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The Enron Corporation

Corporate Complicity in Human Rights Violations

"Many energy companies have invested in closed or repressive countries -- arguing that their investment would help develop the local economy and thereby improve the human rights situation. But in this case, Enron has invested in a democratic country -- and human rights abuses there have increased. Enron hasn't made things better for human rights; it has made things worse."

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REPORT OF THE CABINET SUB-COMMITTEE TO REVIEW THE DABHOL POWER PROJECT

CHAPTER I

INTRODUCTION

1.1 In terms of the decision of the Cabinet of the Maharashtra Government, a Sub-Committee of the Cabinet was constituted on 3rd May 1995 (Annexure I) to review the Dabhol Power Project of the Dabhol Power Company (DPC), a private company with unlimited liability, promoted by the Enron Power Development Corporation, U.S.A. and to report whether it subserves the interests of the State of Maharashtra. The Sub-Committee was headed by Shri Gopinath Munde, Deputy Chief Minister and consisted of Shri Sudhir Joshi, Minister for Revenue, Shri Hashu Advani, Minister for Finance and Planning, and Shri Liladhar Dake, Minister for Industries, Cottage Industries Law & Judiciary as members. Shri Hashu Advani, Minister for Finance and Planning could not attend after the first meeting due to his ill-health.

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May 29, 1995

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1.2 The terms of reference of the Sub-Committee were as under:

- (i) The reasons for not calling competitive bids.
- (ii) Whether there was any secrecy in relation to the discussions and negotiations on the project.
- (iii) Whether the capital cost of the project is reasonable.
- (iv) Whether any unusual or undue concessions were given for the project.
- (v) Whether the rate of purchase of power is reasonable.
- (vi) Whether there will be any adverse impact on the environment in the Konkan area because of the project.
- (vii) How far the project is useful for the development of the State, and
- (viii) Any other important issues relating to the project.

1.3. As per the G.R. No. BPC 1095/CAR-2670/Energy II dated 3rd May 1995, Secretary (Energy) acted as coordinating Secretary and, along with Secretary (Finance), Principal Secretary (Planning), and Principal Secretary (Law and Judiciary), assisted the Sub-Committee in their deliberations.

1.4 The Sub-Committee met on the following dates in May 1995: 3rd, 9th, 10th, 16th, 17th, 18th, 19th, 25th, 26th, and 29th and heard the representatives of institutions and interested individuals. The Sub-Committee also heard the representatives of the DPC, who made oral and written presentations. The Chairman and other officers of the Maharashtra State Electricity Board (MSEB) were present on all the days when the Cabinet Sub-Committee met. Detailed oral and written presentations on several days were made by the Chairman and other officers of the MSEB on the background of the project, as well as on the various issues relating to the project. The other institutions and persons who made oral and/or written presentations before the Sub-Committee were:

Sr. No.	Name of the Institution	Person represented	Date of meeting
1.	Tata Institute of Social Sciences	Dr. Vidya Rao	9.5.95
2.	Prayas, Pune	Shri Subodh Wagle	18.5.95
3.	Soclean, Mumbai	Shri Debi Goenka	18.5.95
4.	Dev and Associates, Pune	Shri Jayant Deo	18.5.95
5.	Mumbai Grahak Panchayat	Shri Shirish Deshpande	18.5.95

6.	Swadeshi Jagan Manch	Shri Ravindru Mahajan	18.5.95
7.	Janata Dal	Smt. Mrinal Gore Shri P.B. Samant Shri P.D. Kunte	18.5.95
8.	Rambhau Mhalgi Prabodhini	Shri Kulkarni V.G.	18.5.95
9.	-	Shri K.S. Joshi	19.5.95
10.	Save Bombay Committee	Shri Kisan Mehta	19.5.95
11.	Independent Power Producers Association of India, Mumbai	Shri Harry Dhaul	19.5.95
12.	Enron Virodhi Sangharsh Samiti	Shri R.G. Karnik Shri A.D. Golandaj Shri Shankar Salvi	19.5.95
13.	-	Shri S.R. Paranjpe	19.5.95
14.	Lal Nishan Paksha	Shri Raja Patwardhan	25.5.95
15.	Dabhol Power Corporation	Ms. Rebecca Mark and others	25.5.95 26.5.95
16.	Lok Vihyan Sanghatana, Pune	Dr. Sulbha Brahme	written submissions
17.	Tata Energy Research Centre	Dr. Pachauri	written submissions

1.5 A large volume of evidence was presented, running to several thousands of pages covering almost all aspects of the Dabhol project. The Committee procured the files and documents on Enron/DPC project maintained by the Energy Department of the Government of Maharashtra and also many other documents related to the deal.

1.6. At the outset, the Sub-Committee expresses its deep appreciation and gratitude, particularly to the voluntary agencies and individuals who had taken extraordinary pains to marshal critical facts about a complex project.

