No.23011/51/2015-CPD
Government of India
Ministry of Coal
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Date:- 04.06.2015

Subject: Public Notice seeking comments on methodology for proposed auction of coal linkages/LoAs to non-regulated sector through competitive bidding.

Government is contemplating to introduce auction of coal linkages/LoAs through competitive bidding as the selection process. Accordingly, an Inter-Ministerial Committee has been constituted in the Ministry of Coal. A draft methodology for proposed auction of Coal Linkages/LoAs to non-regulated sector which covers Cement, Iron & Steel including Sponge Iron, Aluminium, Fertilizer, and Others through competitive bidding has been prepared. An Approach Paper on the draft methodology for the proposed auction has been prepared for public consultation.

The members of the public and stakeholders concerned are requested to submit their comments/views, if any, on the proposed methodology on the email id: slclt.moc@nic.in upto 10.00 A.M. on 11.06.2015.

4.6.15
(Rajesh Sinha)
Joint Secretary to the Govt. of India
011-23384887

Approach Paper for Auction of Coal Linkages

Auction of Coal Linkages/LoAs for non-regulated Sector

Joint Secretary
Ministry of Coal
Government of India

Draft: for public consultation only

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Subject: Proposed auction of coal linkages/LoAs to non-regulated sector through competitive bidding.

1. Coal India Limited (CIL) has been supplying indigenous coal to Regulated, Strategic, and Non-Regulated sectors. Regulated Sector covers non-captive coal based power generation units. Strategic Sectors are Rail and Defence. Non-Regulated Sectors cover Cement, Steel, Captive Power and Others. About 90% of the supplies are made through long-term Fuel Supply Agreements (FSAs) with end-users and the rest through electronic auctions (e-auctions).

2. Hon'ble Supreme Court of India vide its judgements in August and September, 2014, had declared 204 coal mines/blocks allocated to the various Government and Private Companies since 1993 as illegal on the grounds that the procedure followed was arbitrary and no objective criterion was used to determine the selection of companies. Pursuant to this judgment, e-auction of Schedule II and Schedule III Coal Mines was conducted. It is logical to interpret that the same philosophy of non-discretionary allocation could be extended for the CIL linkages as well. This would require CIL to allocate linkages through a market-based mechanism.

3. Key questions to be considered while allocating such linkages are as follows:-
   (a) Who should be given these linkages and the methodology thereof?
   (b) At what price should such linkages be given?

4. The coal linkages are presently granted to various entities on the basis of decisions of a Standing Linkage Committee. In the non-regulated sector, there is no justification of providing coal at a price less than the market price because the market is not regulated and the price of the final product is determined by the market forces. This also provides a non-level playing field within the non-regulated sector in favour of those having linkages vis-a-vis those not having such linkages.

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5. An Inter-Ministerial Committee (IMC) was constituted to consider and examine various structures and implementation models for implementing the competitive bidding for auction of coal linkages/LoAs and to recommend the optimal structure that would meet the requirement of all the stakeholders. Some options for market based allocation of linkages were discussed by the IMC.

6. Any framework for this purpose that is based on approach to the auction of coal linkages should have the following features:
   (a) It should be transparent, minimize discretion and should create a level playing field.
   (b) It should encourage market based pricing structure.
   (c) It should have differentiation for regulated and non-regulated sectors.
   (d) It should ensure that all market participants have a fair chance to secure the coal linkage, irrespective of their size.
   (e) It should attempt to ensure an optimal allocation of coal across user industries and geographies.

   Moreover, revenue maximization should not be the sole objective and should not take precedence over the need to make available coal, a scarce and essential commodity, in a fair manner to the end-users.

7. At present RoM prices of CIL are different for Regulated and Non-regulated sectors. This is a fair principle and especially in the non-regulated sectors, the various end-use sub-sectors have their own distinctive economics and a methodology. If the sectors are pitted against each other, it would lead to some sectors losing out on linkages. Therefore, separate quantities may have to be earmarked for Regulated and Non-Regulated sectors on the one hand, and furthermore, within the Non-Regulated sub-sectors, Cement, Iron & Steel including Sponge Iron, Aluminium, Fertilizer, and Others would have separate quanta in the auction process.

