

# A REVIEW ON CANCELLATION OF PPP PROJECTS IN INDIA

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**Abstract-**This paper refers to cancellation of privately financed infrastructure projects of Energy, Telecom, Water & Sewerage and Transport sectors in India during 1990-2011. This document seeks that the percentage of cancellation (i.e. 1.32%) of private projects in India is minimum as compare to it's neighboring countries such as China, Pakistan, Bangladesh, Nepal and Bhutan etc. In India 3 Projects out of a total 251, 3 out of a total 37, 1 out of a total of 12 and 1 out of a total 306 are cancelled in Energy, Telecom, Water & Sewerage and Transport sectors respectively. This paper describes the reasons of cancellation (Pre-closed) of projects under different circumstances. This paper is prepared on the basis of available concerned literature, data obtained from World Bank and PPIF, data obtained from PPP India and cases of pre-closed projects. The study of this paper helps us to identify the most critical reasons of cancellation of projects of different sectors.

## Abbreviations-

PPP	-	Public-Private- Partnership
BOT	-	Build-Operate and Transfer
ROT	-	Rehabilitate –Operate and transfer
OPGC	-	Orisa Power Generation Corporation
CESCO	-	Central Electricity Supply Company
GRIDCO	-	Grid corporation of Orisa Limited
OHPC	-	Orisa Hydropower corporation
AES	-	Applied Energy Services(A multinational company infrastructure projects and distribution)
DPC	-	Dabhol Power Corporation
MSEB	-	Maharashtra State Electricity Board
GE	-	General Electric
LNG	-	Liquefied Natural Gas
OPIC	-	Overseas Private Investment Corporation

MTNL	-	Mahanagar Telephone Nigam Limited
DoT	-	Departments of Telecommunications
CMTS	-	Cellular Mobile Telephone Service
BML	-	Bharti Mobile Limited
EGTL	-	Evergrowth Telecom Limited
CVC	-	Central Vigilance Commission
ILD	-	International Long Distance
ILDO	-	International Long Distance Operator
PSTN	-	Public Switched Telephone Network
GoM	-	Government of Maharashtra
PMC	-	Pune Municipal corporation

## I. INTRODUCTION

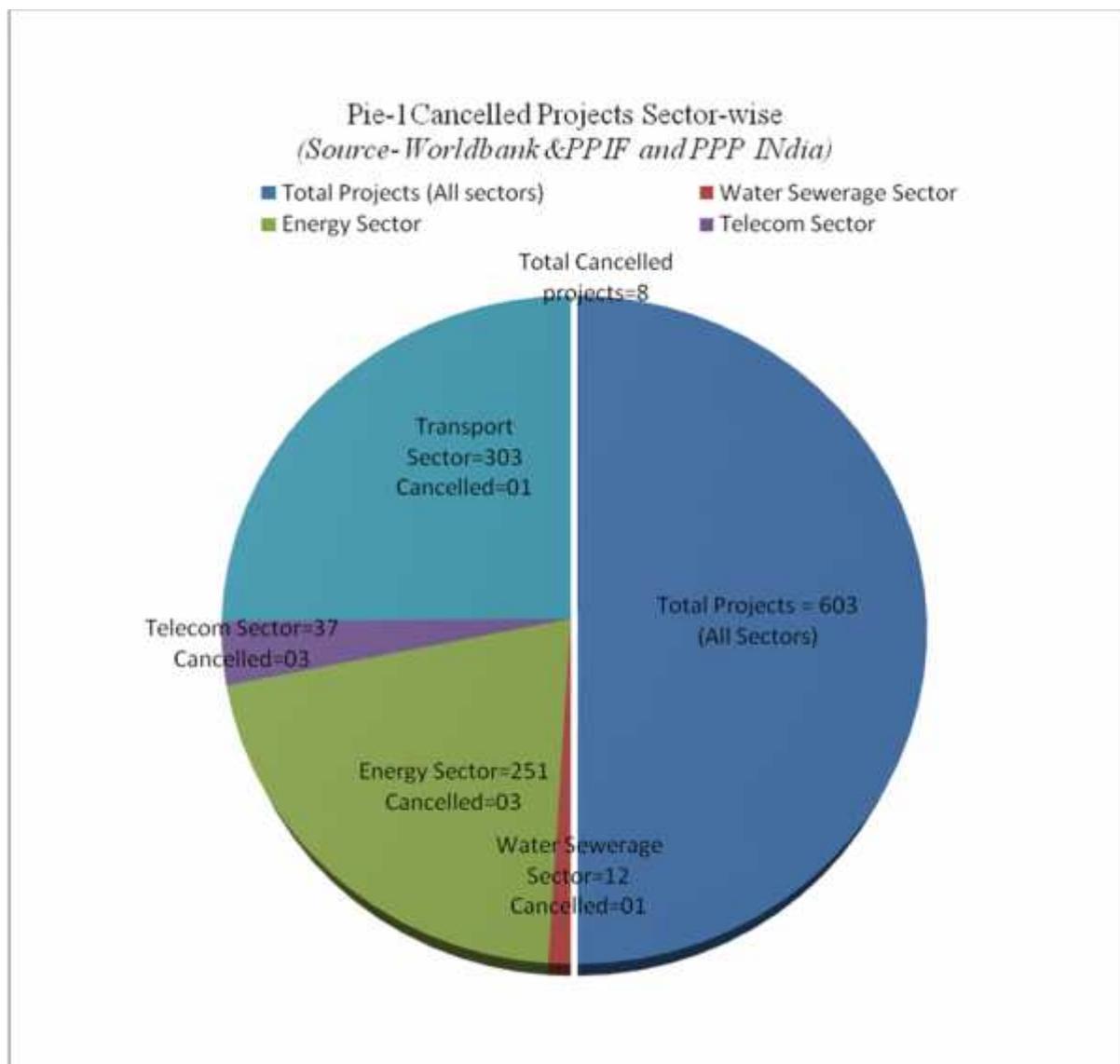
The cancellation of privately financed infrastructure projects is the subject of great concern and thinking in developing countries because privatization of infrastructures projects is the demand of any developing country such as India for infrastructure development. In India nearly 603 infrastructure projects involved private participation, attracting investment commitments of US\$ 273432.73 million and only 8 private infrastructure projects from different sectors were canceled in 1990–2011. Renegotiations or cancellation of private infrastructure projects and distribution in India and particularly in some sectors and regions. In India 3 projects in Energy sector, 3 projects in Telecom sector, 1 in Water and Sewerage sector and 1 in Transport sector were cancelled. The details of cancelled projects are shown in table-1 and pie as given below:

