News_MOR_2009-5.pdf

16-07-2009 - The Island.

Kerawalapitiya LNG POWER PLANT

Gas Hopefuls for Electricity, now from Australia

by Dr Tilak Siyambalapitiya

A recent news report said that work has begun on a liquefied natural gas power plant at Kerawalapitiya. The power plant will be built by an Australian company, and a letter of intent is to be issued by Ceylon Electricity Board (CEB) soon, said another report. Mr O S Perera, a former Chief Engineer of CEB wrote to The Island (11th June 2009) said that "Natural gas power plant a windfall" and continued to say that "the project is being actively promoted by a Most Venerable Buddhist Priest and therefore the details given to the media regarding the power project should be correct". That's what a former Chief Engineer of CEB has to say. It was also revealed that officials of CEB and the Attorney General's department are delaying the project. Mr O S Perera also revealed that Aloka Engineering will not charge for any capacity costs, and hence will give a free gas terminal for the people of Sri Lanka. Thank you.

Subsequently, Mr GAD Sirimal and Mr Neil Perera, both distinguished officers retired from the energy sector, expressed their views. Dr Janaka Ratnasiri also highlighted the environmental benefits of LNG (The Island, 29th June).

People of Sri Lanka should thank Aloka Engineering for their most generous thought of giving Sri Lanka's people a gift of about USD 600 million. The last gift of a power plant Sri Lanka had was the Victoria hydropower plant from the British Government in 1984, and that was 120 million pounds sterling. So, this LNG terminal to be gifted by Aloka Engineering is about three times the value of the gift in 1984 by the British Government. However, Engineer MVR Fernando raised some questions about the project (The Island, 17th June 2009). What is the cost of operating this power plant ? How competitive is LNG as a fuel source for power generation ?, he asked.

We have to turn to specialists, when we need to learn about the costs of power generation. First and foremost, the country's experts on power generation economics are in CEB. Yes, CEB has many shortcomings, but has maintained strong, professional planning units in all spheres of its activity. They have repeatedly reviewed all these technologies and concluded that coal power is the cheapest way in which we can provide a reliable supply of electricity to our economy, at a regionally competitive price, using environmentally compliant power plants. Many Governments in the past did not trust CEB experts, and the present one including HE the President have repeatedly said that the power sector is in this sorry state because previous Governments did not listen to CEB experts. That's why one coal power plant and one large hydropower project are now under construction. Several more are being studied and negotiated. As far back as in 1997, against CEB's wish, the then Treasury Secretary advertised calling for LNG power plants to be built in Sri Lanka, encouraged off and on by the then BoI Chairman, hoping to teach a lesson to CEB on its insistence on coal power. Alas, there were no offers. Then the same Government appointed an international panel to review CEB generation plan, who concurred with CEB's recommendations. Additionally, the World Bank (2002), USAID (2003) and Japan International Cooperation Agency JICA (2006) conducted studies on their own, published reports, and concluded as follows:

The World Bank 2002: "LNG is not an economic source of power for Sri Lanka for the foreseeable future. The arguments about LNG have simply added to the delays in making a decision for the coal project, without any real prospect of LNG projects becoming bankable in Sri Lanka in the near future."

USAID 2003: "The prime difficulty in introducing gas is that the potential demand in Sri Lanka is small, reaching only 1.3 bcm by 2011" and went on to say that "... the cost of this gas would still be higher than the coal".

JICA 2006: Recommended LNG-based power generation from year 2020, not owing to economic reasons but to fulfill fuel diversity and lower emission objectives.

So, our own experts who work in CEB, three overseas independent experts/agencies have clearly said that LNG is not on, and too expensive. Of course, if one compares with auto diesel, electricity from LNG is indeed cheaper, that too, provided we get that USD 600 million gift the terminal from Aloka Engineering, who will then charge us only for gas. Well, auto diesel power plants we have are one large national blunder, at times a safety valve to come out of a hopeless power crisis, and at times, built to please politicians in more than one way. If you want long-term economics, you compare your options with the lowest cost option, not against the cost of a blunder.

In spite of all these studies and conclusions, LNG power plant proposals keep coming back, over and over again, largely owing to commercial pressure on Sri Lanka government, from at least two countries, at times backed by their official agencies, too. Sri Lanka's National Energy Policy (Gazette Extraordinary, 1553/10, 10th June 2008) gives the following guidelines: "The strategy of the Government shall be (to) immediately diversify into a third fuel...... this third fuel shall be coal. Non-conventional Renewable Energy (NRE) shall be the fourth resource in this diversification and security strategy". Therefore, it is very clear what the Government's policy is: diversify into coal to ensure price competitiveness to the electricity customer, diversify into renewable energy to uphold national energy security and fuel diversity. Unfortunately, LNG is neither cheap nor indigenous, and therefore has no space in the present energy policy. However, the policy does not explicitly exclude LNG for ever, but imposes a moratorium on oil or other fuels of which the price is indexed to that of oil, to be excluded and rejected, until 80% of electricity in the country is from non oil-based fuels. (ie coal for economy and diversity, renewable energy for diversity, some for economy). The policy articulates that Sri Lanka is willing to pay more for renewable energy to help national energy security, but will not compromise the right of her citizens to use cheaper sources of energy (coal) as in any other region or in the world.

