

**CENTRAL ELECTRICITY REGULATORY COMMISSION
NEW DELHI**

Coram:

1. Dr. Pramod Deo, Chairperson
2. Shri Bhanu Bhushan, Member
3. Shri R Krishnamoorthy, Member
4. Shri S Jayaraman, Member

Petition No. 21 / 2008

In the matter of

Application for grant of permission to Power Exchange India Limited for setting up and operating the Power Exchange

And in the matter of

Power Exchange India Limited, Mumbai

....

....

Petitioner

ORDER

The applicant, the Power Exchange India Limited, had made this application in accordance with the guidelines issued vide the Commission's order dated 6.2.2007 in Petition No. 155/2006 (suo-motu) for setting up and operating the Power Exchange (PX). The Commission in its order dated 27.5.2008 accorded approval to the applicant for setting up and operating the PX and also directed the applicant to seek approval for the PX design, bye-laws and rules in accordance with the observations made in the order abid before starting the operation of the PX.

2. The applicant, vide affidavit dated 13.8.2008, has submitted the draft rules, bye-laws and business rules of the Power Exchange India Limited for approval by the Commission. The draft rules primarily deal with the powers of the Board of Directors and the Chief Executive of the PX, membership of the PX, disciplinary matters including penalty, suspension and expulsion of the

members, etc. The draft bye-laws deal with the rights, liabilities and obligations of the members, trading system, procedure and other parameters of trading on the PX, risk management, market surveillance, clearance and settlement of contract, maintenance of records, annual accounts and audit of the PX, settlement funds and dispute resolution. The draft business rules deal with the procedural and operational aspects of the PX in greater details. Therefore, the business rules are treated as part of the bye-laws of the exchange and any reference to the bye-laws in this order includes the reference to the business rules as well.

3. The draft rules and bye-laws of the PX have been examined in the light of the guidelines issued vide our order dated 6.2.2007 in Petition No. 155/2006 (suo-motu) (hereinafter referred to as "the guidelines") and the order dated 27.5.2008. We have given our careful consideration to the draft rules and bye-laws submitted by the applicant, and record our observations thereon in the succeeding paragraphs.

General Observations

4. In para 2 (f) and (g) of the guidelines, the areas to be covered by the rules and bye-laws of the PX were clearly delineated. The draft rules and bye-laws submitted by the applicant broadly cover the areas stated in the guidelines. However, we notice that the draft rules vests ample discretion in the Relevant Authority to decide on procedural and substantive requirements of the PX from time to time. The terms used are "as may be specified", "as may be stipulated" or "as may be prescribed" by the Relevant Authority. However, these terms have not been defined in the definition clause of the rules, and manner of exercise of such powers by the Relevant Authority have not been indicated. Only in the bye-laws, the term "prescribed" has been defined as "specified by Rules, Bye Laws and Business Rules or any circular issued from time to time". In our view, a

single term may be uniformly used in the rules and bye-laws to denote the discretionary powers of the Relevant Authority and the parameters of exercise of such powers should be clearly defined in the Rules.

Rules

5. Para 2 (g) of the guidelines provides that the rules should particularly include the following, namely:

- (a) the governing body of the PX, its constitution and powers;
- (b) management of the PX and the manner of transaction of its business;
- (c) powers and duties of the office-bearers of the PX;
- (d) members - their admission, qualifications, expulsion, suspension and re-admission;
- (e) procedure for registration of members, and nomination and registration of authorized representatives of members.

6. The constitution of the Board of Directors (the Board) has been provided in the Articles of Association of the applicant company. Rule 3 of the draft rules deals with the power and functions of the Board and also the Relevant Authority for the purpose of the rules and bye-laws. The Board has been empowered to make rules, bye-laws, business rules and code of conduct, and amendment or repeal thereof; to issue circulars for all or any matter relating to conduct of business on the PX; organization, management, operation and control of day-to-day management of the PX, delegation of powers to the managing director, constitution of committees and issue of directives etc. Rule 3.9 accords over-riding effect to the decisions of the Board over all matters concerning functioning, regulation, business, membership and day-to-day management of the PX. This

renders the rules and bye-laws redundant and defeats the purpose of their approval by the Commission. The relevant provisions need to be omitted. In case of any ambiguity in the rules or bye-laws, the matter should be clarified through proper amendment. .