Table- 1-Cancelled Public – Private – Partnership (PPP) Projects in India

(Source-World bank & PPIF, IRB Ltd., Clive Harris, John Hodges, Michael Schur, and Padmesh Shukla, and Marie-Helene Zerah and Lyonnaise Des Eaux)

S.No	Project	Sector	Committed Investment	Year of Financial Closure	Year of Cancellation
1	Dabhol LNG-Fired Power Plant -	Energy	\$930	1996	2001

	Phase I				
2	Dabhol LNG-Fired Power Plant - Phase II	Energy	\$1,870	1999	2001
3	Central Electricity Supply Company of Orissa (CESCO)	Energy	\$31	1999	2001
4	Kaman Paygon BOT Project	Transport	\$3.5	1998	2009
5	Pune water Supply & Sewerage Project	Water Sewerage	\$185	1996	1998



**What is project cancellation-** ‘Cancellation’ uses the criterion of whether the private sector continued to be active in a project or not, rather than a strict legal definition of exit from the project. Thus a project that has been abandoned by a private party and later revived by another is regarded as having been cancelled. But if the private party sold its interest to another without a cessation of service or abandonment, it is not a cancellation.

During a contract or license, if following events occur before the end of project, then the project is said to be cancelled:

- ✓ The private company sells or transfers its economic interest to any other person or private sector
- ✓ The private company physically leave the project (i.e. private company withdraws all staff from the project)
- ✓ The private company stops to give services to all customers or halted construction of the project

**Special reasons of cancellation-** In India private infrastructure projects are associated with many reasons of cancellation but here some special and common reasons of cancellation corresponding to their sectors are listed below:

**(a)Energy (Electricity) Sector-** In electricity sector the Dominance of government ownership is the main reason for the cancellation of projects because this is responsible for happening the following acts:

- Overstaffing
- Gross inefficiencies
- Tolerance of theft and collusion in theft
- Poor commercial and accounting practices
- Poor investment in maintenance and modernization
- Rising deficits

On the basis of factors cited above the Distribution and supply are the worst affected. Private investors are reluctant to take over hitherto state-run distribution unless they get guarantees on safeguards against risks as well as for adequate return. The governments are unwilling and unable to take the actions required to clean up the system in

order to make the investment attractive for private investors.

