



National Electric Power Regulatory Authority Islamic Republic of Pakistan

NEPRA Tower, Attaturk Avenue (East), G-5/1, Islamabad
Ph: +92-51-9206500, Fax: +92-51-2600026
Web: www.nepa.org.pk, E-mail: registrar@nepa.org.pk

No. NEPRA/TRF-337/LESCO-2015/6997-6999
May 19, 2016

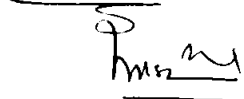
Subject: Decision of the Authority in the matter of Motion for Leave for Review filed by Lahore Electric Supply Company Ltd. (LESCO) against Determination of the Authority for the Financial Years 2015-2016 to 2019-20 Dated March 8, 2016 [Case # NEPRA/TRF-337/LESCO-2015]

Dear Sir,

Please find enclosed herewith the subject Decision of the Authority (38 Pages) in the matter of Motion for Leave for Review filed by Lahore Electric Supply Company Ltd.

2. The Decision is being intimated to the Federal Government pursuant to Section 31(4) of the Regulation of Generation, Transmission and Distribution of Electric Power Act (XL of 1997).

Enclosure: As above


19.05.16
(Syed Safeer Hussain)

Secretary
Ministry of Water & Power
'A' Block, Pak Secretariat
Islamabad

CC:

1. Secretary, Cabinet Division, Cabinet Secretariat, Islamabad.
2. Secretary, Ministry of Finance, 'Q' Block, Pak Secretariat, Islamabad.



**DECISION OF THE AUTHORITY IN THE MATTER OF MOTION FOR LEAVE FOR
REVIEW FILED BY LESCO ELECTRIC SUPPLY COMPANY LIMITED (LESCO) AGAINST
DETERMINATION OF THE AUTHORITY FOR TE FY 2015-16 TO FY 2019-20 DATED
MARCH 08, 2016**

1. The consumer end-tariff for Lahore Electric Supply Company Limited (LESCO), hereinafter called "the Petitioner" pertaining to the FY 2015-16 to 2019-20, was determined by the Authority vide determination dated March 08, 2016. Being aggrieved with said determination, the petitioner has filed a motion seeking leave for review with inter-alia following relief:-
 - i) To revise T&D losses target i.e. 13.85%, 13.35%, 12.85%, 12.35% and 11.85% pertaining to the FY 2015-16 to 2019-20 respectively;
 - ii) To allow the creation of new field offices (divisions/ sub-divisions/ circles);
 - iii) To allow cost of new hiring to staff the new offices, having financial impact of Rs.1,064 Million;
 - iv) To allow cost of replacement hiring amounting to Rs. 800 million;
 - v) To allow segregation of O&M cost into controllable and uncontrollable costs;
 - vi) To allow sufficient repair & maintenance cost;
 - vii) To allow sufficient other expenses cost;
 - viii) To revise the salaries & wages cost;
 - ix) To revise the Weighted Average Cost of Capital (WACC);
 - x) To review the PYA amount;
 - xi) To review the other income i.e. treatment of late payment charges;
 - xii) To allow Z-Factor for extra ordinary events;
 - xiii) Performance Standards be revised;
 - xiv) To revise the Security deposit rates and policy;
 - xv) To reconsider the request for PHPL loans;





- xvi) To reassess the efficiency factor X assessed at 5.9%;
 - xvii) To consider the impact on sale to Industrial consumers on account of provision for RLNG to the textile industry for self-generation;
 - xviii) To rationalize the Peak and off peak rates of Industrial Tariff;
 - xix) The Principle on which new tariff category A-3 General Services has been created be applied to other consumers falling within the ambit of the said principle;
2. Under rule 16(6) of NEPRA Tariff (Standards & Procedure) Rules, 1998, a motion is required to be filed within 10 days, however, the subject motion was not filed within the prescribed time, however, in order to meet with the ends of natural justice, the delay was condoned and the petition was admitted for further process.
3. Notice of the motion for leave for review was served upon the parties to the impugned tariff determination.
4. In response whereof, the intervener M/s Anwar Kamal Law Associates (AKLA) raised the objections that sufficient time has not been provided to file the response; that the tariff should had been determined in July 2015 and with the delayed determination, undue benefits is being given to the DISCOs; that the observations of the intervener is not duly reflected in the impugned tariff determination and that the Investment Plan of the Petitioner was approved by the Authority but details which show the proposal on which the Investment will be made along with its cost-benefit ratio and time-lines to complete such proposal are neither given in the Determination nor are available anywhere else in the public domain.
5. All Pakistan Textile Mills Association (APTMA) file the following objections;
- i. The reference RFO price (Rs.47,981/M.Ton) used by NEPRA for determining monthly reference Fuel Oil Charges component of the Power Purchase Energy Cost is not Justified.
 - a. A World Bank quarterly report on commodity markets outlook issued in January, 2016 has concluded, "All main commodity price indices are projected to decline in 2016 relative to last year due to persistently elevated supplies and, in the case of industrial commodities, weak growth prospects in emerging

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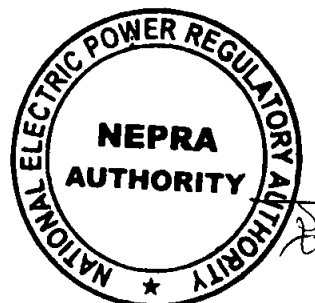
market economies. Energy prices are expected to fall 25 percent from 2015, with oil prices projected to average \$37/bbl in 2016.” The US commodity markets predictions expect the RFO price to range between US\$20-40 in 2016 (January-December).

- b. NEPRA determined actual fuel prices in its FPA determinations for the Months of July 2015 to January, 2016 as compared to its reference monthly fuel prices in its Annex-IV (Power Purchase Cost) of the NEPRA MYT determination in the matter of Petitioner for FY 2015-16, are contradicting to each other as illustrated below:

	Fuel Charges Component of PPC Rs./kWh						
	Jul-15	Aug-15	Sep-15	Oct-15	Nov-15	Dec-15	Jan-16
FPA Determinations	4.3559	3.8546	3.5527	5.5222	5.2383	4.2676	5.8236
MYT Determination (Annex IV)	4.9811	4.7552	5.1217	5.2366	5.0497	5.8619	7.1241
Reference Fuel Cost Overstated	14%	23%	44%	-5%	-4%	37%	22%

- c. NEPRA’s claim that its determination is futuristic that keeps in consideration the future oil scenario is absolute misrepresentation of the facts and misuse of its authority to bulldoze its irrational decision since all major stakeholders’ analysis and market reports have been altogether ignored and no evidence, rationale or oil forecast scenario of NEPRA has been presented in its determination to justify the RFO price assumption of Rs.47,981/M Ton.
- d. Setting a higher fuel cost will result in higher tariff upfront though compensated through FPA later but in the process forces the industry to quote higher costs that make their bids uncompetitive and upfront payment of GST that places unnecessary liquidity pressure on the industry. The DISCOs also face adverse circumstances in months when huge FPA amounts are paid back.