7. Rule 4 of the draft rules provides that the Managing Director of the PX shall be its Chief Executive and shall be the Relevant Authority for its day-to-day management and affairs including trading, clearing and settlement of contracts on the exchange and any other power as may be delegated by the Board. The manner of appointment and tenure of the Managing Director of the PX has been provided in the Articles of Association of the applicant and the requirements of the guidelines are complied with.

8. As per Para 6.2 (g) of the guidelines issued vide order dated 6.2.2007 *ibid*, the PX is required to make provisions for the powers and duties of its office bearers in the rules. It is noticed that the powers and duties of the office bearers have not been specifically defined. This requirement shall be complied with by making suitable provisions in the rules.

9. On perusal of the draft rules, we further notice that there is no provision for segregating ownership, day-to-day management/operations, and participation in trading. In order to ensuring ring-fencing between day-to-day operations and participation in trading, and to bolster and preserve confidence of the trading participants on the PX, we direct that the following provisions be suitably incorporated in the rules:

“The Managing Director, the Chief Executive Officer, any Director in-charge of day-to-day operations, any employee, any consultant or any advisor of the power exchange shall not be directly or indirectly associated with any trading member or client or participant of the power exchange or with a holding or subsidiary company thereof.”

10. Rule 5 of the draft rules deals with the membership of the PX, eligibility for membership, admission of members, termination of membership and readmission of membership. Categories of members have been suitably defined in the bye-laws and the business rules. We however notice that any individual above the age of 21 years has been made eligible for membership of the PX. In our view, individual membership of the PX should be open to the Indian nationals only and accordingly, the applicant should include suitable clause in the rules that an individual seeking membership must be a citizen of India. Sub-rule 5.4 of the draft rules provides that "members may also have to comply with any other registration as may be required under law, including with competent regulatory authority like CERC or any such other authority as may be required from time to time". Since the Commission does not require the members of the exchange to be registered with it, reference to "CERC" in the said sub-rule may be deleted. Subject to our observations as noted in this paragraph, the provisions regarding members of the exchange appear to meet the requirements of the guidelines.

Bye-laws

11. Para 2(h) of the guidelines provides that the bye-laws of the PX will broadly cover the following areas:

- (a) trading system including operational parameters for trading;
- (b) rights and liabilities of the trading members;
- (c) market surveillance and investigations;
- (d) clearing and settlement procedure;
- (e) risk management;
- (f) provision for payment security mechanism

- (g) maintenance of records and accounts;
- (h) Preparation of annual accounts and audit thereof;
- (i) Arbitration, dispute resolution and conciliation;
- (j) Mechanism for determination of transaction charges ; and
- (k) Mechanism for redressal of grievances.

12. The bye-laws broadly covers the areas specified in the guidelines. Clause 5.3 of the bye-laws provides for trading days and sub-clause 5.3.2 vests full discretion on the Relevant Authority to declare a working day as closed holiday or vice versa. In our view, the PX should be open for trading on all working days of the year and any alteration in the pre-decided holidays should be done after following a prescribed procedure. Accordingly, the following provisions may be substituted in place of sub-clause 5.3.2:

"5.3.2 – In exceptional circumstances and for reasons to be recorded in writing, the exchange may at any time:

- (a) alter or cancel any of the Exchange holidays fixed under these Bye-laws, the Rules and Business Rules;
- (b) keep the Automated Trading System (ATS) or any other trading system of the Exchange available for trading on any day notwithstanding that such day had earlier been declared as an exchange holiday;
- (c) close trading in any one or all Contracts on the ATS or any other trading system of the Exchange for one day:

Provided that the Exchange may, for the reasons to be recorded in writing, close the trading in any one or more or all Contracts on the ATS or any other trading system of the Exchange for a period not exceeding three trading days without the approval of the Commission."

13. Clause 5.12.2 of the bye-laws empowers the PX to modify or change the matching algorithm relevant to any market or order books any time where it is necessary to do so either in the opinion of the exchange or as prescribed under the relevant regulations. We make it clear that prior consideration and approval of the Commission is necessary for introducing such changes and

accordingly, the applicant is directed to insert the words "Subject to the approval of the Commission" at the beginning of the said clause.