**(b)Water Supply & Sewage Sector-** In this sector the project cancellation mainly depends upon the following reasons:

- Low costs of Tariffs
- Rise in water charges
- Poor collections of water charges
- Plugging leakages of water
- Incorrect evaluation of capital investments
- Non mobilization of Public and political opinion in advance behind the project

**(c)Telecom Sector-** In this sector the cancellation of projects mainly depends upon the following reasons:

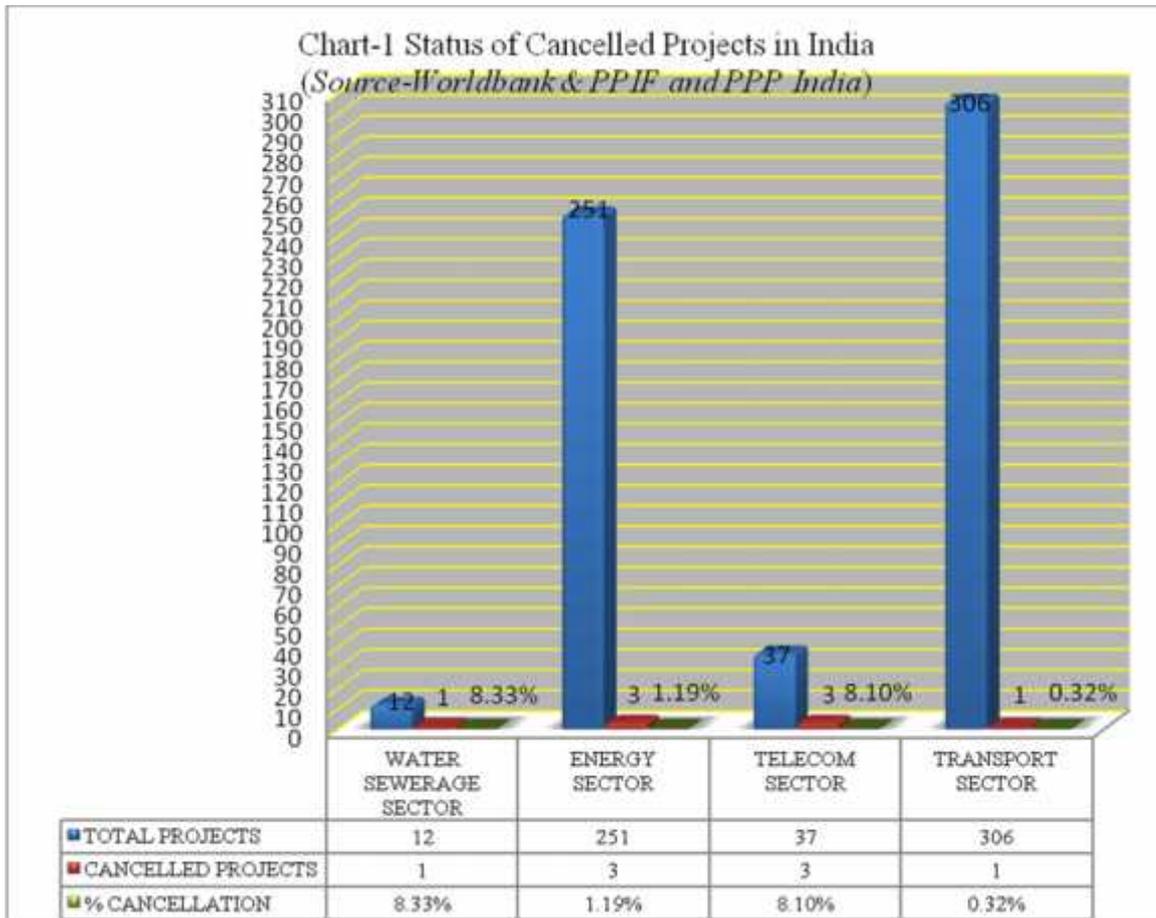
- High license fees in relation to the revenues
- Inadequate demand of services
- Impose of artificial market structures to private company by Government

**(d)Transport Sector-** In this sector the cancellation of projects mainly depends upon the following reasons:

- Inability of Government`s supports to private company to Tolls collection
- Poor estimation of forecasting the number of users
- Lower use of the tolled facilities, leading to revenue shortfalls.
- Imposition of Tolls on the improved facilities when there were none charged on the earlier unimproved one.
- Government`s failure to build public opinion in favor of such projects