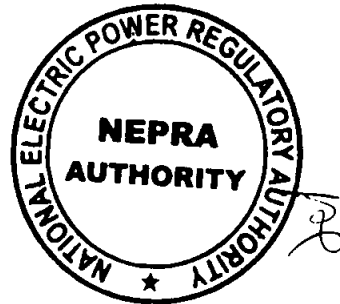
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- e. The RFO price used by NEPRA for reference fuel price cost calculation is grossly overstated, in contradiction of its own earlier determination for Nandipur, FPA determinations and totally in the opposite direction of the fuel price scenario predictions of World Bank and other Market forces.
 - f. The reference fuel oil power purchase energy price be revised downwards using RFO price of Rs.23,000/M.Ton that is not expected to increase in near future as forecasted by the market forces.
- ii. NEPRA's determination of the Petitioner's T&D Loss as 11.75% is highly overstated since;
- a. Determination of the Petitioner's T&D loss target is not aligned to the weighted average T&D loss calculated based on section wise losses indicated in its petition.
 - b. The Asian Development Bank Multi tranche financing Facility deliverable requirement i.e. "Systems technical losses are reduced each year by 10% of the previous year's loss figure" has neither been taken into account by the Petitioner nor by NEPRA in setting the T&D annual Targets.
 - c. Calculation of weighted average T&D Loss at LESCO level based on the voltage level T&D loss determined by LESCO consultant, has been totally ignored by the Petitioner as well as NEPRA. Further the Petitioner has added the voltage level of losses in linear mode and considered its weighted average loss for all customer irrespective of the voltage level on which the Petitioner receive power.

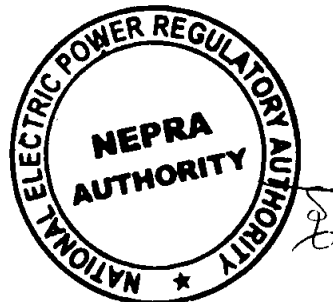
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- d. NEPRA, revised the target of T&D losses as 11.75% for the FY 2015-16 without substantiating how it arrived at this number since the T&D losses determined by the Authority's technical professionals is 9.01%.
 - e. NEPRA's instant determination with respect to power export to others DISCOs at (para 55.1.III.ii) its voltage level technical losses comprising of 1% at 132KV and 5% 11KV (HT) system losses. This means if LT loss of 3.09% as claimed by the Petitioner on the basis of its technical study is added to 132 & 11 KV T&D loss, the total T&D losses of the Petitioner comes to 9.09%.
 - f. Therefore, the NEPRA determined target of 11.75% T&D loss for 2015-16 should be corrected downwards and should not exceed in any case beyond the level of 9.8% as determined by the NEPRA for FY 2013-14. Proper calculation of the weighted average T&D loss based on the voltage level losses and voltage level power distribution mix should also be provided in the determination.
- iii. NEPRA in its determination continued with its previous practice of recovering export wheeling cost from the Petitioner's customers by keeping it a part of the total revenue requirement used for determining the tariff rates. NEPRA did not determine the amount of wheeling charges for export of power to other DISCOs based on its own formula and excluded it from total revenue requirement to be recovered from the Petitioner customers. Therefore, NEPRA should work out the amount of wheeling charge for the time being in accordance with its own crafted formula and exclude it from the total revenue requirement to be recovered from the Petitioner's Customers. This will put pressure on the Petitioner to ensure billing of the wheeling charges for export of power and avoid its loss if not billed.
- iv. NEPRA's approved investment plan for the Petitioner is too optimistic and difficult to implement since:

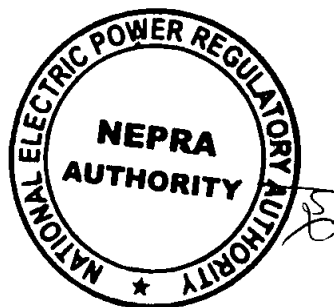
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- a. NEPRA determination reveals incapability of the Petitioner that could implement only 52%-76% of the approved investments programs in the last 3 years, but NEPRA still allowed an unprecedented mega size investment program over a 5 year program. This may not be acceptable to the new investor if LESCO is privatized as scheduled and thus the Regulator's determination in this regards is a matter of serious concern.
 - b. The Petitioner has expressed its total inability to achieve the performance targets determined by NEPRA, however, if all these conditions are to stay even after the approved investments, then the subject investment program should not be included in Rate base for RORB determination.
 - c. NEPRA determined the performance targets to be achieved as result of the approved investments in the five year period, but did not determine the course of action including relief to the customers in case the NEPRA set targets are not achieved after implementing the approved investments by the Petitioner.
 - d. Therefore, NEPRA is requested to ensure that investment size is rational. RORB part of the investments failing to achieve determined performance targets should be withdrawn from the tariff as negative prior year adjustment to ensure that the requisite investments are not made to merely enhance the Distribution Margin.
 - e. The Petitioner has mentioned that the sale of power to industrial customer will decline since industrial customers are expected to rely more on self-generation. Therefore, NEPRA, should ensure that power sale to industrial customers has taken into account the negative growth as expected by the Petitioner, and accordingly the power purchase cost is adjusted to eliminate any overstatement. The cross subsidy from industrial customer be kept at zero percent to keep the power rates attractive for getting supplies.
6. The concerns so raised by the Interveners were forwarded to the Petitioner, who has provided the following rejoinder;
- ✓ Regarding setting of reference RFO prices, the Petitioner has stated that as already highlighted during the tariff hearing proceedings and the review motion hearing proceedings, the multiyear tariff regime is futuristic in nature and takes into account the most likely and stable scenario of fuel prices as reference. Even the APTMA has been agitating and proposing in the past, while challenging the FPA in almost all the High Courts and up till the Supreme Court, to use a higher Fuel price as base so that its members are not

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burdened to pay the positive adjustment of FPA on the ground that the goods manufactured by use of electricity at a certain price are sold when the positive adjustment of FPA is received therefore they cannot recover/claim the upward difference from their clients.

- ✓ As such recovery of billions of rupees as power purchase cost remained suspended for years spent on account of litigation filed by APTMA and its members for which no relief was given to the Petitioner.
- ✓ Moreover, even if the prices quoted by APTMA (unfortunately APTMA has taken fuel price without freight and other related costs) do remain stable at existing level in the coming months, the petitioner is not going to benefit from high reference fuel price as the variation will have to be passed on to the consumers in any case. So the request of the intervener is not pragmatic.
- ✓ On the issue of T&D losses, the Petitioner has submitted that it has serious reservations about target of line losses fixed by the Authority. Our main concerns are summarized as under:-
 - Existing state of affairs, where the actual line losses during 2014-15 were 14.10% not considered.
 - The target for FY 2015-16 is being fixed at the end of third quarter of this financial year;
 - Proposed reduction in losses of 2.25% was actually based on the IGTDP and DIIP (investment plan), duly considered & approved by the Authority.
 - Despite approving the IGTDP/DIIP, the Authority fixed 11.75% as base figure of losses target for FY 2015-16. This reduction of 3.75% is not justified.
 - On one hand, Authority, in Para 31.16 has acknowledged the paramount principle of multi-year tariff regime that existing state of affairs of the utility is considered as benchmark for future efficiencies and on the other hand the existing state of affairs of LESCO w.r.t. losses has not been considered.
 - Reduction in losses of 3.75% as determined by the Authority, would require further colossal investment and commensurate time for implementation.
 - The approved investment plan of 93 Billion is not entirely meant for reduction in line losses. Out of Rs 93 Billion total investment, Rs 30 Billion

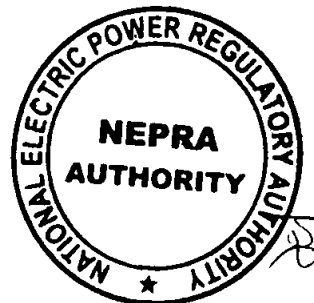
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is meant for AMI project, which will help to control the administrative losses and not the technical losses.