CIRCUMSTANCES LEADING TO THE REVIEW

1.7 The Dabhol Power Project of the Dabhol Power Company (DPC) promoted by the Enron Power Development Corporation—which for easy reference is referred to as the

“Project”—had invited loud public criticism all over India, although the Project belongs only to Maharashtra. Cutting across all political and ideological differences, public men and women of acknowledged competence, integrity, and eminence had severely questioned the Project. The Project became the subject of techno-economic and political debate. Many environmentalists too joined the public outcry. The press, in general, became critical of the Project. The Project generated one of the most intense intellectual debates at the national level on any single commercial venture. But the issue was not confined to the press or seminars or intellectual debates. It soon took the shape of a mass agitation with the ordinary public getting involved in satyagraha, giving the Project law and order dimensions. Thus, during the years 1993 and 1994, the Project snowballed into a major public issue, particularly in Maharashtra where elections to the State Assembly were due in February 1995.

1.8 The public debate on the Enron Project served to highlight several intriguing, unusual, and unreasonable features of what was viewed by many as a thoroughly one-sided arrangement in favour of the DPC, and against the national interest, in particular, against the interests of Maharashtra. What the public perceived as secret and surreptitious was the manner in which the negotiations were conducted and the Project was approved. The intriguing conduct of the previous State Government only served to heighten the rising suspicion and apprehensions in the public mind that the previous government had a lot to conceal. The previous government had also claimed confidentiality about the Project papers which only added to the public apprehension that there were extraneous motives and corrupt elements in this Project. Even when some public spirited persons challenged the Project in the Court of Law, the previous government insisted before the Court that it shall not make the crucial documents of the Project public.

1.9 As it happens, and it is bound to happen in all democracies, the widely suspected and highly questioned Project became an issue in the State Assembly elections held in January 1995. The Shiv Sena-BJP alliance which fought the elections against the then ruling Congress had emphatically declared in their joint electoral declaration addressed to the electorate of Maharashtra that if they came to power, the Project would be reviewed and if it was found to be against the interests of the country, the State of Maharashtra, and the people, it would be canceled. The Joint Manifesto of the Shiv Sena-BJP alliance for the Maharashtra Assembly Elections 1995 had made a commitment that the “Suspicious Enron deal will be reviewed.” Thus, the Enron issue had become a trans-party and trans-political public and electoral issue involving the entire public of Maharashtra where the State elections were held early this year. Though the polling in a majority of the constituencies in the State elections concluded on 12th February 1995, the votes were counted much later in March, 1995 because of the staggered election programme in different States. The electoral verdict of the people of Maharashtra was in favour of the Shiv Sena-

BJP alliance which assumed office on 14th March 1995 under the chief ministership of Shri Manohar Joshi. Thus, the Shiv Sena-BJP alliance had not merely secured the mandate of the people to review the Project, but under the mandate of the people, it was obliged to review the Project forthwith and in an expeditious manner, so as to restore the peoples' confidence in the institution of the government. It was in these circumstances that the new government appointed the present Sub-Committee to review and make recommendations on the Enron Project.

CHAPTER II

THE PROJECT IN BRIEF

2.1 The Project is being set up by DPC which is promoted by EPC of the U.S.A. in association with General Electric and Bechtel Engineering, also of U.S.A. The Project envisages two phases of implementation for establishing a total capacity of 2,015 MW at Dabhol on a Build Own and Operate basis (BOO) for which a Power Purchase Agreement (PPA) was signed having a duration of 20 years. MSEB has the option to extend the PPA by 5 or 10 years. If it does not do so, the PPA will terminate on its expiry date and MSEB can require that the power station be transferred at a price equal to 50 percent of the depreciated replacement cost. Phase I of the project involves installation of 695 MW capacity, the balance 1,320 MW being installed in Phase II. The Project is based entirely on imported fuel and Phase I would use imported distillate oil. After the installation of Phase II, the entire 2,015 MW capacity will be operated on imported Liquefied Natural Gas (LNG). The Enron Project is the first and only project in India solely based on imported LNG. The annual foreign exchange outgo at the current rupee-dollar rate is estimated at \$1.45 billion which has a built in potential for increase on account of escalation. Phase I of the Project is to be commissioned in December 1997. The total cost of the Project is over \$2.8 billion for both Phases, of which \$910 million relates to Phase I. The arrangement between DPC and MSEB embodied in the PPA involves a guaranteed purchase of power at 90 percent PLF [Plant Load Factor] of the Project at rates calculated by a formula in the PPA which has built in escalation provisions. In addition, the Maharashtra Government has guaranteed payment of dues under the PPA by MSEB to DPC. This is also counter-guaranteed by the Central Government. The choice of Enron for the Project was made not by inviting public bids, but by private negotiations with a single party. Several features and provisions of the agreement between Enron and MSEB were intriguing and unusual and such intriguing features began to surface in public through the media and through social and political activists. The choice of Enron without inviting bids was challenged before the Courts. The previous administration had contended before the Courts that choice without bids was not improper. The Court held that the government could, in appropriate cases, make a choice without public bids. Even the judicial verdict did not allay the apprehensions of the public and the issue continued to rise like a tornado as exposure after exposure of the deal

