

# Controversy over India's Dabhol power plant deal irks Washington

by Ramtanu Maitra

In a rare public statement of its kind, the Office of the Secretary of the U.S. Department of Energy has warned India that failure to honor the agreements between a subsidiary of the Houston-based Enron Corp. and the state of Maharashtra in setting up a 695 MW power plant at Dabhol in Maharashtra, could jeopardize several, if not all, private power projects in which U.S. companies have shown interest.

Echoing Washington's concerns, British Chancellor of the Exchequer Kenneth Clarke, in an interview with the Indian daily *The Hindu*, in Bangalore at the end of a week-long visit to India, said that the strident controversy over the Dabhol power project might send a negative message to international investors and undermine confidence in India as a place for investment. Rejecting outright consideration of the change in the nature of the contractual status of the parties concerned, Clarke said, "Investors abroad will start doubting the continuity of economic reforms. This will vitiate the climate for long-term investments."

## The 'Enron deal'

The "Enron deal," as it has come to be known in the Indian media, consists of two phases. In the first phase, whose financing was concluded last March, the 695 MW power generation plant at Dabhol, based on imported distillate, will be made operational at the latest by May 1, 1997. In the second phase, plant capacity would be expanded to 2015 MW, making it the largest single power-generating center in India. In the second phase, the plant would be changed over to using imported liquefied natural gas (LNG). The second phase, which is yet to be finalized in negotiations, can be accepted or rejected by the Maharashtra State Electricity Board (MSEB) by July 31, 1995. Conditions include that for any delay in supplying power, Enron will pay \$14,400 per day for the first 180 days and \$100,000 per day thereafter. For any shortfall in the plant's performance capacity, it will pay a one-time charge of \$100 per kilowatt.

Enron also guarantees that the plant will be available 95% of the time. For any shortfall, a penalty will be paid to the MSEB. For its part, MSEB guarantees the purchase of all the power generated, to ensure an 86% plant load factor—a term used to describe the efficiency of the plant. MSEB will still

be paying Enron if it is unable to evacuate this power. The MSEB will pay 7.5¢ per kilowatt-hour (kwh) for this power in 1997, which is almost 60% more than what the MSEB charges its customers as of now. Enron has also been assured a 4% escalation of power tariff thereafter annually. The estimated cost of the project is \$2.8 billion.

The deal began to take shape in 1992, when the government of India invited the Houston-based company to invest in India's growing power sector. The invitation was a corollary to the 1991 announcement by the Narasimha Rao government whereby the private sectors were urged to enter the power sector, which, till then, was almost exclusively a public sector investment area. In March 1992, the government announced a list of incentives—including a 16% rate of return on equity on a 68.5% plant load factor (PLF). And beyond 68.5%, the rate of return on equity increases by a maximum of 0.7% for each 1% increase in the PLF. The government did not find it necessary to link the rate of return to more efficient use of capital; or, in other words, to use it as an incentive to minimize fixed costs.

## Initial optimism

From the very outset, both Bombay and New Delhi had pushed the Dabhol power project with a missionary zeal. In Bombay, Sharad Pawar, then-chief minister of Maharashtra and a powerhouse in the national Congress Party, actively participated in negotiating the agreements on the first phase of the project. Similar zeal was also exhibited by Union Power Minister N.K.P. Salve. The project was cited as an example of the new-found goodwill between India and the United States and was seen by some in India as an unmistakable indicator of the latter's support for India's ongoing economic reforms and liberalization.

There were definite reasons for such optimism. India's growing power crisis was making the country less tempting to investors, and a living hell for a large section of the people who are supposed to be happy about the reforms. The Eighth Five Year Plan (1991-95) was starved of resources. Installed power capacity to be added during the plan has been scaled down from almost 40,000 MW to 20,000 MW. Observers are apprehensive that even the 20,000 MW target, which is

less than the additional power capacity achieved during the Seventh Five Year Plan, will not be met. The austerity measures to reduce the budget deficit—in order to reduce the rate of inflation, to keep the currency stable, to maintain debt payments, etc., a standard formulation adopted by the International Monetary Fund and World Bank and sold relentlessly to most of the hapless Third World policymakers—has cut deep into the power sector outlay earlier proposed in the plan. In such a negative environment, the Enron deal looked like the light at the end of the tunnel.