- Investments already allowed by NEPRA in the previous years for STG, DOP/ELR, barely permitted the Petitioner to keep up with the load growth and increase in number of consumers has nullified the impact of such investment hence it will be unjustified to say that the past investment should have reduced the losses to the extent of 11.75%.
- Delay in procurement on account of sector level litigation could not produce desired result.
- The existence of hard areas in LESCO's service territory has not been appreciated. These are the real cause of administrative losses. Even NEPRA has been acknowledging the administrative losses in its determination upto 2012-13.
- The unrealistic nature of the target losses is evident from the fact that the Authority has fixed 8% loss target for FY 2019-20. If 2.17% of transmission loss, as per study, is deducted there-from then the remaining loss comes to 5.83%, which is extremely unrealistic on the face of it.
- The statement of APTMA whereby it attributed that LESCO committed to reduce technical losses by 10% per annum on account of ADB Multi Tranche-1. The Petitioner does not directly deal with ADB for such funding and it falls within the domain of Federal Government. As such the statement "Systems technical losses are reduced each year by 10% of the previous year's loss figure" was for all the distribution companies and not specifically for LESCO for which ADB has provided MFF-1. As far as LESCO is concerned under the ADB Tranche-1 most of the sub projects were augmentation of power transformers and addition of transformers at the existing 132kV substations of LESCO and construction of one new 132 kV substation. It is submitted that with the augmentation and addition of power transformers there is no significant improvement in the technical loss reduction rather it enhances the power transformation capacity of the grid stations which is essentially needed to provide relief to the overloaded power transformers as well as to accommodate the load growth.
- Losses evaluated by the consultant are for entire transmission and distribution system and not for individual consumers according to their supply voltages.

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- ✓ Regarding wheeling charges, the Petitioner is of the view that wheeling mechanism is not applicable on export of power to other XWDISCOs. Moreover, its not only export of power but import and exports are simultaneously happening therefore, this point is uncalled for.
- ✓ The Petitioner, on the issue of withdrawal of RoRB part of Investments, owing to failure to achieve the performance targets, has mentioned that perhaps whole of the FY 2015-16 would lapse before the present tariff become effective. Secondly, the commentator's suggestion is completely in contrary to the multi-year tariff regime.
- ✓ Regarding sale of power to Industrial Consumers, the Petitioner has submitted that the impact of non/less consumption by industrial consumers due to their enhanced reliance on self-generation because of availability of gas/RLNG would increase the per unit revenue requirement for which consumers in other categories of tariff would suffer. In view of this LESCO has proposed following measures, which should be approved to compensate the impact on consumers in other tariff categories:
 - a) Amendment in the "Billing Demand" clause by reviving the earlier clause of 50% of the Sanctioned Load or the actual maximum demand whichever is higher;
 - b) Upward revision of Fixed Charges in the Industrial Tariffs
- ✓ On the issue of Investment Plan, the Petitioner has stated that necessary project time lines and the cost benefit ratios are available in the Distribution Integrated Investment Plan (DIIP). As regards the improvement in system, it is submitted that the investment made in the past barely permitted the utility to keep up with the load growth. However, execution of the proposed / approved investment plans will not only improve the technical losses of transmission and distribution but also enhance the reliability and system capability, also keeping pace with the robust customer growth.
- ✓ Regarding non-transparent and non-prudent working in the power sector, the Petitioner has submitted that the comments of the intervener are uncalled for as the regulatory proceedings of any tariff filing are conducted through well participative hearing sessions and exchange of information/ documents. Particularly the AKLA have participated in the ongoing MYTP hearings three times through their written comments. This speaks of the fairness and transparency of the defined process. The petitioner also has high regards for

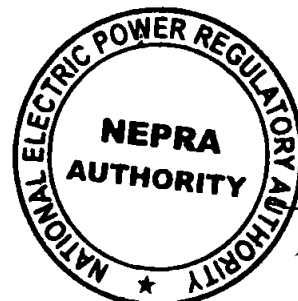
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the valuable contribution by the interveners as all these processes lead to improvements in the sector.

7. In order to consider the motion for review, a hearing was scheduled for 6th April, 2016 for which due notices were served upon the parties. On the date of hearing, Chief Executive Officer of the petitioner company was present along-with his Technical and Financial Team. The Intervener M/s APTMA also attended the hearing, however, no representation was made on behalf of AKLA.
8. Arguments heard and record perused. Though there was no representation from the intervener, yet the written concerns so received have been deliberated. Regarding provision of sufficient time to respond to the Notice and the data provided, the Authority observed that as per rule 16 (7) of the NEPRA (Tariff Standards & Procedure Rules 1998, Parties to the proceedings shall be afforded a reasonable opportunity, orally or in writing as deemed fit by the Authority, to respond to a motion for leave for review. As per the available record, the Intervener was emailed the notice of hearing well before the hearing date i.e. on 1st April, 2016. In view thereof, the Authority considers that sufficient time was allowed to the parties to respond to the MLR. AKLA raised the issue of delayed submission of tariff petition and late determination by the Authority in its Intervention Request against the tariff petition filed by the Petitioner, which has already been addressed at para 4.2.2, 8.22.1 and 8.22.2 of the determination dated March 08, 2016. AKLA while claiming that its contentions have not been addressed, has not referred any specific issue. The Authority has discussed its comments in detail under para 4.2, 5.3 and 8.22 of the determination dated March 08, 2016. On the point of Investment Plan, in the impugned determination, vide paras 40 to 50, it was discussed in detail with respect to the target projects to be carried out in the tariff control period along with their completion time lines under each head of investment i.e. STG, DoP expansion & rehabilitation, ELR, CIP, Civil Works and HR Improvement Plan.
9. As regards submissions of the APTMA, the same are discussed as under:-
 - a. The Authority after careful review of the Intervener's concerns on the assessment of reference fuel cost component is of the view that it has determined references for the Petitioner based on the best estimates, keeping in view the past trends and available information on the future trend of the fuel prices. The Authority while projecting the future RFO prices was cognizant of the decreasing oil prices scenario therefore the new reference for RFO was assessed as an average of Rs.47,981 /M.Ton instead of previously determined average of Rs. 65,000 / M.Ton. The Intervener stated that the Authority's argument of determining fuel price references keeping in view the futuristic approach is absolute misrepresentation of the facts and misuse of its authority and referred

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World Bank's quarterly commodity markets outlook (issued in January , 2016), in order to justify its claim. The Authority brings on record that the same World Bank's commodity report issued in July, 2015 covering the control period projected crude oil as USD.57/b. Further, Independent statistics and analysis of the US Energy Administration, in its short term energy outlook (STEO) issued in July 2015, projected WTI crude oil rates as USD.59/b for the month of July and showed an increasing trend up to USD.66/b. Based on the latest projections provided by the aforementioned reports and the analysis of Intervener, whereby it claims that the future RFO prices would not increase more than Rs. 23,000/M Ton (based on USD. 30/b) has already proven wrong as the WTI crude oil has already touched USD. 42.17/ b (on 12th April, 2016). Here it is pertinent to mention that it is not Brent Oil (for which a price of \$ 34/b is projected), which as per the Intervener is USD 5 /b higher than the WTI.