began to add to the unusual character of the Enron-MSEB arrangement. The several unusual, intriguing, and incredible aspects of the Enron-MSEB arrangement many of which were widely publicised and which led to public suspicion and apprehensions about the Project, were the starting point of the Sub-Committee's review work.

CIRCUMSTANCES LEADING TO THE SIGNING OF THE POWER PURCHASE AGREEMENT

2.2 The chronology of events clearly points out that the then State Government did not, at any stage, explore the possibility of getting competitive bids and preferred to deal with Enron alone in this matter. The chronology of events is as follows:

In June 1992: An Indian high-power delegation returns to India after a visit abroad in May/June 1992, during which Enron, it is claimed, showed interest to set up a power plant in India based on LNG technology.

On 10.06.92: Almost immediately, the Secretary (Power), Government of India, informed the MSEB Chairman at Delhi that a team of Enron officials would visit Maharashtra and requested him to show some sites on the coastline of Maharashtra so that the power plant could be set up there.

On 15.06.92: Within 5 days, the Enron team with representatives of General Electric, arrived in Delhi and had discussions with GOI officials.

On 17.06.92: Within the next two days, the Enron-GE officials arrived in Bombay.

On 18.06.92

& 19.06.92: They were taken to Ratnagiri, Pawas, Dabhol, and Nagothane. They were also shown Usar, Uran, and Nhava Sheva Port by helicopter.

On 19.06.92: A meeting of the team in MSEB's office was arranged with officials of the Maharashtra Government at which the team chose the Dabhol site.

On 20.06.92: MoU [Memorandum of Understanding] between MSEB and Enron for the Dabhol project was signed.

2.3 Thus, in a matter of less than three days after its arrival in Bombay, an MoU was signed between Enron and MSEB in a matter involving a project of the value of over Rs. 10,000 crores at that time, with entirely imported equipment, in which, admittedly, no one in the Government had expertise or experience. In fact, the file does not even show what Enron was—what its history is, business or accomplishment. It looked more like an ad hoc decision rather than a considered decision on a durable arrangement with a party after obtaining adequate and reliable information. Neither the balance sheet and annual accounts of Enron, nor any information about its activities, area of operation, its associates, etc. was obtained by the government then or even later. Further, the MoU, as

the then Secretary, Energy, Maharashtra Government has recorded, casts a responsibility on the MSEB to finalise certain decisions so that a proper Power Purchase Agreement could be signed “in sixty days.” This MoU was termed as “one sided” by the World Bank in its letter dated 8th July, 1992. The CEA [Central Electricity Authority] had also considered it to be “one-sided” as referred in their comments contained in the enclosure to the letter dated 21st July 1992 from the Ministry of Power.

2.4 At the suggestion of then Secretary, Energy, Maharashtra and as approved by the then Chief Secretary and as repeatedly requested by the State Government, the Central Government secured the services of the World Bank to assess the Enron project. In fact, at one stage, Enron itself was seeking to involve the World Bank for finance and participation as, in the view of the then Chief Secretary, Maharashtra, “Enron is convinced that the World Bank has full and scientific knowledge of the working of the Power sector in India.” This is despite the fact that the Finance Secretary felt that Enron would pre-empt the other projects of the State from getting World Bank assistance, if Enron were allowed access to the World Bank funds. However, later in its Report, the World Bank clearly advised that the Enron Project is (i) unviable, (ii) does not satisfy the test of least cost power, (iii) is too large and (iv) is not justified by the power demands of Maharashtra. Once the World Bank’s assessment came and it clearly vetoed the Project, the response of all those who persistently asked for the World Bank advice, confessing that in those areas the Government did not have experience or expertise, was to underplay and even suppress it. Almost every official other than the then Secretary, Finance supported the Project ignoring the World Bank’s advice. This report of the World Bank dated April 30, 1993 said that, as a project, in their view, it was unviable and they could not finance it. The efforts of the protagonists of the Enron deal were hence to regard World Bank’s views as merely that of a consultant or, at best, of a financier of the Project. Its views were sought because the Government of Maharashtra had no expertise in the techno-commercial aspects of private power production at the international level. The World Bank’s views covered all aspects including whether the Project would suit the interest of Maharashtra—and the World Bank advised that the Project as formulated did not suit the needs of MSEB. The World Bank’s letter of April 30, 1993 is at Annexure II. The conclusion reached by the World Bank in para. 16 of the annexure to their letter was that, considering the data available regarding the Demand of Energy, “an LNG-based power plant operating in base load is not the least cost option for expanding power supply.” It was also pointed out by the World Bank in para. 17 of the Annexure to their letter that, “the suggested load increase is unproven and the proposed high forecast is not a suitable basis for evaluating the Project.” From the documents made available to the Sub-Committee and the presentation made before it, it is clear that neither any independent assessment of the demand of energy was made (though it was claimed that CEA has formed a group with MSEB representatives to study the demand for

