Auctions of coal mining leases: did we miss some points

June18th, 2020 will be marked as a historical day in Indian Coal Mining Industry when Ministry of Coal (MoC) has announced commercialization of 41 coal blocks. The government's objective with coal commercializationhas been very sacrosanct i.e.to increase the domestic coal production in the country which will have many direct & indirect benefits apart from enhancing the revenue through taxes, premiums to creating employment opportunity. However, the success of auctioning process will be considered partial, if the operationalization of coal blocks does not happen. Looking from the industry perspective there are the 3 (three) pivotal aspects of commercial coal mining business in India, these are building strong revenue model, raising of funds and technical due diligence of coal blocks.

	Issues	Perspective	Concerns
	Building strong revenue model		
(1)	Commercial coal mine production (without having an end user arrangement) is to compete with CIL/SCCL long term FSAs &spot auction prices.	In order to remain competitive, the commercially mined coal needs to be sold the coal at discounted prices	This would require a buyer agreement in place by the time coal production starts i.e. after 3-4 years. The market of coal as source of fuel is getting thwarted by renewable energy penetration in tune withGovernment's much emphasis on promulgation of cleaner sources of energy
(2)	Improper revenue sharing mechanism for sale value of coal	The revenue sharing mechanism along with royalty & taxes willat representative prices linked to NCI escalation (which is a function of coal sales channels)	The representative prices are as high as around 50% as compared to CIL prices for a particular grade of coal. Also, there is no clarity on NCL escalation.It will result in higher outlay of revenue sharing *vis-a-vis* actual revenue realization for the coal miner and ultimately impacting the bottom line of the business.
(3)	Unreasonably higher collection of upfront amounts	The calculation of upfront amount is on the geological reserve and on the representative prices of grade of coal and is entirely payable before getting the vesting order	The geological reserve mentioned in the tender document against each coal block is way higher as compared to the extractable reserve mentioned in the production schedule. The higher initial cash outflow for non-minable reserves and partly remittance of the upfront amount is unjustifiable and will be deterrent to larger participation
	Raising of Funds		
(4)	Due to high capital-intensive nature of the coal mining business the general capital structure is in the range of 70:30 or higher	Lenders are shying away from investing in high carbon footprint businesses.	Land, R&R, upfront amount, and previous allottee payments are forming the 60% of the initial capital investment and is non-fundable by the NBFCs/banks. Moreover, without a robust revenue model the lenders are finding it a very difficult to finance it. Thereby achieving the timely financial closure of the project would be a challenge
	Technical due Diligence		
(5)	Technical Due Diligence of existing coal mining infrastructure	Identified coal blocks having existing infrastructure with their detailed cost breakup have not been furnished	A Thorough due diligence is required for existing mine infrastructure for estimating the correct valuation of the established infrastructure assets. However, in most of the blocks the WDV of those assets for year 2014-15 has been imposed on the bidder under prior allottee expenses
(6)	Land and R&R payments	Coal blocks where partial land acquisition has been made but physical possession of the land is not done yet	It will be a double whammy for the bidder to acquire and get the physical possession of the land along with the payment provision to prior allotteefor the already acquired land is to be done
(7)	Establishing the Coal Quality for the project life	The quality of coal needs to be ascertained based on the weighted average grade of the coal.	Tender documents arebased on higher mentioned grade of coal. The realistic estimation of extracted coal grade will give altogether a very different picture and will truly base on the risk appetite of the bidder

Digging deep there are many loose ends that needs to be tighten for achieving the collective success of the entire auctioning process. Some of them are as:

a. Govt must notify the minimum available extractable grade of coal from the particular coal block. This would reduce down the risk appetite of the bidder for marketing & selling of coal.

b. For non-fundable part of the project i.e. land, R&R, etc. the government must come up with something like viability gap funding (VGF) in order to share the risk of investment

c. For initial investment made by the prior allotteefor the existing infrastructure in the coal block/mine; a realistic valuation of the asset must be done by 3rd party nominated by the government and based on it the prior allottee expense must fixed up.

d. Amidst competition from other sources of energy and government's promulgation for clean & green energysources; there should be a proper of exit mechanism to be provided in the tender document/coal mine development and production agreement (CMPDA) considering the high capital investment.

If the issues faced by industry are not addressed within the proper timeline then the commercial coal block auctioning process will just become another exercise in futility.

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