- b. The Authority being cognizant of the fact that every projection has some limitation and it is not possible for anyone to apprehend and foresee all the factors causing variations in fuel prices, owing to which the mechanism of monthly fuel price adjustment is introduced so that neither the consumers nor the DISCOs should take the undue benefit of the variation in fuel prices, since the Authority cannot change its projection on mark to mark basis. The FPA mechanism ensures that in case of any variation in fuel prices from the reference prices, the impact of the variation is either recovered from the consumers or the benefit of the same is passed on to the consumers through monthly FCA mechanism. Further, the argument the reference fuel price determined in the case of Nandipur Project is contradictory to the Authority's determined fuel references is not correct as the determined RFO price of Rs. 47,981 / M Ton, is an average of twelve month's projection of RFO's future prices which are subject to review as per the approved Methodology, whereby the RFO reference price set for Nandipur Project would continue same for the life of the project. Thus, the perspective of setting both references are different. In view aforementioned discussion, the Authority considers that APTMA's observation in this regard is not valid. However, the Petitioner's input in this regard was very valuable and is strongly encouraged to participate in the future proceedings.
- c. The Authority on the point of T&D losses observed that the weighted average T&D loss of 9.40% worked out by APTMA is not correct being based on incorrect sales mix and therefore cannot be relied upon. Further, the referred reduction of 10% is from the actual loss figure is an operational target from the lender and cannot be construed as a regulatory target. The Authority in its determination in the matter of the Petitioner with respect to the Motion for Leave for Review filed against the





Authority's decision pertaining to the FY 2013-14, has elaborated on the rationale for the assessment of 11.75%. In addition to aforementioned, the rationale for allowing a T&D loss target of 11.75% has also been discussed in detail and with reasonable clarity under para 39 of the MYT determination in the matter of the Petitioner, dated March 08, 2016.

- d. The issue of wheeling charges has already been addressed under para 51.2 of the MYT determination of the Authority dated March 08, 2016.
 - e. The rationale / basis for allowing the investment plan of Rs.93,832 million has been discussed in detail under the issue of "Investments" under para 40 to 50 of the aforementioned determination dated March 08, 2016. Here it is pertinent to mention that the Authority has incorporated a true up mechanism whereby each year, the amount of actual expenditure would be considered and any undue benefit drawn by the Petitioner would be adjusted and vice versa. Further, the Authority would also extensively monitor the execution of allowed investments.
10. As regards, submissions of the petitioner, the same are being discussed under respective heads as under:-
11. **Transmission and Distribution Losses**
- 11.1 The Petitioner regarding Transmission and Distribution (T&D) losses has stated that although the Authority allowed the requested IGTDP as submitted by Petitioner however, it reduced the limit of T&D Losses by determining 11.75% as base line for setting future T&D losses target during the control period. The Petitioner further contested that the Authority denied the proposed reduction of 2.25% and determined 3.75% reduction in losses over the five year's control period.
- 11.2 The Petitioner on setting the base line of T&D losses as 11.75% submitted that;
- ✓ The Authority has ignored actual line losses of 14.10% for FY 2014-15, which were projected at 13.85% for the FY 2015-16.
 - ✓ The investment, planned during the tariff control period, is not entirely meant for reduction in line losses. Out of total investment plan of Rs. 93 billion, the amount of Rs 30 billion is purely meant for execution of AMI project over the tariff control period which will help to control the administrative losses only (approx.. 1.5% currently) and not the technical losses.

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- ✓ The proposed reduction of 2.25% in losses is strictly based on the IGTD and investment plan (DIIP), duly considered and approved by the Authority. Therefore, reduction of 3.75% determined by the Authority, is not plausible because in order to achieve the same, further planning, investment and time for implementation thereof would be imperative.
- ✓ The investments already allowed by the Authority in the previous years for STG, DOP/ELR, is very less as compared to the investment allowed in the instant case. Hence it shall be unjustified to say that the past investment should have reduced the losses to the extent of 11.75%. Moreover, the impact of increase in load growth and number of consumers coupled with the high prices of electricity in the past has nullified the impact of such investment. The investments in the past hardly permitted to keep up with the load growth and resultant increase in number of consumers. The high prices of electricity in the past coupled with overall economic condition of the majority of consumers were major impediments in controlling of theft.
- ✓ The number of consumers per sub-division increased beyond the number for which a sub-division was designed and staffed e.g. Bedian Road Sub-division which has 50,000 plus consumers with 42% shortage in meter reading staff. Creation of new field offices (sub-divisions, divisions and circles) to cope with such increase in the number of consumers required fresh hiring. Hiring / recruitment, to replace the retired employees as well as for staffing new field offices, could not be done initially on account of the overall ban on recruitment imposed by the Government. Later on, when the Government permitted recruitment, the Authority has continuously been disallowing the cost thereof. Recently, the Authority permitted all XWDISCOs, including the Petitioner, that while creating and staffing the new field offices, to follow PEPCO criteria for the same but strangely when the Petitioner acted upon the same, the Authority, in the instant determination, has disallowed all such costs.
- ✓ LESCO, in compliance of the directions of Authority, engaged the services of a well-known expert for conducting a study of losses of all of its feeders under the TOR duly approved by the Authority. The partial results of study completed till that time was submitted to the Authority, which has been admitted by the Authority as a representative sample. Despite acknowledging the sample as a representative one, the result thereof has not been appreciated and considered.

11.3 The Petitioner further on the fixing of 11.75% losses as baseline submitted that for the FY 2015-16, the Authority did not consider the following important factors: -

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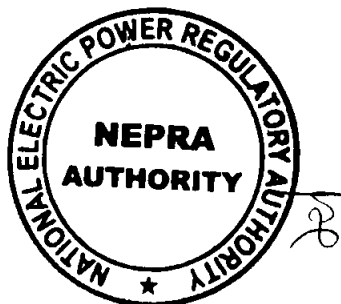
- ✓ The target for the FY 2015-16, is being fixed at the end of third quarter of FY 2015-16;
 - ✓ The determination is yet to be notified and as such, will only become effective, applicable and operative, in terms of applicable law, once the same is notified;
 - ✓ This determination would actually become effective and operative when the FY 2015-16 would actually be over;
 - ✓ No time will be left for recovering the revenue requirement determined by the Authority for FY 2015-16 and implementing the IGTD and the investment plan for FY 2015-16.
 - ✓ Decrease in losses from 14.10% (FY 2015-16) to 11.75% (determined for FY 2015-16 and as baseline) comes out to be a reduction of 2.35%, which is not only too aggressive but also impossible as the FY 2015-16 will elapse before effectiveness of this determination.
- 11.4 The Petitioner also stated that existence of hard areas in the Petitioner's service territory has not been considered, which has an impact on overall losses not less than 1.5%. The Authority has fixed 8% loss target for the FY 2019-20 and if 2.17% of the transmission loss, as per study, is deducted therefrom the remaining loss comes to 5.83%, which is extremely unrealistic on the face of it. The Authority while reducing the target loss has taken different stances whereby on one hand in paragraph 39.20 of the instant tariff determination, the Authority acknowledges that the study included sufficient number of urban and rural feeders, representing the overall consumer mix and loading conditions and accordingly stated that the study & software used were acceptable however on the other hand the target losses have been fixed in complete disregard of this study.
- 11.5 The Petitioner thereof, requested that the hard facts and the ground realities be kept in view while fixing the target of losses, especially in a locked period of five years, as it poses serious question for the Petitioner's commercial viability.
- 11.6 The Authority has discussed in detail the issue of T&D losses under para 39 of the MYT determination of the Petitioner for the FY 2015-16 to FY 2019-20 wherein complete rational / basis have been provided for the target level of T&D losses. Further, the plea of the Petitioner for not having sufficient time to achieve the target level of T&D losses of 11.75% is not maintainable as the level of T&D loss target is the same as for the last year, thus, in fact the Petitioner was aware of the target of 11.75% before the start of the FY 2015-16. The Authority also feels that the Petitioner statement of controlling only the administrative losses of 1.5% by the implementation of AMI project of Rs. 30

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billion is imprudent when compared with PC-1 of the project (submitted with the tariff petition of FY 2014-15), which clearly mentions that the AMI project along-with other benefits will also result in overall energy saving by 2% as a whole and 5.21% in the circles under the projects. The Authority also believes that the remaining amount of Rs. 63 billion is quite sufficient to achieve the targeted level of T&D losses i.e. 1.75% (3.75% less 2% with the help of AMI Project) keeping in view that it includes rehabilitation, energy loss reduction and expansions projects.