power), nor any comparative study of different fuels was carried out before opting for imported LNG as the fuel for the Project. In respect of these issues, MSEB merely pointed out the non-availability of local coal and gas and the environment-friendly nature of a LNG-based power plant as compared to a coal-based plant. The World Bank, in its further letter of 26.7.93 (which is at Annexure III) reconfirmed its earlier findings and advised the reshaping of the Enron Project to primarily serve higher value intermediate loads and stated that this would require consideration of a larger consumer base on a regional basis to share the risks and costs of the project. It also advised on the phasing and timing of the LNG project. The World Bank never certified the Project as viable at any point of time.

2.5 The chronology of events about the splitting of the capacity of the Project are as below:

20.06.92: The MoU was signed assuming a nominal capacity of 2,000 to 2,400 MW.

8.07.92: The World Bank team was available in Bombay for preparation of Request for Proposal (RFP) for the Nagothane Power Project. The team was requested to evaluate the MoU of Enron. The preliminary analysis, forwarded by the World Bank to the Government of Maharashtra via their letter of 8th July 1992, mentioned the one-sided nature of the MoU.

18.08.92: In the High Power Board meeting of the Government of India Secretaries held on 18.08.92, MSEB indicated that it had suggested that Enron may study the possibility of developing the project in two phases of 1,200 MW each. However, Enron was of the view that due to economies of scale, they would like to retain the configuration they had proposed.

29.08.92: Enron submitted an application to Chairman, FIPB [Foreign Investment Promotion Board] for a combined-cycle 2,550 MW power project based on LNG. It was envisaged that No. 2 fuel oil could be used to fuel the power station for up to one year following the commencement of commercial operation, depending on the availability of externally-sourced LNG. Initial generation of power was expected to begin in December, 1995. The power generation system would be initially using fuel oil and subsequently using LNG. The main plant equipment remain the same for No. 2 fuel and for LNG.

5.12.92: In the FIPB meeting of 5th December, 1992, Enron were informed that their proposal may be down-sized to enable it to be handled at the present stage. Two options were available: (a) scaling-down to 1,920 MW at a cost of U.S.\$ 2.65 billion and (b) a project of 1,200 MW at a cost of U.S.\$ 1.95 billion. It was brought out by Enron that if the size of the project came down to 1,200 MW, one train load of LNG would still have to be purchased and the surplus of gas marketed directly to industrial consumers. In view of the matching of one train load of LNG with the plant size of

1,920 MW, Enron agreed to work on the basis of 1,920 MW with the possibility of further expansion later.

3.02.93: FIPB approved the proposal to set up a 1,920 MW power plant (which capacity may be expanded to 2,550 MW at a future date) based on imported LNG.

12.03.93: Director, (Fund Bank), Ministry of Finance, Department of Economic Affairs, New Delhi informed the World Bank that the clearance to 1,920 MW Combined Cycle Gas Turbine project at Dabhol is given by the Government of India and requested the World Bank to consider this project for World Bank financing and requested the views of the World Bank on the DPC.

30.04.03: World Bank communicated their views on the DPC to Secretary, Department of Economic Affairs, Ministry of Finance, New Delhi.

The above chronology of events indicates that it is difficult to appreciate when and why the decision to split the project and to use No. 2 fuel oil for Phase I was taken. Nor is it clear that this was done after a careful consideration of the requirements of MSEB and the State of Maharashtra. In fact, it seems to address only the concerns of Enron. The conduct of the negotiations shows that the sole objective was to see that Enron was not displeased—it is as if Enron was doing a favour by this deal to India and to Maharashtra. In fact, the entire negotiation with Enron is an illustration of how not to negotiate, how not to take a weak position in negotiations, and how not to leave the initiative to the other side.