14. The applicant in the draft bye-laws (business rules) has sought to indemnify itself against any events of force majeure. In order to indemnify the National Load Despatch Centre, the Regional Load Despatch Centre and the State Load Despatch Centre, we direct that the bye-laws should provide that the power exchange including its buyers and sellers, shall keep each of the National Load Despatch Centre, Regional Load Despatch Centres and State Load Despatch Centres indemnified at all times and shall undertake to indemnify, defend and save the National Load Despatch Centre, Regional Load Despatch Centres and State Load Despatch Centres against any claim for damages, losses, and actions, including those relating to injury to or death of any person or damage to property of any person, demands, suits, recoveries, costs and expenses, attorney fees, against the third parties, arising out of or resulting from or attributable to the transactions at the PX. The bye-laws should also provide that the PX, including its buyers and sellers, shall keep each of the National Load Despatch Centre, Regional Load Despatch Centres and State Load Despatch Centres indemnified at all times and shall undertake to indemnify, defend and save the National Load Despatch Centre, Regional Load Despatch Centres and State Load Despatch Centres harmless from any and all damages, losses, claims and actions arising out of disputes among buyers and sellers, as well as with power exchange inclusive of confidentiality issues. The bye-laws should further provide that the clearance/curtailment advice issued by National Load Despatch Centre to the power exchange at 1400 hrs shall be on good faith basis. It shall be further provided in the bye-laws that the clearance/curtailment advice by the National Load Despatch Centre shall not be binding and Central Transmission Utility, National Load Despatch Centre, Regional Load Despatch Centres and State Load Despatch Centres shall not have any

financial liability on account of inability, for any reason whatsoever, to achieve the complete matching between the advice of National Load Despatch Centre issued at 1400 hrs and the final schedules issued at 1800 hours.

15. A provision should necessarily be made in the bye-laws that any entity or the principal or subsidiary or sister concern of an entity defaulting in payment of the transmission charges, UI charges, and the fees and charges for the National Load Despatch Centre, Regional Load Despatch Centres and ULD&C schemes may be barred by the Commission from selling through the PX.

16. The bye-laws (business rules) do not provide for checking of bid quantity through the PX software with respect to the standing clearance given by the State Load Despatch Centres. A suitable provision for validation of bid quantity either through software or manually before finding the price solution shall be incorporated.

17. The MW quantum in a buy bid of or on behalf of an entity (including a distribution utility) shall not exceed the maximum deficit that the entity can have, i.e. maximum consumer load minus minimum generation. Similarly, the MW quantum in a sale bid of or on behalf of an entity (including a distribution utility) shall not exceed the maximum possible surplus of the entity, i.e. maximum generation minus estimated consumer load. For this purpose, 'generation' shall include entitlements under power purchase agreements entered into for catering to consumer demand in entity's system. This shall be stipulated in the bye-laws.

18. In terms of the Commission's guidelines, the bye-laws are to *inter alia* cover the mechanism for market surveillance and investigation. This requirement has been complied with.

However, it shall be made clear in the bye-laws that the Commission shall have a right to carry out checks at any time to ensure that the surveillance mechanism at the power exchange is in effective operation and can pass appropriate orders.

19. In clause 8.1.11 of the bye-laws, it has been provided that "the settlement responsibility shall rest wholly and solely upon the counter parties to the contract and/or the concerned Members as the case may be; and the Exchange shall act as the common agent of the Members for receiving and paying funds, without incurring any liability or obligation as a principal." In our view the clearing house and the PX cannot absolve itself of the responsibility if the lapse is attributable to them or malfunctioning of their equipment or software. The provisions of clause 8.1.11 of the bye-laws may be modified as under:

" 8.1.11. The clearing house should act as a legal central counter party for all transactions in the contracts admitted on the exchange:

Provided that if the Exchange or Clearing House on an investigation concludes that either all or part of transactions in any contract are found to have been executed on the ATS in a fraudulent manner and / or are done as financial transactions with intention to defraud the Settlement Guarantee Fund, the Clearing House shall have discretion to withdraw itself as a legal central counter party to such transaction at any time:

Provided further that if the Clearing House decides to exercise its discretion to withdraw itself as a legal central counter party to the transactions, either in full or in part, and/or either from both sides or single side of the transaction, it shall afford an opportunity of being heard to all the parties affected or likely to be affected and the decision taken by the Clearing House shall be final and binding on all the parties concerned, including the Clients."

