Maharashtra State Power Generation Company Limited

Risk Management Policy

RISK MANAGEMENT

COMPANY POILICY, PROCESS AND MEASURES

THIS IS A COMPREHENSIVE GUIDE TO THE ALL EMPLOYEES OF MAHARASHTRA STATE POWER GENERATION COMPANY LIMITEDTO PRACTICE RISK MANAGEMNT ACROSS ALL FUNCTIONS AND LEVELS TO IDENTIFY AND MITIGATE POTENTIAL RISKS TO OPTIMIZE BUSINESS PERFORMANCE AND ENHANCE STAKEHOLDER VALUE.

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A. BACKGROUND

Maharashtra State Power Generation Co. Ltd. ("the Company" or MSPGCL) is a government company incorporated under the Companies Act, 1956. The Company is engaged in generation of power. It has power Thermal, Gas, Hydro and Solar power plants across the state of Maharashtra. The Company works under regulated competitive business environment. The business activities of the Company carry various internal and externalrisks.

This document lays down the framework of Risk Management at MSPGCL and defines the policy for the same. This document shall be under the authority of the Board of Directors of the Company. It seeks to identify risks inherent in any business operations of the Company and provides guidelines to define, measure, report, control and mitigate the identifiedrisks.

'Risk' in literal terms can be defined as the effect of uncertainty on the objectives. Risk is measured in terms of consequences and likelihood. Risks can be internal and external and are inherent in all administrative and business activities. Every member of any organization continuously manages various types of risks. Formal and systematic approaches to managing risks have evolved and they are now regarded as good management practice also called as RiskManagement.

'Risk Management' is the identification, assessment, and prioritization of risks followed by coordinated and economical application of resources to minimize, monitor, and control the probability and/or impact of uncertain events or to maximize the realization of opportunities. Risk management also provides a system for the setting of priorities when there are competing demands on limitedresources.

Effective risk management requires:

(i) A strategicfocus,

(ii) Forward thinking and active approaches tomanagement

(iii) Balance between the cost of managing risk and the anticipated benefits,and

(iv) Contingency planning in the event that critical threats arerealized.

In today's challenging and competitive environment, strategies for mitigating inherent risks in accomplishing the growth plans of the Company are imperative. The common risks inter alia are: Regulations, competition, Business risk, Technology obsolescence, return on investments, business cycle, increase in price and costs, limited resources, retention of talent,etc.

B OBJECTIVE

The main objective of this Policy is to ensure sustainable business growth with stability and to promote a pro-active approach in reporting, evaluating and resolving risks associated with the Company's business. In order to achieve the key objective, this Policy establishes a structured and disciplined approach to Risk Management, in order to guide decisions on risk related issues.

The specific objectives of this Policy are:

- To ensure that all the current and future material risk exposures of the Company are identified, assessed, quantified, appropriately mitigated, minimized and managed i.e. to ensure adequate systems for riskmanagement.
- To establish a framework for the company's risk management process and to ensure itsimplementation.
- To enable compliance with appropriate regulations, wherever applicable, through the adoption of bestpractices.
- To assure business growth with financialstability.

C **LEGALFRAMEWORK**

Risk Management Policy is framed as per the following regulatory requirements:

A. COMPANIES ACT, 2013

1. Provisions of the Section134(3)

   There shall be attached to financial statements laid before a company in general meeting, a report by its Board of Directors, which shall include—

   (n) a statement indicating development and implementation of a risk management policy for the company including identification therein of elements of risk, if any, which in the opinion of the Board may threaten the existence of the company.

2. Section 177(4) stipulates:

   Every Audit Committee shall act in accordance with the terms of reference specified in writing by the Board which shall, inter alia, include,

   (vii) evaluation of internal financial controls and risk management systems.