CHAPTER III

3.1 The Cabinet Sub-Committee has carefully considered the various documents presented to it as also those obtained by it and the various points submitted during the oral presentations by the different institutions/persons who appeared before it. The Sub-Committee also received a copy of the statement of Shri Sharad Pawar, Leader of the Opposition in the Council. The response of the Sub-Committee on some of the major points raised by him is given in Annexure IV. The findings of the Committee on the terms of reference are given below:

3.2 Reason for not having competitive bids:

The issue about competitive bidding has repeatedly arisen in the context of private sector power projects. The issue has now been settled by the new Government of India policy. The Lok Sabha Standing Committee on Energy (May 1995) in its 26th Report also deals with how the private negotiation policy was wrong. But between private negotiations between a single party and the Government, on the one hand, and competitive bidding as per the new policy, a third option also existed. In the third option, which is not as transparent as the second option—we involve more than one party in the negotiation for awarding the contract. The policy of competitive bidding was itself followed by the State of Maharashtra in respect of private power projects, as in the

cases of Nagothane and Khaparkheda projects. There is no reason cited in any file note or correspondence as to why another bidding party could not have been involved in the Project. Involving another party does not make it an open bid, but prevents it from being a secret pact between the State and a chosen party. In fact, during the first visit of Enron on 18/19 June 1992, the team was shown, in addition to Dabhol, Nagothane and Ratnagiri, but they chose Dabhol. By not exploring the possibility of inviting another party capable of setting up such a project, the State Government deprived itself of the advantage of competitive bidding in the evaluation of the Project. It is this one-to-one dealing with Enron and absence of competition that led to secrecy and lack of transparency in the negotiation and handling of this Rs. 10,000 crore contract. As a result of this, the State Government could not resist successfully the insistence of Enron on confidentiality of negotiations for commercial or other reasons and ultimately this resulted in an uneven agreement. The Sub-Committee is aware that matters relating to lack of competitive bidding and secrecy in negotiations have been agitated before the High Court. While the High Court has said that the course followed by the State Government is not illegal or arbitrary, this does not mean that this is the best method, especially in respect of transactions involving public money where transparency is by far the most important criterion so as to bring credibility in Government functioning.

There was no effort on the part of the then Government to explore the possibility of involving another party interested in making private investment in the new power policy in India out of a number of multinational parties contacted by the Government during their visit abroad to market the power sector in India. The Sub-Committee has, therefore, no hesitation in concluding that this basic

failure of the State Government that led to further problems in the one-to-one negotiations.

3.3 Whether there was any secrecy in relation to the discussions and negotiation in the Project:

The matter regarding secrecy in respect of Government's/MSEB's agreement with DPC was agitated in various High Court cases. It was alleged that the deal was shrouded in secrecy. It was also the contention of Government/MSEB that the proposal was deliberated at length for one-and-a-half years. The draft agreements were prepared from time to time and it was ultimately after 8 or 9 drafts that the PPA was finalised. It was, therefore, claimed that nothing was done secretly. The then Government/MSEB claimed confidentiality of documents on account of the commercial nature of the transactions. No doubt, the documents were shown to the parties to the litigation but this was done only on the instruction of the High Court. The Government refused to make these public nor were they made freely available to the Members of the Legislature. As soon as the present Government came to power, it demanded that the

documents, PPA and Fuel Management Agreement should be made public and the DPC readily agreed to make it public. Therefore, it is very clear that even if the previous Government had not insisted on such great secrecy, there would not have been any adverse commercial impact, as claimed. Considering all these developments, the Sub-Committee concludes that while the principle of confidentiality of commercial transaction may be a sound principle in respect of private transactions, in the case of Government transactions where public finance is involved, recourse to such a method is always fraught with danger, raising suspicion in the minds of the people, regarding purity of the deal and, therefore, it was not correct on the part of the State Government to deprive general public access to the vital documents like the PPA and the Fuel Management Agreement.

The Sub-Committee has also noted the testimony given by Ms. Linda Powers, Vice President, Global Finance of Enron Development Corporation before a Committee of the U.S. House of Representatives, stating that, "...our company spent an enormous amount of its own money—approximately \$20 million on this education and project development alone, not including any project costs." The Sub-Committee feels that these remarks need further clarification.

3.4 Whether the capital cost of the project is reasonable

The most intriguing aspect of the Enron project has been the incredibly high capital cost of the Rs. 4.49 crores per MW. The previous Government and Enron have been justifying it on the basis that it compares well with the capital cost of the other Fast Track Projects cleared for the private sector. The comparative table of the capital cost of the seven Fast Track Projects is as under:

Project	Capacity (Megawatts)	Type of Fuel	Cost per Megawatt (Rupees in Crores)
Enron	2,015	Gas (LNG)	4.49
Jagrupadu	235	Gas	3.52
Godavari	208	Gas	3.60
Vishakapatnam	1,000	Coal	5.81
Mangalore	1,000	Coal	5.08
Ib Valley	420	Coal	4.82
Zero unit NLC	250	Lignite	4.50

It is evident from the above data that the cost of the Enron Project is more comparable to the coal based projects than to gas based projects. Even as compared to the other gas based projects the cost of the DPC Project is clearly higher by at least 25 percent. Considering the fact that the other gas based projects, Jagrupadu and Godavari, are insignificant in

capacity as compared to Enron, a comparison with them will be misleading. Being small projects, their capital cost per megawatt is bound to be higher. Even then, the capital cost of the Enron project is higher than the cost per megawatt of these smaller projects.