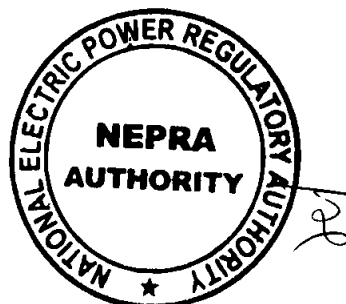
- 11.7 The Authority further in order to evaluate the quality of studies conducted by the Petitioner's Consultants, held meetings with the representatives of the consultants wherein it was observed and also agreed by the consultants that losses in an electricity distribution company can be accurately measured only through metering equipment at different voltage levels from high voltage (132 kV) to the consumer-end and the results of the studies depend on the set of approximations which can exactly replicate the actual operational conditions over different periods. It is also observed that the results of the studies depend on the suitability of the software being used for the studies, size of the database and comparing results of the study with actual in-field monitoring and data collection. The consultants used PSSE software for analyzing 132 kV losses. PSSE software is a standard software for simulation studies however it was noted that system operational conditions under different periods were not modeled adequately. For 11 kV feeder level studies, Synergy software is being used which is a refined version of FDRANA which was used by the XWDISCOs earlier, for evaluating loading position of individual feeders for making improvements and/or induction of new feeders. It is observed that although the software may allow accurate modeling of a feeder it cannot be considered as ideal software for calculating the losses of all feeders collectively. The XWDISCOs did not appear to have clear criteria for selecting sample feeders for the studies as only general guiding instructions were provided to the consultants by the XWDISCOs. For the low voltage analysis also, it was noted that the XWDISCOs and the consultants did not develop a clear criteria and guidelines for selecting the samples. Most importantly the consultants failed to corroborate its results by putting up metering equipment and measuring actual losses over selected circuits at high voltage and low voltage levels. It was also noted that modeling of loads at different voltages is also very important in addition to the accuracy of data. No clear statements were available that the XWDISCOs carried out detailed scrutiny of the data and modeling of loads. The Petitioner in view thereof is directed to address the aforementioned observations of the Authority while submitting the completed study.
- 11.8 Based on the aforementioned discussion, the Authority considers that the Petitioner has failed to submit any new evidence / rationale in support of its claim which would provide basis for the Authority to revise its earlier decision in this regard, hence the Petitioner's request is rejected.





12. Recruitment Plan & New Divisions/Sub Divisions

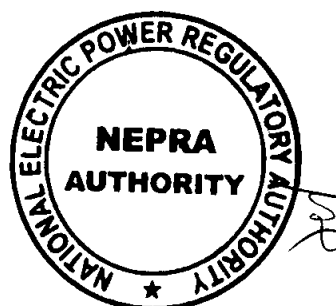
- 12.1 The Petitioner submitted that the Authority, in its MYT determination, has reverted its previous decision of allowing the creation of new circles, divisions and sub divisions with the remarks that decision was specific for single year tariff regime, whereby each year its financial and qualitative impact may be evaluated/analyzed and that under multiyear tariff regime the instant decision becomes irrelevant as the existing state of affairs of the Petitioner is considered as benchmark for future efficiencies.
- 12.2 The Petitioner has requested to allow cost of creation of new field offices as it is in compliance of the yardstick (i.e. for creation of new field offices sub-divisions/ divisions/ circles) as directed and allowed by the Authority.
- 12.3 The Petitioner also submitted that the Authority disallowed the requested recruitment of 4,545 personnel having an impact of Rs.1,064 million apparently on two grounds; Petitioner has not got approved the yardstick of employees from Authority and has not provided the quantified benefits of fresh hiring such as improvement from the exiting state of affairs nor it include the future targets, rather it gives some generic statements e.g. better service to consumer, system will improve, efficient utility functions etc.
- 12.4 The Petitioner regarding replacement hiring certificate stated that the auditor is working on this assignment but the quantum of work involved, due to lack of data in soft form, requires more time to satisfactorily complete the job. The Petitioner also provided a letter from the auditor in this regard.
- 12.5 The Petitioner delineated that all the XWDISCOS came into being upon restructuring of WAPDA, whereby the assets, business and employees of WAPDA were transferred to these XWDISCOS under various agreements such as the Business Transfer Agreement and the Operation and Development Agreement by protecting the terms and conditions of such employees. Later on the XWDISCOS offered employment to the said employees as per the transitional phases envisaged under the Power Sector Restructuring Plan duly approved by the Council of Common Interest in 1993. The Petitioner informed that all the rules and procedures of WAPDA were made applicable to the newly incorporated XWDISCOs until they have their own rules and regulations in place or the regulator frames the rules and procedures. The Petitioner further mentioned that one of the said rules was the SOP dated 08.08.2002 whereby the yardstick for creation, development and maintenance of the operational establishments was revised and this is why the Authority, by letter No. NEPRA/R/TRF-100/12654-63 dated August 26, 2015, directed Petitioner, including all other XWDISCOs to





follow the yardstick/SOP dated 08.08.2002 of WAPDA for creating new Sub Divisions, Divisions and Circles. Secondly, it is also understood that for this reason the Authority has allowed the cost of working strength as well as retired ones to LESCO, therefore, rejecting the cost of fresh hiring on the basis of absence of yardstick approved by the Authority is not justified.

- 12.6 The Petitioner argued that the Authority while rejecting the cost of new hiring has not considered that new grid stations, field offices and infrastructure that would be added pursuant to the approved IGTDP and investment plan and the Petitioner would be requiring additional manpower to operate and maintain the same.
- 12.7 The Authority after going through the submissions of the Petitioner is of the view that the Petitioner has not fully comprehended the justification given by the Authority in para 31.12 to 31.20 of the MYT determination, wherein it has been mentioned that the Authority had been directing the Petitioner in its previous determinations for justification of additional hiring with proper rationale and comprehensive recruitment plan based on best utility practices and its quantified benefits in terms of improved customer service, losses reduction, improvement in recovery etc., along with a comparison of existing state of affairs, which the Petitioner failed to do so.
- 12.8 The Authority never decided anything against the rights of the employees which were transferred to the newly created XWDISCOs and their rights were protected, owing to which the Authority kept on allowing the inflationary increases over incurred O&M costs. Thus, the endorsement of the Authority was to the extent of "cost" of then existing employees only transferred to the newly created XWDISCOs that is the reason why the Authority principally decided to allow the replacement hiring cost with the condition of provision of certificate from the Auditor. The certificate also establishes the movement in "costs" and the same it allowed (as it was treated in the case of the Petitioner). The Authority considers that the notion that since the aforementioned employees were initially recruited on the WAPDA yard stick hence the yard stick also stands approved, is not correct as the Authority has not carried out any due diligence on the referred yard stick. That is the main reason that the Petitioner was directed in the past, to get its yard stick approved from the Authority, in case it intends to carry out any additional hiring. It was further directed that the proposed yard stick must be based on the best utility practices including the exiting state of affairs. The Authority has always emphasized on the best utility practices and exiting state of affairs as it is of the firm view that since the referred yard stick was approved way back decades before and totally ignores the technological advancements in

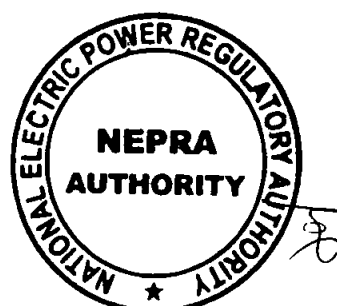




terms of IT and Engineering during that period. The direction was never complied by the Petitioner.