**How many private infrastructure projects have been canceled in India?** The cancellation or renegotiation of private infrastructure projects in India has been quite small. Data from the World Bank (PPI-Private Participation in Infrastructure Project Database) and other literature shows that 8 projects were cancelled out of a total of 603 projects that reached financial closure between 1990 to 2011. The cancelled projects were only 1.32% with investment commitments of \$3683.9million, amounting to 1.34% of the total investment of \$273432.73 million. The 1 project was cancelled out of a total of 12 projects and the projects

were cancelled only 8.33% with investments commitments of \$185millions in Water and Sewerage sector. The 3 projects were cancelled out of a total of 37 projects and the projects were cancelled only 8.10% with investments commitments of \$664.4millions in Telecom sector. The 3projects were cancelled out of a total of 251 projects and the projects were cancelled only 1.19% with investments commitments of \$2831millions in Energy Sector. The 1 project was cancelled out of a total of 306 projects and the projects were cancelled only 0.32% with investments commitments of \$3.5millions in Transport sector. The Status of project cancellation is shown in chart -1 given below

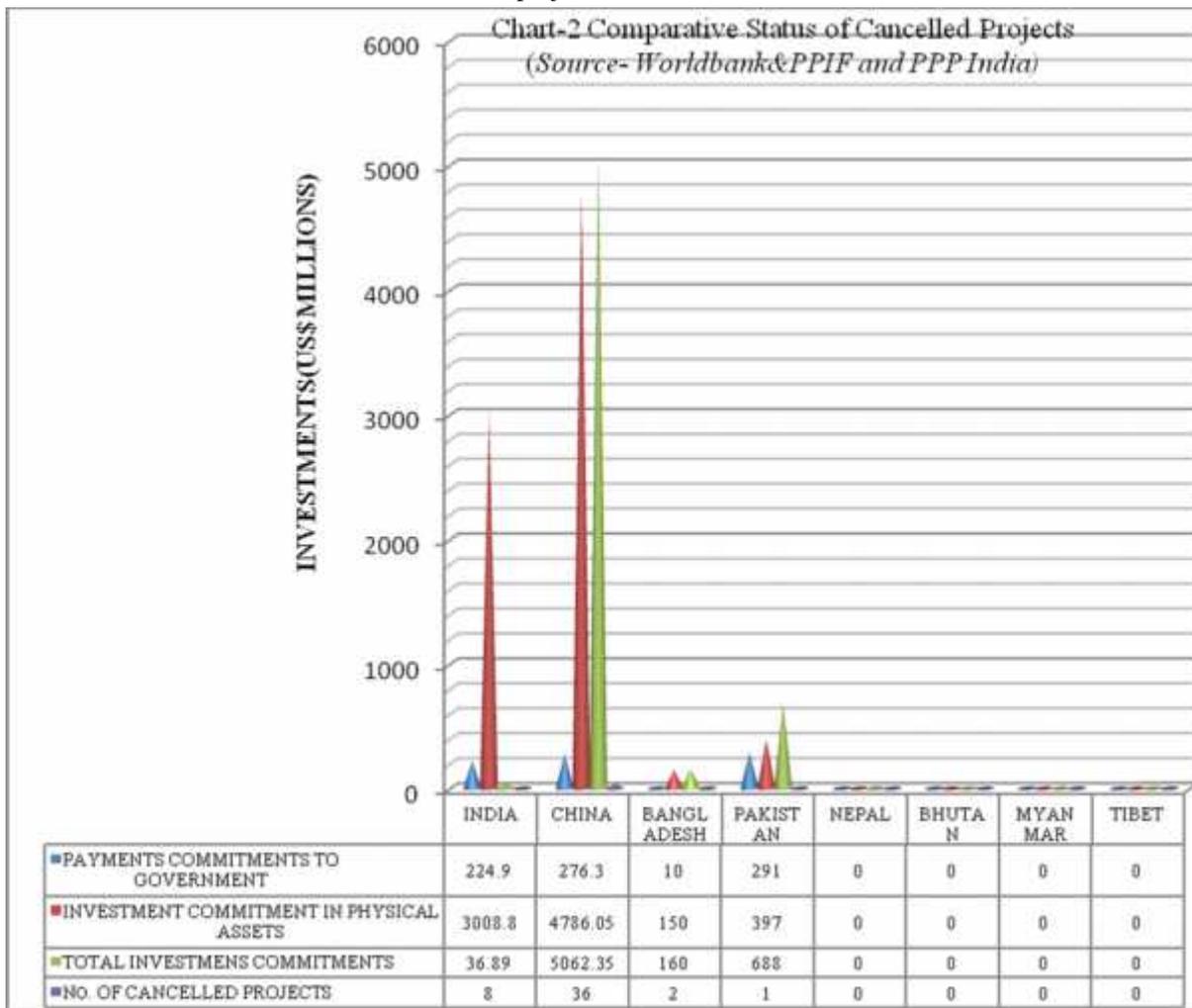


**Comparison with neighboring nations-** Data obtained from World bank and PPIF shows that the India has got first rank in minimum cancellation of private projects as compare to it`s neighboring countries during 1990-2011. In India 8 projects were cancelled out of a total of 603 projects(The cancelled projects were only 1.32%) , in