3. SCHEDULE IV [Section 149(8)]

CODE FOR INDEPENDENT DIRECTORS

II. Role and functions:

The independent directors shall:

(1) help in bringing an independent judgment to bear on the Board's deliberationsespecially on issues of strategy, performance, risk management, resources, key

appointments and standards of conduct;
(4) satisfy themselves on the integrity of financial information and those financial controls and the systems of risk management are robust and defensible

In line with the above requirements, it is therefore, required for the Company to frame and adopt a **“Risk Management Policy”** (this Policy) of theCompany

D. KEYDEFINITIONS

(i) **“Management”** in relation to the company means Chairman & MD, Wholetime Directors and Executive Directors of the Company.

(ii) **"Board of Directors"** or “Board” in relation to a Company, means the collective bodyofDirectorsoftheCompany.(Section2(10)oftheCompaniesAct,2013)

(iii) **"Policy"** means Risk ManagementPolicy.

(iv) **Risk Assessment** –The systematic process of identifying and analyzing risks. Risk Assessment consists of a detailed study of threats and vulnerability and resultant exposure to variousrisks.

(v) **Risk Management** –The systematic way of protecting business resources and income against losses so that the objectives of the Company can be achieved without unnecessaryinterruption.

(vi) **Risk Management Process** - The systematic application of management policies, procedures and practices to the tasks of establishing the context, identifying, analyzing, evaluating, treating, monitoring and communicatingrisk.

E. APPLICABILITY

This Policy shall come into force with effect from date of approval by the Board.

F. ROLE OF BOARD OF DIRECTORS

1. The Board is to ensure framing, implementing and monitoring risk management plan, having in place systems for risk management as part of internal controls with duty being cast upon Independent Directors to bring unbiased angle to the Board’s deliberations on making risk management systems more robust.

2 The Board shall define the roles and responsibilities of the Risk Management Committee and may delegate monitoring and reviewing of the risk management plan to the committee and such other functions as it may deem fit.

G. STRUCTURE AND ROLE OF RISK MANAGEMENT COMMITTEE

The Committee will comprise of senior executives of the company, chaired by the CMD,which will be responsible for defining, implementing and review of risk managementprocesses within MSPGCL. The RMC will provide updates to the Board from time to timeon key risks faced by the company and the relevant mitigation actions.
The following will be the members of RMC:
1. Chairman & Managing Director-Chairman of Committee
2. Director (Finance)
3. Director (Operations)
4. E D (O&M)
5. CGM(F)
6. CGM(RCD)
7. CS Convener of the Meeting of RMC

The following shall serve as the Role and Responsibility of the Committee for the evaluating the effectiveness of the Risk Management Framework:

1. Review of the strategy for implementing risk management policy
2. To examine the organization structure relating to Risk management
3. Evaluate the efficacy of Risk Management Systems – Recording and Reporting
4. To review all hedging strategies/risk treatment methodologies vis a vis compliancewith the Risk Management Policy and relevant regulatory guidelines
5. To define internal control measures to facilitate a smooth functioning of the risk management systems
6. To approve the Guidelines for dealing with the risks and communicate to the personnel for implementation.
7. To approve the Risk Management (including Risk Treatment) strategy, controlstructure and policy guidelines and delegate authority and accountability for riskmanagement to the Company's executive team.
8. Ensure periodic review of operations and contingency plans and reporting to Boardin order to counter possibilities of adverse factors having a bearing on the riskmanagement systems.

H. BROAD PRINCIPLES FOR RISK MANAGEMENT

The Management has to review the business plan at regular intervals and develop the Risk Management Strategy which shall encompass laying down guiding principles on proactive planning for identifying, analyzing and mitigating all the material risks, both external and internal viz. Environmental, Business, Operational, Financial and others. Communication of Risk Management Strategy to various levels of management for effective implementation isessential

Risk Identification is obligatory on all vertical and functional heads with the inputs from their team members are required to report the material risks to Management along with their considered views and recommendations for risk mitigation.

