs for the Indian Railways.

15.37 The RTA is expected to advise the Ministry of Railways on matters related to the fixation of tariffs, that is, rates for passenger and freight services (including freight traffic carried in privately owned wagons using the railway system) and track access charges. Apart from focussing on the requirements of the Railways, the Authority will engage with all stakeholders to usher in a new pricing regime through a transparent process. This is expected to lead to the rationalisation of fares and freight structures, improvements in the fare-freight ratio and gradual reduction in the cross-subsidisation across different segments.

15.38 **We endorse the initiative to set up a RTA and urge expeditious replacement of the advisory body with a statutory body, through necessary amendments to the Railways Act, 1989.**

Road Transport

15.39 Passenger road services in most States are run by SRTUs. In addition, companies, government departmental undertakings and municipal undertakings also provide public transport services. According to the "Review of the Performance of SRTUs, 2012-13" brought out by the Ministry of Road Transport and Highways, of the thirty-eight SRTUs, only two reported net profits in that year. The aggregate losses of the SRTUs amounted to Rs. 7,269 crore, 56 per cent of which was accounted for by three SRTUs. Departmental undertakings provide road passenger services in a few states, mainly in the North-east, and their performance is no different from the SRTUs. However, in comparison with the power sector, the fiscal impact of the SRTUs on state finances is limited.

15.40 Section 22 of the Road Transportation Corporations Act, 1950, which deals with corporation finances, states that "it shall be the general principle of a Corporation that in carrying on its undertaking it shall act on business principles". In terms of pricing, the first step would then be to separate the social obligations of providing bus connectivity to all villages as well as concessional fares to socially deserving target groups from the rest of the pricing formula. Both these require government financial support, and it is axiomatic that such fiscal support should be contingent on the reliable and timely supply of relevant information. However, we observe that the accounting information system is incomplete and lacks transparency and that annual reports are not released in time. **Accordingly, we recommend that accounting systems in the SRTUs make explicit all forms of subsidy, the basis for determining the extent of the subsidies and also the extent of reimbursement by State Governments.**

15.41 At present, there is no independent regulatory authority for the road transportation sector. Current arrangements, both at the Union and State level, give rise to a potential conflict, as the rule-making body is also the implementing body. Consequently, there is no independent assessment of the performance of the SRTUs across various parameters. **We, therefore, recommend the setting up of independent regulators for the passenger road sector, whose key functions should include tariff setting, regulation of service quality, assessment of concessionaire claims, collection and dissemination of sector information, service-level benchmarks and monitoring compliance of concession agreements.**

Irrigation

15.42 Water fees/charges for irrigation are collected from farmers for two main reasons. The first is to cover operations and maintenance (O&M) costs, so that a project is financially sustainable. In many cases, fees include a charge for the cost of capital required to construct the project. This cost recovery is important for future investments in irrigation. The second objective is to encourage farmers to use less water per unit of output, or generate higher net economic returns per unit of water, or both. Historically, the first objective has been paramount, but as water scarcity increases, the water-use efficiency objective is likely to grow in importance and be accorded higher priority.

15.43 At present, there is no uniform set of principles for fixing water rates. Water charges vary from State to State, project to project and crop to crop. Rates vary widely for the same crop in the