Pakistan 1project was cancelled out of a total of 55 projects(The cancelled projects were only 1.8%),in China 36 projects were cancelled out of a total of 1018 projects(The cancelled projects were only 3.53%),in Bangladesh 2 projects were cancelled out of a total of 29 projects(The cancelled projects were only 6.89%) and no

project was cancelled in Nepal, Bhutan , Myanmar and Tibet. The investment details of cancelled projects of

neighboring countries are given below in chart-2:



**Critical Problems Related to Cancellation of PPP**

**Projects-** In India the PPP projects are associated with the following critical problems:

- Given the PPP rush, little thought generally is given to project design and viability. Result: many projects have cancelled to take off, or run into opposition.
- Total lack of transparency—even after the deal has been signed. In many cases, terms and conditions have been changed to suit private developer without any review.
- Shift from build-operate-transfer to design-build-finance-operate-transfer has led to contractors raising 100% project finance via debt. End-users foot the bill.

- To get the projects, contractors are known to offer unsustainable bids, affecting the viability of operations—making demand for tariff review inevitable
- Social sector PPPs face an inherent risk of services becoming costlier and not reaching the poor. It is difficult to hold the private sector accountable.
- Lack of an independent regulator to monitor, evaluate and review projects remains a major drawback. So, public assets are transferred without proper evaluation.

**Success factors for PPPs-** The following are the some success factors for avoiding the cancellation of projects:

- A Strong political will is essential
- Underlying economics of the project should be attractive
- The project must be well designed and structured
- The private sector sponsor should be sufficiently capable
- There must be a provision of access to suitable source of finance /guarantees
- Robust legal and institutional framework of PPPs must be established
- Public sector capacity should be strong

## II. CASE STUDIES

In this article we will try to understand the problems and reasons of cancellation of all 8 cancelled projects in India.

### (1)Dabhol Power Project (Phase-I & II)-

**Project Overview-** Dabhol power plant is a massive combined-cycle power plant (largest Gas- fired power plant) of capacity 2184 megawatts spread over two phases on the western coast of India's Maharashtra state. The Dabhol power plant was initiated in 1992 and took nine years to commence operation. A 20-year Power Purchase Agreement (PPA) was signed in 1993 between DPC and the Maharashtra State Electricity Board (MSEB) with guaranteed off-take through a take-or-pay contract. The Phase-I was of capacity 740 megawatts and Phase-II of 1,444 megawatts. The total project cost is \$2.9 billion. Enron owns 65%, Bechtel Enterprises owns 10%, General Electric owns 10%, and the Maharashtra State Electricity Board owns 15%. The project was cancelled in 2001 as MSEB stopped drawing the expensive power from the project: total tariff payments by MSEB from May 1999 to December 2000 were Rs.29.31 billion. The other details of project are given below in table-2

Table-2 Details of Enron Maharashtra Power Plant (Dabhol Power Project)

(Source- World bank & PPIF)

	Phase-I	Phase-II
Project Name	Enron Maharashtra Power Plant	
Project company	Dabhol Power Company	
Location	Dabhol, Maharashtra State	
Financial closure	Dec.1996	1999
Primary sector	Energy	
Sub-Sector	Electricity	
Segment	Electricity generation	
Capacity	740 MW	1444 MW
Technology	Liquefied Natural Gas(LNG)	(LNG) & Locally available Naphtha
Type of PPI	Greenfield project	
Subtype of PPI	Build, Own, and Operate(BOT)	
Type of Agreement	Power Purchase Agreement(PPA)	
Contract period	20Years	
Type of Concession	Renewable	
Termination Year	2001	
Cancellation Year	2001	
Publicly traded	NO	

Renewal Number of Bids	0	
Number of systems	1	
Sponsor name	Bechtel(10%) USA Enron(80%) USA General Electric Capital(10%)USA	Enron(65%) MSEB(15%)India Bechtel(10%)
% Private	85%	100%
Payments commitments to Govt.	0	0
Investment commitments in physical assets	\$930(Millions)	\$1,870(Millions)
Government Support	Financing, Insurance & loan Guarantees are provided by Bank Of America(\$635 Millions)	
Funding details	Risk Insurance(\$200 Millions) by Overseas Private Investment Corporation(OPIC) Loan Guarantees(\$300 Millions) Four Indian banks have guaranteed the loans	