- 12.9 Since the Petitioner has failed to provide any new evidence / information in support of its request, therefore, the request of the Petitioner to allow additional hiring cost is not accepted.
- 12.10 The issue regarding creation of operation sub-divisions, divisions and circles was raised by the Petitioner in its Tariff Petition for the FY 2013-14. The Authority before making any decision of the issue decided to have separate presentation from the Petitioner in this regard.
- 12.11 The Petitioner gave detailed presentation in July 2014 and built up its case by stating that the excessive number of consumers merit creation of new circles.
- 12.12 The Petitioner did not submit any details of financial cost involved with the proposal. However, it enlisted following benefits of creation of new circles;
- Better Customer Service;
 - Improvement in technical system;
 - Decrease in customer complaints;
 - Improvement in Power supply continuity;
 - Efficiency in utility function and utility practices;
 - Reduction in Administrative losses;
 - Reduction in work burden on employees;
 - Improvement in Recovery;
 - Improvement in LESCO image.
- 12.13 During the presentation, the claimed benefits were discussed at length. The Petitioner also requested for additional manpower for the new circles, divisions and subdivisions, whereby it required 60 staff members for each sub-division (including 47 technical staff members and 13 general) .
- 12.14 The Authority made the creation of circles/ divisions/ sub-divisions an issue while determining the consumer end tariff for the FY 2014-15 and all the distribution companies were provided opportunity to submit their comprehensive

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proposal in the matter along-with evidence to justify the need of creation of any new operational and administrative units for approval of the required cost.

- 12.15 The Authority after careful evaluation of the Petitioner's proposal considered it beneficial for both i.e. for the Petitioner's own operational management and for the consumers as well. Accordingly, the Authority accepted the proposal principally, however, directed the Petitioner to send the cost estimates of the entire project to the Authority along with the completion timelines and quantified benefits not later than 30th June, 2015 also decided to closely monitor the project to check if it is achieving the claimed advantages. Consequently, the Petitioner was directed to send quarterly report of progress made on creation of new circles w.e.f. 30th June, 2015.
- 12.16 The Petitioner during its MYT determination process informed the Authority that it created new subdivisions in pursuance of Authority's tariff determination for FY 2014-15 and letter No NEPRA/R/TRF-100/12654-63 dated August 26, 2015. The Petitioner further stated that the process of creation of new circles and divisions was planned to be completed soon. The summary of financial impact of new hiring and creation of new division/ subdivision as submitted by the Petitioner is as under:

Description	Mln. Rs
Estimated Impact of 18 sub-divisions – Allowed by NEPRA	323
Estimated Impact of 13 additional sub-divisions – Approved by BOD	234
Estimated Financial Impact of Other Recruitments	507
Total (For 10 month of current Financial Year)	1,064

Further, the Petitioner requested to allow in the base year the cost of creation of new circles and division as detailed below:

Description	Recurring (Mln. Rs)	Non. Recurring (Mln. Rs.)
Estimated Financial Impact of 2 Circles	67	27
Estimated Financial Impact of 6 Division	15.60	115.75
Estimated Financial Impact of 31 Sub Divisions	20	124

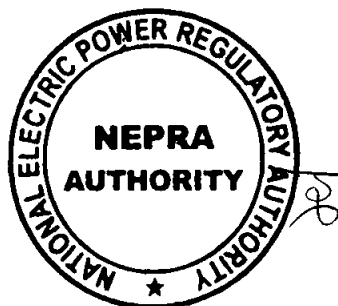
- 12.17 The Authority in its MYT determination dated March 08, 2016 allowed the cost of civil works in this regard. However, the Authority evaluated Petitioner's request regarding O&M cost of new circles/divisions /sub-divisions in the context of transitioning from Single year to Multiyear tariff regime and the anticipated change in management through the ongoing privatization program. The





Authority also considered that allowing creation of new circles / divisions /sub divisions was decision specific under single year tariff regime, whereby each year its financial and qualitative impact were to be evaluated/analyzed. Under multiyear tariff regime the instant decision becomes irrelevant as the existing state of affairs of the Petitioner is considered as benchmark for future efficiencies. Further, keeping in view the existing management change whose prime objective would be to bring efficiency may come up with an idea which would may render the whole idea of creating new circle obsolete. The Authority further felt that in the era of technological advancements, every effort needed to be adopted to get the benefit of technology to bring efficiency through reducing reliance on more man power. Thus, keeping in view the arguments with respect to management change, multiyear tariff regime and the fact that the Petitioner failed to comply with the Authority's direction, the Authority decided not to include the requested cost as a part of reference cost for future increases in the Petitioner's MYT determination dated December 31, 2015.

- 12.18 The Petitioner in the MLR has submitted that its existing Circles/ Divisions and sub-divisions are overburdened due to increase in number of consumers over the period and therefore to serve the consumers in a better way, creation of new circles/ divisions/ sub-divisions is imperative. The Authority understands that managing higher number of consumer with minimum resources could only be possible through heavy investment in advance technologies and by applying out of box thinking, which primarily is attributed to the private sector. Further, if the process of privatization gets delayed; the consumer's suffering due to current situation of circles/ divisions/ sub-divisions would increase. The Authority is also cognizant of the fact that the Petitioner has already created new Sub Divisions. In view thereof the Authority has principally decided to allow the Petitioner to create new circles /divisions / subdivisions. However, allowing upfront O&M cost regarding creation of new circles, divisions and subdivisions, without having the progress reports in not in the interest of consumers. The Authority understands that it will be in a position to adjudicate on the issue once the Petitioner provides details of the actual cost incurred in respect of creation of new circles, divisions and sub-divisions and substantiates the same with the quantified benefits achieved. Accordingly, the Authority has decided to carry out a mid-term review of the Petitioner's O&M cost to the extent of creation of new circles, divisions and sub-divisions only. The mid-term review would be carried out in case if the ongoing privatization program is deferred and Petitioner remains in the Public sector.
- 12.19 The Authority will evaluate the cost incurred by the Petitioner on the grounds of prudence, regarding creation of new circles, divisions and sub-divisions from FY 2015-16 till the time the Authority carries out its midterm review. If the





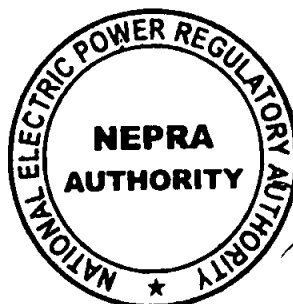
Petitioner manages to prove the prudence of the cost, the Authority may consider allowing the same as prior year adjustment and may include the same in the base cost of the Petitioner for the remaining control period.

12.20 The Authority will assess the cost incurred by the Petitioner regarding creation of new circles, divisions and sub-divisions in the midterm review on the principal of prudence. The Authority will assess the prudence of the cost based on the following parameters in addition to what has been discussed above for future increase as per consumer end tariff methodology.