I. IDENTIFICATION OF MAJOR RISKS IN EACH CATEGORY

In today's challenging and competitive environment, strategies for mitigating inherent risks in accomplishing the growth plans of the Company are imperative. The Management has identified following major risks specific to MSPGCL that have impact on the business &profitability:

1. OPERATIONAL RISKS:

Risks inherent to business operations including those relating to incorrect practices in O &M, Projects, incorrect estimation, unfavourable and ambiguous contract terms, project related delays, delay in collections, deficiency in design & drawings, time extensions, labour unrest, disputes and technology obsolescence etc.

2. FINANCIAL RISKS:

The company has identified financial risk and categorized them in three parts viz (i) Credit Risk, (ii) Liquidity Risk & (iii) Market Risk. The details regarding sources of risk in each such category and how company manages the risk is explained as under:

(i) **Credit Risk-** Credit risk is the risk of financial loss to the company if a customer or counter party to a financial instrument fails to meet its contractual obligations and arises principally from the company's receivables from customers and investment securities. One of the major risk experienced by the Company is DISCOM's defaults in release of funds and irregular payments .This has created an undue pressure on cash management and has resulted in excessive borrowings at higher interest rates. The frequent occurrence of such defaults has lead to the financial solvency and liquidity risks (which will eventually compound in to CreditRisks). The Company establishes an allowance for doubtful debts and impairment that represents its estimate of incurred losses in respect of trade and other receivables and investments.

(ii) **Liquidity Risk-** Liquidity Risk is the risk that the company will not be able to meet its financial obligations as they become due. The Company has a strong focus on effective management of its liquidity to ensure that all business and financial commitments are met in time. The company has adequate borrowing limits in place duly approved by shareholders and Board. Company sources of liquidity includes operating cash flows , cash and cash equivalents and fund and non fund based lines from banks. Cash and fund flow management is monitored daily in order to have smooth and continuous business operations.

(iii) **Market Risk-** Market Risk is further categorized in

a) Currency Risk- The Company is exposed to currency risk on account of its borrowing in foreign currency from World Bank and Germany. As the company operates in regulatory environment any variation in foreign exchange rate is allowed to be recovered from consumers at actual.

b) Interest rate Risk- The Company is exposed to interest rate risk depending upon conditions of money market and RBI regulations.
c) Commodity Risk- The primary fuel of the Company is coal and gas. These are mostly Government controlled sectors. Any changes in pricing rules of these commodities by the Government of India or international regulations affects the working of the company.

3. RESOURCES RISKS:

Risks arising from inappropriate sourcing or sub-optimal utilization of key organizational resources such as talent, capital and infrastructure, erosion of talent/skills and ineffective HR Policies will have significant bearing on the bottom line of our business. The Company has adopted mitigation measures to minimize the effects of these risks.

4. PURCHASE AND INVENTORY RISKS:

The Company is dependent upon vendors and suppliers for procurement of specialized equipment, materials, consumables and services like fabrication, erection and civil works. The selection, quality, efficiency and effectiveness of these agencies and the prices will have direct bearing on the quality and successful execution of O &M and the profitability of the business. In addition, unplanned procurement and building up of excessive inventory will block the funds and lead to strained finance management and expose the company to financial risk.

5. REGULATORY & COMPLIANCE RISKS:

The complexity of the business and regulatory landscape is increasing dramatically. The Company is exposed to risks arising from inadequate compliance to regulations, sudden burst of new regulations, contractual obligations and, Change in Law, etc.TheCompany submits the annual revenue requirement to Maharashtra Electricity Regulatory Commission (MERC), based on these approved tariffs the Company raises monthly energy bills to Customers. The tariff so determined by MERC are based on the MERC (Multiyear tariff) regulations which get revised periodically. Thesetariff are determined based on normative parameters as set out in the said regulations. Any changes in the normative parameters or guiding regulatory provisions have impact on the income from sale of power of the company

6. BUSINESS RISKS:

Risks arise out of excessive dependency on selected portfolio (Power Generation), change in political and economic environments, loss of trust in the market (Fidelity), competition and litigations. The most of the installed capacity is based on fossil fuel (coal based) having enormous adverse impact on environment. Any national or international development restricting fossil fuel based power generation will impact the future profitability of MSPGCL

7 COUNTERPARTY RISKS:

Risks arising from our association with entities for conducting business will have impact on the performance of the Company and will affect Company’s reputation as well as profitability. These include clients, vendors, transporters, alliance partners and their respectiveindustries.