**What went wrong?** Bharatiya Janata Party (BJP), a right-wing party defeats the Congress and comes to power in 1995. BJP makes lots of nationalistic noise, their leader says “we will not be dictated by foreign power giants”. The new Government appoints a committee of state ministers (the Munde Committee) to review the Dabhol project. The Munde Committee had prepared and issued a sharply critical report that recommends cancelling the Dabhol project. The state government was cancelled the project on this advice of the Munde Committee. Enron had decided to go for arbitration against state Government and seeks \$300 million as compensation. The state Government had filed suit to void the agreement. A meeting was held between Rebecca Mark, Chairman of Enron International and Bal Thakre, the top power in one of the ruling parties. This meeting resulted in renegotiation between Enron and the state. A revised agreement was made between Enron and state Government and Enron had started the power generation of phase-I (740 megawatts) in 1999. MSEB stopped drawing the expensive power from the project and denied to pay Rs.29.31 billion. In April 2001 the Enron had began arbitration proceedings and in June 2001 the Dabhol Power Company (DPC) had ceased operation of the Phase-I portion of the plant and halted construction on the 90% completed Phase- II portion (1,444 megawatts).

**Reasons of Cancellations-** The main reasons of cancellation of project are as follows:

- The project had lost the support of newly formed State Government of Maharashtra.

- There was a contract dispute between the Government and plant owners.
- The company was associated with allegations of fraud, misrepresentation, violation of human rights, malfeasance and corruption at highest level.
- Lack of transparency and competition in the bid process.
- The project was not financial viable according to World Bank because it denied to finance the project.
- Cost of the project was greater than comparable projects
  - ❖ Enron cost Rs 4.49 Cr per MW
  - ❖ Comparable projects cost Rs 3.6 Cr per MW
- The power generated by plant was more expensive than that from domestic power purchaser therefore the MSEB stopped drawing the expensive power from the project.
- The MSEB was not paid an amount of Rs.29.31 billion to company.
- The process and content of original and revised agreement were criticized by Government.

## (2) Central Electricity Supply Company of Orissa (CESCO)-

**Project Overview:-** CESCO, which was initially incorporated as a wholly-owned subsidiary company of GRIDCO, obtained license from Orissa Electricity Regulatory Commission for distribution and retail supply of electricity in Bhubaneswar, Cuttack and Dhenkanal

Electrical Circles with effect from April 1, 1999. With the sale of 51% of equity holding to a strategic investor i.e. a consortium of AES (U.S.-based multinational company) and Jyoti Structures, CESCO became a joint sector company with effect from 01.09.99.

AES was one of the first Independent Power Producers (IPPs) to commission a thermal power plant in India - the 500 MW Ib Valley Project in Orissa. Subsequently, when

the State-owned generation company Orissa Power Generation Corporation (OPGC) was disinvested, AES picked up 49 per cent stake in the company. Thus, AES became a prominent private player in Orissa's power generation scene. Until 1999 it was quite happy doing what it was good at - generate and supply power to GRIDCO, the State-owned transmission company. The other details of project are given below in table-3

Table-3 Details of CESCO Project

(Source- World bank & PPIF)

Project Name	CESCO Project
Project company	AES Orissa Distribution Co Pvt. Ltd.
Location	Orissa State
Financial closure	Aug.1999
Primary sector	Energy
Secondary sector	Not applicable
Sub-Sector	Electricity
Segment	Electricity distribution
Capacity	500Number of connections (thousands)
Technology	N/A
Type of PPI	Divestiture
Subtype of PPI	Partial
Contract period	
Termination Year	2001
Cancellation Year	2001
Publicly traded	No
Renewal Number of Bids	0
Number of systems	1
Sponsor name	AES Corporation (51%) USA
% Private	51%
Payments commitments to Govt.(US\$ in millions)	10 (in1999) 0 (in2000) 0 (in1999) 21.9(in2000)
Investment commitments in physical assets(US\$ in millions)	11.4 (in1999) 8 (in 2000)

**What went wrong?** When the Orissa government, acting on the reform course charted out by the World Bank, called for bids from private investors to take over the four distribution companies unbundled from GRIDCO, it faced an awkward situation. BSES was the only eligible bidder for all the four companies. At least a modicum of variety was needed if the government was not to be blamed for handing over all the four distribution areas to a monopoly. With a little persuasion, AES agreed to take over CESCO, handling distribution for the districts of Bhubaneswar, Cuttack and Dhenkanal. However, it did so only after conducting detailed studies.

Even as the company was getting its act together, the supercyclone broke over the central zone and devastated everything in its path including the distribution networks. Rebuilding the mangled networks took priority over plugging power pilferage. GRIDCO displayed considerable understanding and indulgence and agreed to stagger its receivables from CESCO for the power it had supplied - a decision that was prompted by social and political considerations rather than commercial prudence.

