PRESS RELEASE

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Average tariff hike of 4.5% along with reduction in AT&C losses below 15% needed to eliminate the gap between ACS and ARR: ICRA

- ***Regulatory assets remain high across key states in India at Rs. 3 trillion; Additional steep tariff hike over and above the average tariff hike would be needed for liquidation of these regulatory assets***
- ***Tariff orders issued for discoms in 23 out of 28 states for FY2026 with a median tariff hike of 1.9%***

Rating agency ICRA highlighted that the regulatory assets (RA) position for seven[1] state discoms remains elevated at ~Rs. 3 trillion. The Hon'ble Supreme Court (SC) has recently directed the liquidation of RA within four years, although implementation by state discoms remains to be seen. Further, the all-India average cost of supply (ACS) - average revenue realisation (ARR) gap stood at 46 paise/unit in FY2024, to eliminate which an all-India average hike of 4.5% along with a reduction in aggregate technical and commercial (AT&C) losses below 15% is needed, amidst a wide variation across the states. Hence, improved operating efficiency and implementation of regulatory reforms remain critical to address discom financial stress. Consequently, the rating agency maintains a Negative outlook on this sector.

The SC issued an order recently on the petitions filed by discoms and regulatory commission in Delhi with respect to the build-up of RAs for Delhi discoms, citing a systemic regulatory failure in the governance of tariff determination and management of RAs. As part of this order, the SC has issued broader directions to all state electricity regulatory commissions (SERCs), mandating liquidation of legacy RAs within four years and capped the creation of new RAs at 3% of the Annual Revenue Requirement (ARR). The SC directed the Appellate Tribunal for Electricity (APTEL) to monitor the implementation and enforce accountability on the creation and liquidation of RAs.

Commenting on this order**, Girishkumar Kadam, Senior Vice President & Group Head - Corporate Ratings, ICRA,** said: "*As per ICRA's estimate and based on the tariff orders issued by the SERCs, the RA position at all India level remains elevated at ~Rs. 3 trillion, mainly driven by the states of Tamil Nadu, Uttar Pradesh, Rajasthan, Maharashtra, Delhi, West Bengal and Karnataka, with the first three states accounting for a majority share. Complying with the SC directive would thus necessitate steep tariff hikes across these states, which would in turn require state government support for effective implementation. Apart from improvement in operating efficiencies, regulatory reforms to ensure timely issuance of tariff orders with cost reflective tariffs remain critical to achieve a sustainable improvement in discom finances going forward"*.

The tariff orders for FY2026 have been issued in 23 out of 28 states as of August 2025, indicating a moderate progress as these should have been issued by March 2025 for all states. Moreover, the median tariff hike at the all-India level remains modest at 1.9% in FY2026, lower than the 2.1% in FY2025, reflecting continued reluctance to align tariffs with the cost of supply, wherein the power purchase cost (PPC) remains the major contributor.

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[1] Tamil Nadu, Uttar Pradesh, Rajasthan, Maharashtra, Delhi, West Bengal and Karnataka

Commenting on the gap between the ACS and the ARR**, Girishkumar Kadam** said: "*The implementation of the Fuel and Power Purchase Adjustment Surcharge (FPPAS) mechanism remains important to ensure the timely pass-through of PPC variation to the consumers. However, this remains patchy, with only a few states operationalising the mechanism fully despite its notification in December 2022. The all-India ACS-ARR gap stood at 46 paise/unit in FY2024, being particularly high in Andhra Pradesh, Madhya Pradesh, Maharashtra and Telangana. ICRA estimates an all-India average hike of 4.5% along with a reduction in AT&C losses to below 15% is needed to eliminate the gap between ACS and ARR, with the tariff hike required varying widely across the states.*"

The rationalisation of GST rates on coal from 5% to 18% and removal of compensation cess of Rs. 400 per ton, is expected to reduce the cost of generation for coal-based power generators. This is expected to further benefit the discoms, as the move is likely to translate into a reduction of around 12 paise per unit in their cost of supply as coal-based capacity accounts for over 70% of total generation at an all-India level.

The financial health and operational performance of state-owned power distribution companies (discoms) remain under pressure due to a combination of factors including inadequate tariff hike, high AT&C losses, mounting RAs and large debt position. The gross debt position for state owned discoms at the all India level rose to Rs. 7.4 trillion as of March 2024, up from Rs. 6.6 trillion a year earlier, reflecting continued reliance on borrowings. Such high debt levels are unsustainable for discoms, given their current revenues and profitability, thereby necessitating support from state governments. Subsidy dependence is projected to rise to Rs. 2.2 trillion in FY2026, up from Rs. 2.1 trillion in FY2025, driven by higher ACS and new subsidy schemes in certain states. Apart from the large subsidy dependence, discoms also receive loss funding support from the state governments putting fiscal pressure on the state finances.

ICRA maintains a Negative outlook on the power distribution segment, on account of weak operating efficiencies, inadequate tariff revisions, and high debt levels. Sustained improvement in AT&C losses, timely pass-through of cost variations through tariffs, and timely liquidation of past RAs are essential for financial turnaround of state discoms.
as the combined impact of the above-mentioned factors evolves.

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