20. Clause 9 of the bye-laws deals with the records, annual accounts and audit of the PX and its members. We notice that the bye-laws do not provide for regulatory supervision of the records and accounts of the PX which in our considered view are required to ensure transparency in

operation and accountability of the PX. Accordingly, we direct that the following may be suitably added in the bye-laws:

“ The Exchange shall submit to the Commission copies of the accounting statements and auditor’s report not later than six months after the close of the year to which they relate. Any person authorized by the Commission shall be entitled to inspect and verify the accounts of the power exchange and its members, if considered necessary and the power exchange shall be bound to render necessary assistance to such person.”

21. Clause 10 of the bye-laws deals with the settlement funds which contains detailed provisions with regard to the members’ contribution to and utilization of the funds. The liability of the PX is limited to the extent of contributions of a member available in the funds. The following provision may be added as bye-law 10.7, namely:

“10.7. Settlement of UI dues: Any shortage or excess delivery of electricity from the total schedule including schedule for contracts traded on exchange by the grid connected entity shall be settled by such entity under UI mechanism as per the procedure laid down by the Commission or any other applicable settlement system as may be prescribed by the State Commissions.”

22. In page 49 of the business rules, the terms “constituents” and “member” have been defined under the heading ‘Notes’. These terms should be defined in the definition clause of the rules for the purpose of clarity and convenience of reference. We further notice that the term “member’ has been defined to “mean and include a member who has been admitted as such by PXI and who holds a registration certificate as a stock broker from CERC.” Since no registration with the Commission is required for the purpose of enrolment as a member with the PX, the sentence “ who holds a registration certificate as a stock broker from CERC” may be deleted.

General

23. In the preamble of the rules and the bye-laws, it shall be provided that any amendments in the rules and bye-laws approved shall be made only with the prior approval of the Commission and

also that the Commission reserves its right to specify any condition or to modify any of the present stipulation, in the light of the experience gained and to meet the needs of the future.

24. The PX shall comply with the instructions of the National Load Despatch Centre, Regional Load Despatch Centre and State Load Despatch Centre in respect of all matters related to coordination and interface with the system operator. In the event of any difference of opinion between the National Load Despatch Centre and the PX, the dispute shall be referred to the Commission for its decision. However, pending decision by the Commission the directions of the National Load Despatch Centre shall be complied with.

25. As the common platform for power trading is a new initiative, the PX shall have interaction with the National Load Despatch Centre on regular basis, and at least every month during the first six months to iron out coordination issues, if any. The results of such interaction shall be communicated to the Commission on monthly basis.

26. The entire country shall be configured into suitable bid areas or zones in accordance with the instructions of the National Load Despatch Centre issued from time to time to ensure that in the event of transmission constraint, it is possible to restrict power flows as per the requirement of the National Load Despatch Centre and appropriate price solution can be found through market splitting mechanism. The timelines of the PX shall be aligned with the timelines specified by the Central Transmission Utility in the Procedure for Scheduling of Collective Transactions.

27. The PX shall be responsible for payment of transmission charges, scheduling and system operation charges to NLDC, SLDCs, State Transmission Utilities as per the regulations specified

by the Central Commission and State Commissions. In the event of default in payments by a member, the PX while utilizing the margin money of such member from the Settlement Guarantee Fund for the purpose of settlement of dues shall give precedence to the payment of transmission charges, scheduling and system operation charges. Suitable provisions to that effect should be made in the rules/bye-laws of the PX.