However, even after several months, long after the cyclone had come and gone, CESCO did not settle its bills with

GRIDCO and the bills were mounting. Currently CESCO is reported to owe Rs.421 crores to GRIDCO for power supplied by the latter. Worse, CESCO broke the escrow in order to pay the salaries of its employees. GRIDCO in turn could not pay its supplier OPGC, to which it currently owes Rs.160 crores.

GRIDCO officials were quoted as saying that AES never made any investments in strengthening the distribution network or plugging the pilferage in the zone. AES, on the other hand, blames the mindset of the employees it has inherited from GRIDCO for its lackluster performance. However, BSES, the counterpart of AES that runs the other three distribution companies in the State, does not seem to have such problems.

CESCO was not able to make a significant dent on the technical and commercial losses of the zone. GRIDCO officials were quoted as saying that AES never made any investments in strengthening the distribution network or plugging the pilferage in the zone. AES, on the other hand, blames the mindset of the employees it has inherited from GRIDCO for its lackluster performance. However, BSES, the counterpart of AES that runs the other three distribution companies in the State, does not seem to have such problems.

CESCO's chief Executive wrote a letter to state finance secretary asking him to clear the dues. He urged the finance secretary to release at least Rs. 100 millions so that CESCO can pay salary to its employees. As there is no response from state government CESCO filed a petition in high court against the state government. High court ordered the state government and its undertaking to pay Rs. 120 millions to CESCO within two weeks and also dues for the month of July by August 15, 2002. AES is ready to forgo its \$10 million investment in Orissa's central distribution company CESCO if only it can exit from the messy business of power distribution in the State.

**Reasons of Cancellations-** The main reasons of cancellation of project are as follows:

- The existing tariff and charges of project are inadequate to meet the estimated revenue requirement of Rs.712.30 cores for the FY 2000 and it would face a deficit of Rs.200.03 cores in the year 1999-00

- Financial condition of CESCO was so worse that it is difficult for the utility to make salaries of employees for the current two months.
- The escrow account of AES managed Orissa Power Generation Corporation with GRIDCO is stated to be the reason for poor condition of CESCO. GRIDCO has right to first access the revenue earned by CESCO through this escrow facility.
- The dues (Rs. 1500 millions) were not paid by the state Government and state run corporation to CESCO.
- CESCO was unable to pay its dues (Rs 421 crores) to GRIDCO has resulted in the latter renegeing on its payments (Rs 160 crores) to the OPGC.
- Supercyclone that occur in the central zone had destroyed the distribution network of electricity. CESCO was not able to make a significant dent on the technical and commercial losses of the zone, because CESCO did not made any investment to improve the system and to bring down technical and commercial losses.
- Due to absence of **Purchased Power Price Adjustment Clause (PPPAC)**, the power purchase cost which are beyond the control of CESCO.
- High energy loss, inadequate customer service and inadequate overall system performance.

### (3) Kaman Paygon BOT Project-

**Project Overview-** The Strengthening of Chinchoti Naka - Kaman - Paygaon - Bhiwandi Road ( SH No. 4 ) Km from 0/00 to 22/600 in Vasai and Bhiwandi Talukas, Dist : Thane with Private Financing and Toll Collection on Build, Operate and Transfer (BOT) basis was conducted by IRB. This project was operated by Ideal Road Builders Private Limited (IRB). The other details of project are given below in table-7.

Table-7 Kaman Paygon BOT Project

(Source-IRB Pvt.Ltd., World bank & PPIF)

Project Name	Kaman Paygon BOT Project
Client / Employer	Public Works Department on behalf of Government of Maharashtra
Project company	Ideal Road Builders Private Limited
Location	Kaman Paygon BOT Project
Financial closure	Dec.1998
Primary sector	Transport
Secondary sector	Not applicable
Sub-Sector	Roads
Segment	Highway
Capacity	22 KM
Type of PPI	Concession
Subtype of PPI	Rehabilitate, operate, and transfer
Contract period	15 Years
Construction Period	24Months
Date of Start	7th December 1998
Actual Date of Completion	25th March 2000
Termination Year	2013
Cancellation Year	2009
Publicly traded	No
Renewal Number of Bids	0
Number of systems	1
Sponsor name	IRB Infrastructure Developers Ltd (100%) India
% Private	51%
Investment commitments in physical assets(US\$ in millions)	3.5 (in1998)
Funding details	Dombivli Nagari Sahakari Bank Ltd The Kalyan Janata Sahakari Bank Ltd.