Capital cost of any project depends on the type of fuel used. Empirical evidence shows that the capital cost of coal-based power plants will be much higher than that of gas-based power plants.

The Committee had the opportunity to peruse the study on comparative capital costs of coal- and gas-based power plants conducted by the U.S.-based Advanced Light Water Reactor Programme (ALWR, PALO ALTO, U.S.A.). The draft report is attached at Annexure V. If the findings of this report are applied to the present case, it would be clear that the capital cost of the DPC is on the high side and needs to be considerably reduced. The capital cost of the Enron Project which is gas-based cannot be compared with the capital cost of coal-based plants which could be 20 to 50 percent higher depending upon the type of coal used and also whether it is a combined cycle coal-based plant or not.

In fact the high capital cost wiped out the main advantage that the Dabhol power was supposed to bring. Because gas based technology was to be used, the capital cost of the Project should have been much cheaper than a coal based plant, whereas the running cost would have been higher. In the instant case we have lost the advantage of a lower capital cost from a gas based plant while still retaining the disadvantages of a higher running cost.

The Committee also had an opportunity to see the capital cost figures of projects implemented by Enron in other countries. It is clear that this is the costliest project being implemented by this company. The Committee noted that in one case at least, the difference in price was as high as 50 percent.

The 26th report of the Standing Committee on Energy (10th Lok Sabha) entitled "New Policy Initiatives in the Power Sector—Status of Their Implementation and Their Impact on the Economy" presented on 31.05.95, has also noticed that the cost of the Project was high as compared to the other gas-based projects and as compared to the cost of BHEL [Bharat Heavy Electricals Limited] turnkey offers. The report says:

There are four gas-based and three coal based power projects in the private sector cleared by CEA so far. Out of the four gas-based projects, the per megawatt (MW) cost in respect of three projects (Jagrupadu, Godavari, and Puguthan) was between Rs. 3.52 crores and Rs. 3.74 crores while for Dabhol, the cost per MW was Rs. 4.19 crores. Of the three coal-based projects, the cost per MW of Vishakapatnam project at Rs. 5.82 crores is considerably higher than the Ib Valley at Rs. 4.82 crores and Mangalore project at Rs. 5.08 crores. BHEL in this connection has pointed out that turnkey costs in respect of projects with BHEL equipment could cost only around Rs.

3.6 crores to 4.3 crores per MW after making suitable adjustments for development cost, inflation and interest during construction. The cost per MW of power projects in general and Dabhol and Vishakapatnam projects in particular appear to be much higher than that indicated by BHEL. The Committee feel that guaranteed rate of return are tempting the investors to inflate their cost to ensure better returns.

According to experts, lack of competitive bidding has led to significant padding in the investment cost. The Committee desires that the Government should ensure that cost of private power projects should be so determined as it conforms to the simple tariff structure recommended in the preceding paragraph. Efforts should also be made to dispel doubts with regard to reasonableness of the cost of power projects.

The concluding remark—that effort should be made to dispel the doubts—is very important. In fact, the Standing Committee [Parliamentary Standing Committee on Energy] has mentioned on page 151 that the private investors appear to have a tendency to inflate costs which would finally lead to higher unit tariffs where the tariff structure is based on the cost-plus approach. In a project like this where escalations have been built in and a guaranteed 90 percent offtake of power is assured, the incentive to inflate costs could well be imagined.

3.5 Whether any unusual or undue concessions were given for the Project:

The Sub-Committee noted that in view of the assured returns to the Project, good profits are virtually guaranteed. This being so, the value of DPC shares] is likely to rise very rapidly. It will be quite easy for DPC to offer these shares at a very high premium to the Indian public. A good deal of this premium is due to the assured return guaranteed by the Government and to what can at best

be described as a one-sided agreement. If elementary precautions to safeguard the interest of the State had been taken while negotiating the PPA, a clause could have been definitely inserted to the effect that the DPC would give Government of Maharashtra/MSEB the first option to purchase at par any share that they wish to offer in the Indian market. On the contrary, the clause regarding definition in the PPA clearly defines “change in ownership” in such a manner as to allow purchase of shares for a consideration payable in rupees out of the proceeds of the sale of a foreign currency which will enable foreign financial institutions and NRIs [Non-resident Indians] to buy shares without MSEB’s consent.