28. The applicant shall submit the following information/reports to the Commission:
- (a) Information of total bid/ traded quantities and market clearing prices on monthly basis for each hour of the day;
 - (b) A complete list of the trading members of the PX and clients registered along with their complete addresses and the names of the contact person, to be updated every month;
 - (c) Details of the Managing Director, Chief Executive Officer, Director in-charge of day-to-day operations of the PX, Manager, officers and staff posted, every six months along with their individual responsibilities and self-certification by these persons of compliance of the direction given in para 9 of this order, with proper endorsement by the applicant; the first report to be submitted by 31.12.2008;
 - (d) An updated list of the Board of Directors and Members of the Committees constituted;
 - (e) Copies of resolutions of the Board of the PX and any other authority, having bearing on the matters covered in the rules and bye-laws, within 10 days of passing of such resolutions; and
 - (f) Copies of Annual Report, together with the Accounting Statements and Auditor's Report by 30th September each year, for the period ending 31st March.

29. The rules and bye-laws approved by us are applicable to contracts (products) of day-ahead trading. In case the applicant intends to start any other type of contract it shall do so only after obtaining prior approval of the Commission. We also note that the term "contract" used by the applicant is likely to be confused with contract used in the sense of agreement enforceable in law. We prefer that the term is replaced by the term "product" or any other appropriate term, to avoid confusion.

30. In accordance with "in principle" approval granted vide order dated 27.5.2008, the PX shall start as a platform for scheduled, day-ahead trading of electricity. All trades cleared by the PX, within the available transfer capacity as advised by the National Load Despatch Centre, shall be compulsorily submitted for scheduling. There shall be no fictional trading in the PX. The day-ahead trading for hourly contracts shall be based on voluntary simultaneous participation by buyers and sellers on a nation-wide electronic platform.

31. Under the business rules, the applicant has not specified fees and charges such as admission fee, membership and application processing fee, annual membership subscription fee, security deposits, annual client fee, transaction fee, professional charges and the like. However, the applicant has mentioned in page 6 (para 4) of the business rules that "such fees, security deposit, contribution and other money as are specified by the Relevant Authority would be payable on or before admission as Member and for continued appointment thereof." The representative of the applicant has clarified to the staff of the Commission that the fee structure as specified by the Relevant Authority has been posted on its website and has submitted a copy of the same (not on affidavit). . It is clarified that the Commission have not gone into the basis of the fees and charges.

Therefore the question of fees and charges leviable by the PX should be the concern of the persons desirous of becoming member of the PX.

32. We wish to make it clear that notwithstanding the approval of the rules and bye-laws by the Commission, the persons enrolling themselves as members or clients of the PX or transacting trade on the PX in any other capacity shall do so after satisfying themselves of all the commercial aspects covered under the rules and the bye-laws, uninfluenced by the fact that the Commission has approved them since these are the matters exclusively between the parties. The observation in this para shall be notified by the PX to its existing members as also to the persons seeking enrolment as member or client in future.

33. The front cover page of the rules and the bye-laws shall contain the following in bold letters of font size not less than 12:

"These rules and the bye-laws, including the business rules have been approved by the Central Electricity Regulatory Commission. However, as observed by the Commission, notwithstanding the approval of the rules and bye-laws by the Commission, the persons enrolling themselves as members or clients of the power exchange or transacting trade on the power exchange shall do so after satisfying themselves of all the commercial aspects including the fees and charges leviable under the rules and bye-laws, uninfluenced by the fact that the Commission has approved them since these are the matters exclusively between the parties."

34. Since there will be multiple exchanges, we direct that the PX would take an undertaking from its members that they would limit their concurrent quantity (MW) for purchase and sale from all the exchanges within the quantity permitted by the appropriate Regional Load Despatch Centres or State Load Despatch Centre. As regards congestion management in a multi-exchange scenario, the Commission will issue necessary directions in due course.

35. We also direct the applicant to approach National Load Despatch Centre for testing and mock run of the PX. The National Load Despatch Centre after being satisfied about facilities available at the PX , particularly the data transfer and communication interface, shall give clearance to the applicant to start operation of the PX.

36. The approved rules and bye-laws along with all the orders of the Commission on the subject shall be posted on the home page of the website of the PX.

37. Subject to compliance of above directions, approval is hereby accorded to the rules and bye-laws submitted by the applicant and the applicant is permitted to start operation of the PX from a date to be announced by it in advance.

Sd/-

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{S. JAYARAMAN]
MEMBER

[R KRISHNAMOORTHY]
MEMBER

[BHANU BHUSHAN]
MEMBER

[DR. PRAMOD DEO]
CHAIRPERSON

New Delhi, dated 30th September, 2008