**Scope of work-**The following items of work is to be constructed under the concession agreement:

- Widening of formation from existing 9 Mtr to 12 Mtr (22.60 kms)
- Widening of Pipe drains from 10 Mtr to 12.50 Mtrs (72.00 Nos.)
- Widening of minor bridges from 7.5 Mtr to 12.00 Mtrs (6.00 Nos.)
- Widening of Carriageway from 7.00 Mtr to 9.00 Mtr
- Improvement of road alignment and strengthening by providing BM, LBM, DBM & BC
- Providing suitable drainage arrangements.
- Construction of Toll Plaza
- Providing Road Furniture items

**What went wrong?** This project has been terminated(pre-closed)and right of company to collect toll was rescinded with effect from November 23, 2009 as per the notification issued by Dy. Secretary to the Government of Maharashtra, public works department, Mumbai with a view to widen the road. The closure was effected pursuant to clause specific to agreement with PWD of Government of Maharashtra. The Govt. has paid Rs 6.16 crores to the company as termination payment.

**Reasons of Cancellations-** The main reasons of cancellation of project are as follows:

- Dispute on widening of road between IRB Pvt, Ltd and Government of Maharashtra, PWD
- Violation of contract agreement by both the company and PWD.

#### (4) Pune water Supply & Sewerage Project-

**Project overview-** In 1996, the Pune's Water supply and Sewerage project of value \$185 million was initiated under the FIRE(D) program. The project was an integral part of a 25-year strategic plan which aimed to gradually extend, to

the total population, a 24-hour water supply and sewerage service through construction and management contracts with a private sector firm. The other details of the project are given below in table-8.

Table-8 Pune Water Supply And Sewerage Project

(Source- Marie-Helene Zerah and Lyonnaise Des Eaux)

Project Name	Pune Water Supply And Sewerage Project
Location	Pune ,Maharashtra State
Financial closure Year	1996
Sector	Water sewerage
Type of contract	Construction And Management Contract
Contract period	25 years
Bidding Process	Competitive Tendering
Cancellation Year	1998
Sponsor name	23.3% grant assistance from GoM 10% from (PMC) Two-thirds from private investments
Funding Partners (Water and Sanitation Program)	Governments of – Australia, Belgium ,Canada, Denmark, Germany, Italy, Switzerland, Norway, Sweden, Switzerland, Luxembourg. Japan, United Kingdom, United Nations development program and World Bank
Investment commitments in physical assets(US\$ in millions)	185
Funding details	Bond Fund(50 million US\$) Loans(75 million US\$) from ICICI Loans(56 million US\$) from HUDCO Housing Guaranty Funds from USAID through the FIRE(D) project

**What went wrong?** In 1997, the local elections in Pune resulted in a change in the composition of the General Body of Elected Councils. This local government council reviewed the project costs and expressed concern that they were too high. The council thought consumers would have to pay too much to ensure that a private operator received a sufficiently high rate of return. The critics began to question the viability of the scheme, process to award the tenders to the private sector and the municipal commissioner had left the project without a local champion due to his transfer, thus the project was opposed by the General Body of Elected Council and the state Government of Maharashtra. The

new municipal commissioner of Pune had decided to cancel the project and ultimately the project was cancelled in 1998.

**Reasons of Cancellations-** The main reasons for the cancellation of the project are as follows:

- The critical reason for project cancellation was the loss of political support from the local and state Government.
- The project was left without a local champion by the municipal commissioner of Pune.

- Lack of transparency in process to award the tenders.
- There was a doubt related to viability of scheme.
- There was a 25% increase in tariffs (Rs 2/cum to Rs2.5/cum).
- There was a 43% increase in annual fees (Rs.175 to Rs250).
- The project cost was too high
  - ❖ Estimated cost was \$106 million
  - ❖ Actual cost was \$185 million
- There was an opposition to high debt burden.

### III. CONCLUSION

In developing neighboring countries India has minimum rate of cancellation of privately financed projects. The lower percentage of cancellation of projects is subjected to good and sufficient working investment conditions for investors and sponsors in different sectors of projects. In India most of projects are cancelled due to loss of political support, high license fees, change in Government's policy and increase in tariffs of charges related to electricity and water supply projects. The loss of political support is the most critical reason of project cancellation.

By the study of this paper, it can be concluded that the minimization of project cancellation depends upon the sufficient Government's support, strong political support, well design and structure of project, capability of sponsor, suitable source of finance, guaranties provided by Government, strong public sector capacity and Robust legal and institutional framework of Public-Private-Partnerships.

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