The Sub-Committee has noted that a very high IRR [rate-of-return] of 25 percent has been conceded to this Project. Such a high rate of return is justifiable in cases where a scheme of incentives can help push up the PLF, as in coal plants. Coal plants normally operate at a lower PLF and a scheme of incentives based on a sliding scale of PLF can help to act as an incentive to the operator. However, in gas-based plants, as

the technology itself is such that it normally operates at a PLF which is in the range of 90 percent, a higher IRR does not serve the purpose of an incentive for the operator to achieve a higher PLF. The Sub-Committee feels that the high IRR has not achieved the purpose of raising the PLF, but has only further bloated the profitability of DPC.

The above are some of the unusual features noticed by the Sub-Committee. Certain other unusual features have also been mentioned under the other issues examined in the report.

3.6 Whether the rate of purchase of power is unreasonable:

An impression has been created in the public mind that in 1997, Dabhol Power will cost only Rs. 2.40 per unit. Even if MSEB purchases power at Rs. 2.40, line losses, distribution costs, and other overheads will have to be added to this cost. The Sub-Committee estimates that the final cost to the consumers of Dabhol Power will be considerable higher.

The most amazing aspect of the entire Project is the fact that the tariff for power has been denominated in U.S. dollars. This means that, regardless of the fluctuations in the dollar-rupee exchange rate, the Project will always earn the same amount. In other words, they are permanently insulated from the vagaries of exchange-rate fluctuations. The Sub-Committee can see no reason whatsoever for this. Foreign direct investment (FDI) comes into this country in several different sectors. There is no restriction on the repatriation of profits legitimately earned by such investments. In no other case, however, is the entrepreneur protected against fluctuations in the international currency market. The Committee fails to see any reason why such preferential treatment should have been given to the power sector and to the DPC.

These unusual concessions makes the calculation of the exact amount that will be paid to MSEB to DPC virtually impossible. As it is the rate for power will depend on the cost of fuel, the contract and price of which is still indeterminate and has yet to be tied up. In addition, the price will

be affected by variations in the exchange rate. The entire exercise puts an impossible burden on the MSEB, and, therefore, on the consumers in Maharashtra. If the cost of the fuel and the rupee-dollar exchange rate rise (and there is no reason to suppose they will not) the effect will be to reduce and eliminate the competitive edge that Maharashtra now enjoys in the country.

The Sub-Committee also would like to point out that the popular impression that Dabhol Power will cost the consumers only Rs. 2.40 per unit is wrong for other reasons as well. Calculation shows that the raw cost of power at best bar is only 54 percent of the total cost to the consumer. The remaining 46 percent is accounted for by overheads, interest, depreciation and return on capital employed. Thus, to the figure of Rs. 2.40 per unit, we will have to add a further 46

percent in order to arrive at the price to be paid by the consumer. This is not all. In order to evacuate the power from Dabhol, MSEB will have to put up high tension lines at a capital cost of about Rs. 370 crores. The interest on the capital cost of these high tension lines to be provided by MSEB for evacuating the power from Dabhol will have to be added to the cost.

MSEB will also have to pay DPC for power supply within twenty-five days. The Committee notes that MSEB today has receivables of nearly 130 days. This means that while MSEB itself will not be able to collect its dues before four months, they will be paying DPC in less than one month. The working capital cost for MSEB will, therefore, rise considerably as a result. When all these things are taken into account, there is little doubt that instead of a figure of Rs. 2.40 per unit, the consumer will have to pay close to Rs. 3.50 per unit for Dabhol Power. In view of the above, the Sub-Committee concludes that the determination of tariff for power in U.S. dollars is a very unusual feature of the agreement and other features mentioned above, the consumer will have to pay a higher price for power than is justified.

3.7 Whether there will be any adverse impact on the environment in the Konkan area because of the Project:

The issue regarding environment got bogged down to whether LNG is an environment-friendly fuel or not as compared to coal. On this comparison—and this the only fuel (coal) which was compared with LNG and in no other respect as in every other respect coal had techno-commercial superiority in India—an impression was assiduously created that LNG, being an environment-friendly material, the environmental considerations are satisfied. The issue is not whether coal or gas is more environment-friendly. If the arguments used for Dabhol were considered as final, coal could never compete with LNG. So the environmental issue which was almost reduced to Coal vs. LNG argument, has not been properly appreciated.

The real environmental issue involved in the Dabhol Project is whether, environmentally, the location of Dabhol, which is in the Konkan (virtually the unpolluted part of Maharashtra) is proper or should the location have been elsewhere where industries have already been established or any other place which cannot boast of the green effects of the Konkan. Therefore, the real

environment issue was sidelined and all environmental analysis focused on the effect of the Dabhol Plant with LNG as fuel on the area around the plant and on the sea and on vegetation.

