Andhra Pradesh Power Sector Reforms

-Treatment of Unfunded Terminal Benefits-
Agenda

• Reforms action
• Liability quantification
• Trust formation
• Settlement process
• Funding by APGenco
Reforms - Bifurcation of APSEB

• In the reforms process, the Andhra Pradesh State Electricity Board was bifurcated into Six entities
  • One Generation Company (APGENCO),
  • One Transmission Company (APTRANSCO)
  • Four Distribution Companies (APDISCOMS)

• As on unbundling (1.2.99), strength of
  – Employees ~53,000
  – Pensioners ~18000
Actuarial Valuation - Need

• State Electricity Boards had under provision for employee terminal benefits

• Terminal benefits – a ‘defined benefits’ plan for employees based on certain calculations including the last drawn salary:
  – Pension, payable monthly for life and continued thereafter as ‘family pension’ for the spouse till spouse’s death
  – Gratuity paid on retirement
  – Unutilised Leave Encashment, at the time of retirement (introduced subsequent to the unbundling)
Actuarial Methodology

• Methodology covers parameters such as
  – Mortality, Staff turnover rates, disability rates, Salary growth (both for inflation and promotions) and the interest regime

• Projections are made using principles of probability and time value of money

• Liability quantification, as of transfer scheme date (1.2.99) for
  – Existing pensioners
  – Past service of existing employees
  – Contribution required for benefits expected to accrue in future
Overview of Liability identified

- In the reforms process of power sector in Andhra Pradesh, the pension & gratuity liability of erstwhile APSEB employees as on 31.1.99 was valued at Rs.4386.95 Crs after auctorial valuation:

| Pension Liability for Retired employees | 1320.43 |
| Pension Liability for Employees in Service | 2811.97 |
| Gratuity Liability for Employees in service | 254.55 |
Continued…

• The liability was vested in the APGENCO through a statutory transfer scheme vide Government Order No.11 dt. 30.1.2000.

• The following are the reasons for incorporation of the liability in the APGENCO books:

  i) APGENCO is not a licensee and will not come under regulatory purview. Hence the commitment on the liability will be allowed as pass-through item in the Generation Tariff

  ii) APGENCO has 5600 MW installed capacity at the time of bifurcation.
Formation of Trusts

• APGENCO has recognized the liability and paid entire commitment on pension liability up to 31.3.2002 in the form of interest against liability.

• To discharge the Pension liability Seven trusts are formed during June,2001.

• MASTER TRUST - to discharge the Pension & Gratuity liability of employees for the service rendered in APSEB.

• Pension & Gratuity Trusts for each company (6 Nos) – to discharge the Pension liability of employees for the service rendered in the company.
Responsibility between Trusts

• The liability in respect of employees retired prior to 1.2.99 is being born by Master Trust.

• The liability in respect of employees retired after 1.2.99 is being shared by Master Trust and P&G Trusts of individual company in the ratio of 74:26 based on the man days worked in the APSEB and served in companies.
MASTER TRUST

• The Master Trust is managed by a Chairman and 7 Trustees.
  – Chairman -- Principal Secretary (Energy) to GOAP.
  – Trustee -- Finance Secretary, GOAP
  – Trustees -- CMD’s of Four Discoms
  – Trustees -- Director( Finance), APTransco
  – Trustee & Convener -  D.F., APGENCO.
Process of Settlement

• APGENCO acknowledged the liability and issued bonds to the Master Trust

• APGENCO will repay the liability in installments.

• Till the repayment of liability, APGENCO will pay interest at floating rate duly matching with actual commitment to Master Trust.

• The repayment of Principal & Interest on these bonds have been guaranteed by Government of Andhra Pradesh Vide G.O.Ms. No.57 dt.7.5.2002.
Structure of Bonds

• There are two bonds:
  1. For the retired employees – Rs.1320.43 Cr
  2. For the service employees- Rs.3066.52 Cr

Bond – I:
(a) Repayment – In 31 years in installments
(b) Scheduled interest – Estimated commitment as per Bond – Principal repayment.
   Additional interest - Actual commitment – (a+b).

Bond – II:
(a) Repayment – In 27 years in installments
(b) Scheduled interest – Estimated commitment as per Bond – Principal repayment.
   Additional interest - Actual commitment – (a+b).
Working methodology

• Master Trust is using the services of unit offices of six companies for the pension disbursement

• Unit offices will send indent for funds requirement to Master Trust by 20\textsuperscript{th} every month.

• Master trust will send indent for funds to APGENCO for the consolidated amount of unit offices requirement by 22\textsuperscript{nd} every month.

• Indent covers 100% commitment against employees retired before 1.2.99.

• 74% commitment against employees retired after 1.2.99.
Working methodology…

- APGENCO will transfer funds to Master Trust and Master Trust in turn will transfer the funds to unit offices to enable pension disbursement on 1st of every month.

- 26% commitment against employees retired after 1.2.99 will be met by respective company trusts. Funds will be transferred by respective company trusts to unit offices.

- The system is working smoothly and there is not even 1 day delay or default in last 8 years.
APGENCO’s Management of Funds

• APGENCO is meeting the principal repayment from the depreciation earned due to valuation of assets by GOAP on replacement method in statutory transfer scheme

• Schedule interest is being met from the return earned on Equity (increased due to higher valuation of assets)

• Regulator has allowed APGENCO to claim additional interest outflow (if any) directly as a part of Generation Tariff.
Pension & Gratuity Trusts

- P&G Trusts are cash funded

- Companies are transferring the funds to the trusts as per actuarial valuation duly charging the expenditure to O&M cost.

- After meeting the commitment of 26%, the balance funds are being invested as per mandatory norms.

- The trusts are being managed by the respective companies.
Critical issues

• 100% pension liability of employees retired before 1.2.99 rests with the Master Trust. The bond expires by 2033. There is a possibility of few pensioners or family pensioners alive by 2033. This necessitates rescheduling the bond by reviewing the situation before expiry of the bond.
Critical Issues..

- 100% pension liability of employees retiring after 1.2.99 will be with the respective company trusts after 2029.

- This necessitates contribution of more funds by six companies to P&G trusts than the present requirement of the trusts.

- At the time of issue of bonds escalation in pension was estimated @ 4% every year and 8% during the pay revision. The gratuity commitment is Rs.2,50,000.

- At present the actual yearly escalation is double the estimation and 3 to 4 times during pay revision. As a result the commitment has increased by 60% over the estimation.

- The issue is addressed by pass through in tariff, accepted in the Regulatory principles set out by the Commission.
### Quantification of deviation

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<th>Year</th>
<th>Estimated</th>
<th>Actual</th>
<th>% Deviation</th>
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<tr>
<td>2002-03</td>
<td>216.60</td>
<td>253.70</td>
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<td>2003-04</td>
<td>242.70</td>
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<td>328.87</td>
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<td>2007-08</td>
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<td>467.58</td>
<td>54%</td>
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<td>2008-09</td>
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<td>2009-10</td>
<td>303.00</td>
<td>499.19</td>
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<tr>
<td><strong>Cumulative deviation</strong></td>
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<td><strong>5%</strong></td>
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Other issues

• The liability towards General provident fund of erstwhile APSEB employees was Rs.230.12 Crs and APGENCO has issued six bonds totaling 230.12 Crs to Six GPF trusts of the companies. The bonds will be mature in 2013. Till maturity interest will be paid equitant to PF rates.

• For the leave encashment, the liability was not recognized at the time of bifurcation and the companies have recognized the liability in their books after option process of employees.

• The employees joined in companies after 1.2.99 are not covered under pension scheme and moved to EPF system.
THANK YOU