On the positive side, it must be noted that the power experts in India had long been discussing *sotto voce* setting up a string of gas-fired power plants along India's west coast, where gas is plentiful and demand for power is high. Two of India's most industrially developed states, Maharashtra and Gujarat, are located in this area. In this context, the setting up of the Dabhol power project seemed fitting and proper.

### **Comes trouble**

Despite its worthiness, the project ran into trouble at the very outset. By the time the first phase agreements were completed, nine court cases had been filed against the project. But the real trouble started with the advent of the state assembly elections in March. A few days after the first phase agreements were completed, and Enron managing director Joseph Sutton had left for a few days' vacation, Sharad Pawar and the ruling Congress Party were ousted in the elections and were replaced by the Shiv Sena-Bharatiya Janata Party combine which had campaigned against the project. In fact, Vijay Natu, a BJP candidate from the Dabhol area, won his seat by effectively using anti-Enron views. The new rulers in Bombay attacked the project, claiming that it reeked of financial kickbacks. They also cited the high cost of the project, the lack of transparency, absence of competitive bidding (which, in essence, they claimed contributed to the high cost of the project), and the negotiated high cost of the power tariff. Subsequently, the Shiv Sena-BJP government has set up a cabinet subcommittee to review the project and the confidential clauses of the agreement. The subcommittee will look into various aspects of the project, including its impact on the coastal environment and the possibility of generation of jobs for the local populace.

One of the most important critics of the project is Kirit Parikh, director of the Indira Gandhi Institute of Development Research. Parikh has pointed out through newspaper articles that the high cost of the plant could have been avoided if transparent and competitive bidding had been used to award the project, instead of just inviting Enron to set up the plant. The most relevant issues, Parikh claims, are a) the capital cost of the plant seems 20% too high, and b) the 86% load factor guarantee would require that during the nighttime, off-peak hours, when the demand for electricity is low, the MSEB will have to purchase power from Enron at 2.40 rupees per kwh when MSEB could have

generated power from its own plants at less than 0.60 rupees per kwh.

### **Politics all the way**

Parikh also concludes that this is the bottom line of the Enron deal. However, BJP and other critics do not agree with Parikh on this score and cite alleged kickbacks, which are yet to be proven. BJP, in the same breath, claims that the party is not against multinationals doing business in India, but insists on competitive bidding, which, according to many past experiences, does not ensure lower cost. Moreover, to accuse Enron of grabbing the guaranteed rate of return is grossly unfair, because it was the government of India, ostensibly to give the privatization of the power sector a big and permanent boost, that had offered the lolly to assuage the fears of finicky international bankers.

But the real bottom line is that the deal was political from day one, and it remains so. The so-called nationalists and confused political parties boarded the anti-Enron bandwagon, hoping that this would get them the media spotlight and thus help them in the elections. It is also evident that the BJP, finding it increasingly difficult to balance reality with abstract political activism, is talking from both sides of its mouth. BJP leader L.K. Advani, who is practically controlled by the Jacobins around the party and its front groups, insists that the U.S. Energy Department is trying to intimidate the BJP by issuing threats of cancelling the Dabhol project. He issued a statement on June 6 demanding that Enron be investigated (under provisions in U.S. law) for underhanded dealings to win overseas business, and prosecuted if evidence is found. New Delhi, on the other hand, backed the deal wholeheartedly when Union Commerce Minister P. Chidambaram went on record on June 6 questioning the propriety of the Maharashtra government's review of the Dabhol power plant project.

At the same time, Enron had all along used its political muscle to shape the deal the way it stands today. Besides Pawar and Salve, U.S. Ambassador to India Frank Wisner held Enron's briefs during his talks with Advani. The issue even came up for discussion during U.S. Secretary of Treasury Robert Rubin's visit to India in April. And now the Office of the U.S. Energy Secretary has issued a warning.

New Delhi fears that if the Enron project is scrapped, the Finance Ministry's projection of net foreign investment flow into India, to the tune of \$3-4 billion in the 1995-96 fiscal year, will receive a serious setback. Since the foreign investment into India is more of a trickle, in contrast to the "flood" promised by the Finance Ministry over the last three years, senior government officials have told newsmen that the issue is a matter of serious concern to foreign investors and all foreign trade missions arriving in the country. They point out that even the multinational institutions like the World Bank and the Asian Development Bank have been seeking clarifications. No doubt, Washington's warnings will help to raise the stakes a notch upward.