- Reduce the duration of interruptions by reducing travelling time for repair and maintenance crews;
- Reduce the frequency of interruptions by improving the quality of line monitoring and maintenance;
- Reduce the extent of commercial losses by increasing the presence of field staff;
- Reduction in customer complaints;
- Better Customer Service in terms of reduction in complaint handling time;
- Improvement in technical system;
- Improvement in Power supply continuity;
- Reduction in Administrative and technical losses;
- Improvement in employees productivity;
- Improvement in Recoveries;
- Reduction in travelling and vehicle costs;
- Efficiency in utility function and utility practices;
- Improvement in Petitioner's image

12.21 The Authority is of the view that the Petitioner before taking any such decision in future, shall evaluate all the options arisen due to technological improvements and regulatory advancements over the period.

12.22 While creating the new circles/ divisions/ sub-divisions, the Petitioner must explore the technological advancements and outsourcing options rather than by



simply relying upon the inherited yard stick of WAPDA/ PEPCO which was approved way back.

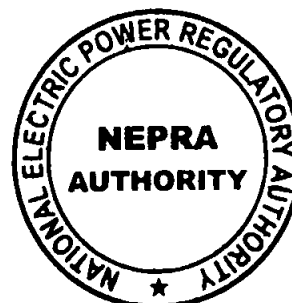
12.23 Regarding replacement Hiring certificate, the Authority in view of non-compliance of its direction regarding the provision of replacement hiring certificate from the Auditor, did not allow the replacement hiring cost of Rs.800 million in the base expense for the FY 2015-16. However, in view of the submissions of the Petitioner and the fact that the Petitioner's reference / base cost is going to be fixed for a period of five years, the Authority has decided to allow extension in time to the Petitioner by December 31, 2016 for the submission of the required certificate. It is however clarified that the Authority as per its previous decision is not changing the already assessed base expense. Its only when the Petitioner would provide the certificate, the Authority may change the base expense of salaries & wages prospectively.

13. Bifurcation of Operations and Maintenance (O&M) Cost

13.1 The Petitioner stated that in its MYT petition it proposed to bifurcate the O&M costs into controllable and uncontrollable costs in order to make a distinction between the costs that can be controlled (or influenced) by the Petitioner and be assessed for efficiency gains and other costs that were external and/or not under its control (or influence). The Petitioner has requested to allow the bifurcation of O&M costs in order to fairly assess the efficiency gains and derive a fair revenue allowance for each year of the tariff control period. The Petitioner also argued that lack of segregation of O&M costs would limit the Petitioner to absorb costs only to the extent of CPI-X in the tariff and the remaining costs would effectively impact the returns to the Petitioner.

13.2 The Petitioner further stated that the uncontrollable costs include NEPRA's licensing fees, rent which is subject to terms of rental agreements, collection expenditure and software licensing fees and increases in salary and wages relating to any GOP directive which it cannot influence and has been included in the base year and as per its MYT determination, it has to bear the risk of future fluctuations of such costs along with the opportunity for optimizing the overall costs as per the MYT methodology. The Petitioner argued that certain uncontrollable costs are unavoidable in the normal course of business and cannot be influenced by the entity. The Petitioner also argued that under an incentivized MYT regulation in international markets, such as the CPI-X methodology that the Authority has approved under the guidelines for determination of consumer end tariff (Methodology and Process), 2015; uncontrollable costs are separated from the costs that a distribution utility can influence (controllable costs) so that the utility is only assessed for efficiency gains based on the costs that it can control and can achieve efficiency gains from. The Petitioner requested to make sure that the essence of the incentivized regulation is maintained and the utility may not be required to achieve the efficiency targets on non-controllable/external costs, which by

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definition it cannot influence. The following costs have been classified as uncontrollable costs by the Petitioner;

- i. NEPRA license Fee
- ii. Rent, which is subject to terms of rental agreement
- iii. Increase in costs relating to any GoP directive which LESCO cannot influence.

- 13.3 The Petitioner also requested that the non-controllable costs may be allowed on actual basis and be trued up annually, based on the evidence of expenditure submitted by the Petitioner to the Authority.
- 13.4 The above concerns raised by the Petitioner in the review motion is already addressed with the clear understanding by the Authority in para 31 of MYT determination. The Authority is of the view that NEPRA's licensing fees is immaterial i.e. only 0.15% of the allowed O&M cost and due to its materiality the Authority does not see any significant risk on the part of the Petitioner and had therefore decided not to consider it as an uncontrollable cost.
- 13.5 Regarding the issue of rent, the Authority has already discussed the matter in detail in para 31.40 of the MYT determination.
- 13.6 The point of increase in O&M cost due to Government directives, becomes irrelevant under a Privatized scenario since the Petitioner would be having its own independent board, free to exercise all powers given to it under the Companies Ordinance 1984 to appoint and determine the term and conditions of its employees without seeking approval of the Federal Ministries. The Authority also believes that even in the Public sector, the Petitioner's Board of Directors is empowered to determine the emoluments of its employees, therefore, does not see any reason to consider the salaries and wages expense as uncontrollable. Here it is clarified that the Authority has been allowing GoP's increases to the Petitioner under SYT regime based on its submissions and pleadings of the Petitioner itself.
- 13.7 Since, the Petitioner has failed to provide any new evidence or reason which would formulate the basis for the Authority to reconsider its decision in this regard; hence the request of the Petitioner is declined.

14. Repair and Maintenance (R&M) Expenditure

- 14.1 The Petitioner in this regard has stated that the Authority while analyzing repair and maintenance expense of the Petitioner, in the MYT tariff determination, worked out

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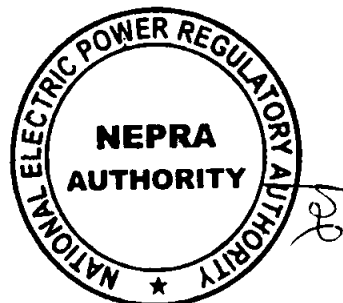


repair and maintenance expenses @ 2.02% of the GFAs. The Petitioner stated that the Authority's analysis and rationale for linking the R&M expense to the asset base is quite rationale and the link between the R&M expense and GFA cannot be denied keeping in view the quantum of investment plan and the ongoing activity of maintenance and repairs of increasing infrastructure. The Petitioner further cited that in India, as per regulation 5.5 of Delhi Electricity Regulation Commission Regulation, 2011, R&M expense (part of O&M) is determined as the constant, "K" (or K factor), multiplied by the opening GFA of the current year and the value of K factor for each year of the control period is determined by the Commission /regulator in the MYT determination.

- 14.2 The Petitioner based on the aforementioned submitted that cost of Rs.1,513 Million allowed for R&M for the FY 2015-16 as base reference cost is on a very lower side in the light of the fact that it has been spending more in the past three years on repair and maintenance. The Petitioner also argued that the R&M cost for the future years of the tariff period calculated as per the methodology would always result in shortage of cost for R&M. Keeping in view the above the Petitioner has requested the Authority to reconsider its earlier decision in light of the additional information and explanations and re-fix the R&M cost as 3.5% of the net fixed assets during the control period.
- 14.3 The Authority while assessing the repair and maintenance cost of the Petitioner for the FY 2015-16 discussed in detail the basis and rationale under para 31.25 to 31.33 of its MYT determination dated March 08, 2016. The Authority also discussed the reasons for the high repair & maintenance cost being incurred by the Petitioner and raised certain observations / concerns with respect to expensing out some costs which needed to be capitalized. The Petitioner has neither responded to the concerns of the Authority nor has provided any new evidence or reason to substantiate its request. In view thereof, the Authority does not see any reason to reconsider its earlier decision in this regard; hence the request of the Petitioner is declined.