What is more ? The Electricity Act No 20 of 2009, now the law of the country, has this to say in section 41: "...transmission licensee shall (in this case CEB), in accordance with the conditions of the transmission license and such guidelines relating to procurement as may be prescribed by regulation and by notice published in the Gazette, call for tenders to provide new generation plant or to extend existing generation plant". So the Attorney General, though faulted by Mr O S Perera, may have very real concerns of allowing CEB to issue a letter of intent on a power plant which is not in the national long-term plan, and has not followed the proper procedure in terms of the energy policy and the electricity act.

The Mihaly Fiasco

The year was 1992. The then Government "ordered" CEB to call for private investment offers to build a coal-fired power plant in Trincomalee. The Government-appointed Chairman succumbed to political pressure, and advertised. A company who has not built a single power plant in the world was selected to build the first coal-fired power plant in Sri Lanka, in a war zone at that time, and was issued with a letter of intent. The project in a war zone and the company with no experience were both obviously not bankable, but the high and mighty of the 1993 era would not listen to CEB engineers' views and chased them away from many a meeting. The game went on, and the project was clearly not bankable, and was subsequently known as the "Mihaly fiasco" ending up with the company claiming project promotion expenses and lost profits from the Government of Sri Lanka. The govt. successfully defended the arbitration case in London, at an enormous cost. At the end of the day, we got no power plant but only an arbitration case to fight out. What Sri Lanka needs is not another arbitration case for a hypothetical LNG power plant which is clearly not bankable without a power purchase agreement, and clearly the government is unable to issue a power purchase agreement based on the facts described above.

If Australia or any of its companies, or for that matter any other country or lending agency or any of the former Chief Engineers of CEB want to help Sri Lanka in power generation, give us a coal fired power plant or a large hydroelectric power plant, or help rehabilitate the ones we already have to get a higher output. We do not need it for free, we will pay for it. After all, the bulk of Australia's electricity comes from coal, not from gas. Help us to do the same. If you really believe LNG is cheaper, build the LNG facility as a merchant power plant, do not ask for any guarantees, letters of intent and power purchase agreements, just like any other BoI investment in Sri Lanka, which have no long term agreements with any buyer for their products. Take the risks and play the game accordingly. If the price is right, there will be buyers. There will be ups and downs, just like in the Hazira LNG terminal in India owned by Shell. In that LNG terminal, there is no power purchase agreement. If the price is right, power plants and other industries will buy gas. Otherwise, they will use other cheaper fuels.

To the Sri Lankan industrial and business community, and the Chambers of Commerce and Industry, and their Federations, etc etc., we have this to say: "sing praises to projects that undermine the long term plan and policy, and get ready to pay higher prices for electricity. That's what some of you did over 1992-2004, and you and all other members of your trade chambers and the whole country are paying dearly for that. Your electricity prices are now higher than the prices in Australia, and will continue to be so: why?: Because Australia uses coal, but they want us to use gas to produce electricity.

To the BoI, the options are plain and clear: electricity is not an export product (at least for now), and it has to be sold within the country. When signing investment agreements with other new investors from now onwards, please say this; we have just signed an investment agreement for a LNG power plant for 25 years. Unlike your garment factory, for which Sri Lanka will not sign a textile supply agreement or garment-purchase agreement, they are asking for a power purchase agreement. For your new garment factory or commercial venture, electricity will be such a percentage more expensive if this gas power venture materialises, and add that, "this is what our predecessors at BoI did in the 1990s to invite oil-fired power plants, and we thought we taught a lesson to CEB, and see the beautiful electricity prices we now have in Sri Lanka, and of course, when another management takes over BoI a few years later, they will continue to blame CEB for the high electricity prices when this LNG power plant is built !!!"

"We have to turn to specialists, when we need to learn about the costs of power generation. First and foremost, the country's experts on power generation economics are in CEB. Yes, CEB has many shortcomings, but has maintained strong, professional planning units in all spheres of its activity. They have repeatedly reviewed all these technologies and concluded that coal power is the cheapest way in which we can provide a reliable supply of electricity to our economy, at a regionally competitive price, using environmentally compliant power plants."