The Sub-Committee feels that even if Dabhol was to have been selected as a site for this project, the negotiating team should not have put certain conditions for counter-balancing the detrimental effects that this project would have had on the environment of the Konkan. The primary occupation of the

people of this area is fishing and the villagers of this area have expressed their fears before the Sub-Committee, during its visit to the Project site, that the fish catch is likely to diminish. The Sub-Committee feels that the ultimate test of this being environment-friendly would be that the capacity of the environment to support the people should not be reduced.

If the above had been kept in mind, it should have been made mandatory for the DPC to take such measures as would enhance marine life so that the livelihood of fishermen is not affected. Further conditions should have been imposed to enhance the green cover and preserve the biodiversity of the area.

3.8 How far the project is useful for the development of the State:

There can be no doubt that the availability of reasonably priced, efficient and reliable power supply is an essential concomitant to industrial development. It would not be possible for Maharashtra to retain its premier position as the leading industrial State in the country if there is any shortage of power or if the power supply available in the State is not reliable. Having said this, however, it must be noted that there is a point at which the cost of power becomes a factor that must be considered along with availability and reliability. It is clear, from the discussion in the forgoing chapters, that this is the case in respect of the power from DPC.

We have already pointed out that because of the indeterminate nature of the price of gas, the cost of power per unit will vary widely. This situation will be aggravated because the capacity charge as well as the fuel charge have been denominated in U.S. dollars. As a result, more than 98 percent of the costs of power from this project will be subject to fluctuations on the international currency market. The extent to which estimates of the cost of power will vary on this account is difficult to estimate. It is clear, however, that the cost of such power will be far more than the State can afford to pay. The Sub-Committee is convinced that there are other and better alternatives that have not been critically examined.

There is yet another dimension to the high cost of Enron power that must be carefully considered. Since MSEB has underwritten capacity to the extent of 90 percent, it means that they are under obligation to consume this power at all times. At night, therefore, when demand falls, MSEB will be forced to back down its less costly power in order to consume the high cost of power of DPC. The effect of this on the working of the Board can readily be imagined. The problem seems to be that MSEB has failed to distinguish between its peak-load requirements and its base-load requirements and plan accordingly. The result is that high-cost power will be given precedence over low cost power in the grid, and this is clearly not in the best interest of the State.

CHAPTER IV

FINDINGS AND RECOMMENDATIONS

On the basis of the above recital of facts and circumstances and on the evidence that has surfaced at the time of the Review, the Sub-Committee's findings and recommendations are as under:

1. On the question of competitive bids:

The previous Government has committed a grave impropriety by resorting to private negotiations on a one on one basis with Enron and under circumstances which made the Enron/MSEB arrangement on Dabhol to lack transparency. Although there was no policy formulated for competitive bidding in power projects this has been accepted practice, in the larger public interest, to involve more than one contender. There was no compelling reason not to involve a second contender for Dabhol. Actually, such a thought does not seem to have occurred to anyone at all. Therefore the Sub-Committee strongly disapproves of the one to one negotiations with Enron and is clearly of the view that it violates standard and well-tested norms of propriety for public organisations.

2. On whether there was any secret or off the record negotiations:

Considering the records available with the State Government and the MSEB, we are led to the irresistible conclusion that they are not the only guide to what actually happened. It is reasonably clear that several unseen factors and forces seem to have worked to get Enron what it wanted.

3. On whether the capital cost of the Project is reasonable:

On the basis of the material accessed by the Sub-Committee, it concludes that the capital cost of the DPC project was inflated.

4. On whether undue favours and concessions have been given for the Project:

Several unusual features of the negotiations and final agreement have been pointed out by the Sub Committee in the report which makes it clear that whatever Enron wanted was granted without demur.

5. Whether the rate for power from the Dabhol plant is reasonable:

The Sub-Committee is of the view that because of the denomination of tariff for power in U.S. dollars and other reasons, the consumer will have to pay a much higher price for power than is justified. This is clearly not reasonable.

6. On the environmental aspects of the Project:

The Sub-Committee is of the view that the real environmental issue is whether such a huge power project should be located in such an unpolluted part of Maharashtra and whether there

is any other part of the State where it could have been located. Also whether a project of lesser size could help the preservation of the environment better was not gone into. It is evident from the environmental assessment that marine life and plants may have to face problems if adequate care is not taken.

7. On whether the Project is useful to the State:

The Sub-Committee is of the view that such high cost power as Enron envisages will, in the immediate future, and in the long run, adversely affect Maharashtra and the rapid industrialization of the State and its competitiveness.

CONCLUSION

The Sub-Committee, having examined the issues and having listed the deficiencies as above, is unanimously of the view that the arrangement in force is not tenable because of the infirmities pointed out above in the terms and conditions of the contract. It, therefore, recommends that Phase II of the Project should be canceled and Phase I should be repudiated.

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Sudhir Joshi Gopinath Munde Liladhar Dake

Minister for Revenue Deputy Chief Minister Minister for Industries

& Member & Chairman & Member