8. Keeping in view the aforementioned objectives, the **broad approach** for Non-Regulated Sector may be that:

   (a) The non-regulated sectors may bid for linkages earmarked for given sub-sectors. Bidders would bid above the CIL price for the relevant grade. The sub-sectors are enumerated as Cement, Iron & Steel including Sponge Iron, Aluminium, Fertilizer, and Others.
   (b) CIL will allocate coal from any such small unit which is suitable in terms of administration and optimization. For this, sub-zones within a subsidiary may be envisaged, so as to minimize grade variations and reduce

transport distance. Railways Plan would go hand-in-hand with incremental CIL production.

(c) The tenure of linkage may be five years. Different quanta of coal linkage may be earmarked for particular user industries as described previously and which would be continuously reviewed at periodical intervals.

(d) A balance between the objectives of transparency, market discovery of price of coal where demand and supply match, and, the interests of end-users would need to be struck.

9. The methodology for auction of linkages that achieves this balance is Supplier Controlled Ascending Market Clearing Auction where the prices are increased till demand-supply equilibrium is established. The initial floor price is set at the relevant CIL ROM Price and for a particular link quantity. If bids are received for quantity greater than link quantity, then the floor price is increased in steps. Auction stops when bids are received for exact quantity i.e. link quantity offered. Maximum bid quantity would be lesser of 65% of end-use plant requirement or 15% of quantity auctioned. The method is illustrated in the table below:

Link Quantity Offered	10 MT
Bidding Round 1	
Floor Price	Rs. 3000 / T
Bids Received for	30 MT
Bidding Round 2	
Floor Price	Rs. 3500 / T
Bids Received for	15 MT
Bidding Round 3	
Floor Price	Rs. 4000 / T
Bids Received for	10 MT
Result: 10 MT quantity awarded @ Rs. 4000 / T	

In this methodology:

- Single price avoids wide variations and speculation.
- Prices are directed by the auctioneer through algorithmic iteration. Clearing price reflects an overall market equilibrium where demand matches supply at a single price.
- Single price is acceptable to all bidders.
- Price discovery is attained while avoiding unviable prices.

- Balances the considerations of judgments of the Hon'ble Supreme Court in the case of Coal Block Auctions in 2014, and the case of Ashoka Smokeless in 2006.

10. For auction of linkages, CIL will chalk out an auction calendar to minimise speculation so that realistic prices are obtained. CIL Production Plan and tentative Auction Calendar can be made available on a quarterly / semi-annual basis. Viable minimum service level of 4200 Tonnes Per Annum (TPA) would be considered. Smaller geographical area, like a coalfield, for coal evacuation may be required to minimise uncertainties in transportation. To assure the end users of price stability for some period, the prices may be fixed for the first 5 years.

11. Future linkages to the non-regulated sector shall be given through e-auction through Supplier Controlled Ascending Market Clearing Approach as detailed in para 8 to 10 above. All allocations after 01.07.16 shall be auction based.

12. Linkage quantities corresponding to existing FSAs, if any, maturing prior to 01.07.16 will also be offered for allocation through above methodology, as and when they expire. There will be no renewal of FSAs of non-regulated sectors.

13. Those entities that have existing linkages that are expiring after 01.07.16, shall be given a termination notice of one year w.e.f 01.07.15. This will also be given wide publicity. The terms and conditions of existing FSA permit such termination of linkages. As per of FSA, *"In the event of any material change in the Coal distribution system of Seller due to a Government directive/notification, at any time after the execution of this Agreement, the Seller may terminate this Agreement without any obligation/liability after providing the Purchaser with prior written notice to the Purchaser of not less than thirty (30) days."* Thus, instead of 30 days, a notice period of one year for termination of linkages will be given so that existing linkage holders will get reasonable time to plan for adaptation to new system or make alternative arrangements. If this is not done, it would create an uneven field to the advantage of existing FSA holders.

14. Any additional quantity allocated to non-regulated sector on account of incremental production of coal shall also be allocated through above linkage auction process.

15. Auctions as per above methodology shall be conducted by CIL.

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Disclaimer

This document is not an agreement and is neither an offer nor invitation by the Ministry of Coal to the prospective bidders or any other person. The purpose of this document is to invite/elicit views or comments of the general public and stakeholders.