Delay in achieving Financial Closure, Suspension of works, Variations, delay in delivery, non-performance of suppliers & contractors, etc. are some of the major risks associated with our customers andvendors/suppliers.

8 REPORTING RISKS:

Risks arising out of wrong information provided in tender documents, improper valuation of inventory, over certification of contractor bills, improper planning and progress reports, etc. are some of the risks specific to ourBusiness.

J. RISK QUANTIFICATION (MEASUREMENT OF RISKS)

The risks are quantified based on their frequency of occurrence and the consequence. The degree of severity is assessed based on the type of the consequence that the risk will make such as; Financial, Reputation, Strategic, Legal & Regulatory, Human Resources and Counterparts and the actions are taken based on the probability of occurrence and impact of risk.

The Company has adopted Analytical Analysis Method and also relies on Expert Judgment for assessment of risks and their impacts and devises strategy to tackle the risk at appropriate level. In both the cases, following matrix is followed in identifying and initiating actions:

Probability	**Impact**	**Action**
High	High	Immediate
High	Low	Consider the steps to take
Low	High	Consider the steps to take and produce a contingency plan
Low	Low	Keep under review

K. RISK TREATMENT AND CONTROL

Apart from the selecting and adopting suitable mitigation measures, the Company is in the process of developing Risk Prevention Capabilities to deal with the Potential Risk Events that will affect the objectives of the Company.

The Company is periodically arranging awareness programs among all the employees cutting across all levels and helping the team to develop the prevention capabilities to limit the probability of occurrence of a risk event that will impact the objectives rather than focusing on limiting the nature and extent of effects that the risk event has on theachievement of objectives post its occurrence.

To make use of available resources most efficiently, the Company has adopted a combination of Preventive and Mitigation measures to treat the risks depending upon their nature and magnitude.

The criteria for the selection of an appropriate strategy to treat the risks areas shown below:

Likelihood		Small	Large
	High	Prevention Measures (Enhance Quality)	Prevention and Mitigation
	Low	Maintain and Monitor	Mitigation Measures (Preparedness)

Impact

L. GUIDELINES TO DEAL WITH THE RISKS

Business Plan including Capital Expenditure and Fund Flow Statement for each segmenttogether with SWOT analysis, data on generation Planning, Materials Management, Assets, Accounts Receivables and Payables as well as Regulatory Regime applicable shall be reviewed in the light of the material risks identified. Through deliberations of the committee a comprehensive plan of action to deal with the risks shall be developed and guidelines flowing from such plan shall be communicated to the employees concerned for mitigation of the risks.

M. INTEGRATION OF RISK MANAGEMENTSTRATEGY

MSPGCL's risk management strategy is to be integrated with the overall business strategies of the organization and its mission statement to ensure that its risk management capabilities aide in establishing competitive advantage and allow management to develop reasonable assurance regarding the achievement of the Company'sobjectives.

N. REVIEW &AMENDMENT

This policy shall evolve by review by the Board from time to time as may be necessary. This Policy will be communicated to all vertical/functional heads and other concerned persons of theCompany.

O. COMPLIANCE AND CONTROL

All the Senior Executives under the guidance of the Chairman and Board of Directors has the responsibility for over viewing management's processes and results in identifying, assessing and monitoring risk associated with Organization's business operations and the implementation and maintenance of policies and control procedures to give adequate protection against key risk. In doing so, the Senior Executive considers and assesses the appropriateness and effectiveness of management information and other systems of internal control, also encompasses review of any external agency in this regards and action taken or proposed resulting from thosereports.