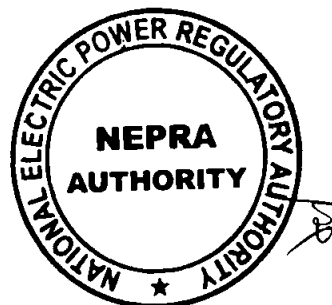
15. Other Operating Expenses / Salary and Wages

- 15.1 The Petitioner on the issue of Other operating expenses has submitted that the Authority determined other operating costs of Rs.1,497 Million by accepting the actual amount of FY 2014-15 and allowed an inflationary increase thereon. However, the actual figure taken by the Authority is not correct since as per the audited accounts of FY 2014-15, the actual amount of other operating expenses, after deducting the amount of bad debt expense, comes out to be Rs. 2,260 Million. Accordingly, it is requested to correct the assessment of other operating expenses by taking the actual figure of Rs. 2,260 million pertaining to other operating expenses as per audited accounts of FY 2014-15.





- 15.2 The Petitioner regarding salaries & wages cost has argued that in para 31.19 of the MYT determination, the Authority expressed that certain percentages have been considered by the Authority for assessing salary and wages expenses at Rs. 7,670 but the base figure on which such percentages have been taken has not been mentioned.
- 15.3 The Petitioner submitted that its actual audited figure of salary and wages for FY 2014-15 is Rs. 9,097 million, and if the cost of Rs. 553 Million of bonus and Rs. 800 Million for replacement hiring, disallowed by the Authority, is deducted from this figure even then the remaining amount comes out to be Rs. 7,744 million. Therefore, it would be justified if the salaries and wages cost is assessed by applying incremental impact on Rs. 7,744/- million and the resultant amount is made the base.
- 15.4 The Authority while allowing operating and maintenance cost always takes into account the prudence of the cost incurred. Assessment of cost for future period, based on actual figures appearing in the financial statement of the Petitioner, does not mean that the Authority is bound to accept the same as incurred by the Petitioner. While assessing the Petitioner's reference / base expenses for the FY 2015-16, the impact of amount capitalized (charged to work in progress) out of O&M expenses, as per the financial statements of the Petitioner, has also been adjusted. Thus, there is no calculation error or mistake in the Authority's assessed amount for the O&M cost, therefore the request of the Petitioner to revise the amount of O&M cost allowed is not accepted.
16. **Weighted Average Cost of Capital (WACC)**
- 16.1 The Petitioner has submitted that in its MYT, it proposed a WACC of 18.33% based on return on equity of 22.47% and cost of debt of 16.56%; workings for the same were also provided to the Authority along with the tariff petition. It was also requested to adjust the WACC annually to reflect the change in risk-free rate and beta, which are based on the prevailing market dynamics. Further a floor on the cost of equity at 19%, as allowed in the generation segment in order to attract the private sector participant was requested along-with proposal to introduce additional incentive for T&D loss reduction.
- 16.2 The Petitioner mentioned that the Authority approved a WACC of 11.83% based on the five-year PIB rates and beta computed from a list of 111 companies selected by the Authority as comparable distribution utilities and assessed the market premium of 7% as compared to the requested 8%. The Petitioner also highlighted that the Authority used cost of debt of three-month KIBOR + 2.75% based on the TFC's issued by K-Electric and disallowed the proposal of the Petitioner for annual adjustment of WACC stating that the notion was against the





spirit of the MYT, however, the Authority, decided to cover the risk of floating KIBOR by adjusting the reference KIBOR bi-annually. The Petitioner further stated that the Authority disallowed the floor on equity of 19% based on the ground that the Petitioner's comparison of Authority's returns allowed to the IPPs and to distribution utilities was not valid.

16.3 The Petitioner submitted that the incentive for reducing the T&D losses more than the target has also been disallowed by the Authority based on the ground that this is not in line with the methodology whereby the return on equity is fixed for the control period, and that the Petitioner can only maximize the profit in absolute terms by increasing the assets base. Further, the reduction in losses below the target would be as a result of Petitioner's efficiency and in order to promote such efficiency the benefit of this efficiency should remain with the petitioner.

16.4 Accordingly, the Petitioner has requested to reassess the following items;

- i. Cost of equity
- ii. Cost of debt
- iii. Floor on return on equity

17. Cost of Equity:

17.1 The Petitioner has stated that setting 5 year PIB yield as opposed to 10 year yield for the purposes of setting benchmark for the risk free rate is not justified as it is normal practice to take a 10 year PIB yield as the risk free rate when determining cost of equity. The Petitioner further submitted that since beta reflects the systematic risk associated with the business, therefore, only the comparable companies should be selected for the determination of beta. The Petitioner also mentioned that comparable companies can only be those that operate in similar business environment and face the same operating risks as the company for which beta is being determined. The Petitioner also highlighted that the Authority determined a beta of 1.33 for the tariff determination for the FY 2014-15.

17.2 The Petitioner on the data used by the Authority i.e. study conducted by Castalia for ERC in Philippines using 111 firms selected from Damodaran data set, stated that the Authority calculated the beta using the transmission and distribution companies in the sample. With respect to the basis of conclusion and the sample used by the Authority for calculation of beta, the Petitioner is of view that:

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17.3 The state of the economy and the extent to which the electricity market has evolved and been deregulated in the countries to which the selected distribution companies belong may be very different from Pakistan.

- In the 111 firms included in the data set of Damodaran, it is necessary to carefully select those companies that bear closest resemblance to the Petitioner for which the beta is being determined.

17.4 Keeping in view above the Petitioner has requested the Authority to narrow down the comparable set of companies to those operating in the same sector and market conditions close to that in which Petitioner operates.

18. Cost of debt

18.1 The Petitioner delineated that the Authority in the MYT determination rejected the request of the Petitioner of setting the cost of debt at 16.56% on the ground that in the privatization scenario, relent loans will be converted into equity. The Petitioner in this regard has submitted that considering privatization appears to have been slowed down if not stopped and also by keeping in view the fact of likelihood of Asian Development Bank loan to the Federal Government which will be relent to the Petitioner, therefore cost of debt of 9.76%, as determined by the Authority, may kindly be reviewed and the actual cost of debt be considered.

19. Floor on the Return on Equity:

19.1 The Petitioner pleaded that the Authority did not accept its plea for setting a floor on the return on equity at 19%. The Petitioner also submitted that the Authority, while accepting that investors are being incentivized to invest in Pakistan's power generation by being offered 17% return on equity on US\$ investments, has maintained that this incentive is available on greenfield projects and, hence, not appropriate when comparing with a running power utility like LESCO. The Petitioner argued that there are significantly higher risks in the power distribution sector as compared to the IPPs, which also have the benefit of sovereign guarantees.

19.2 The Petitioner also pointed out that the power market may change during the control period as the market moves away from the single-buyer model and quoted the example of Turkey whereby change in electricity markets by introduction of electricity retail markets has increased the risk and impacted the returns to the distribution companies. Therefore, it is important to incentivize potential investors by offering a minimum floor on the return on equity, which is accordingly proposed to be 19%.

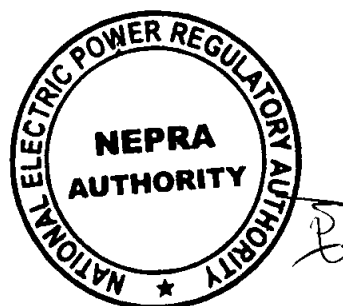
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- 19.3 The Authority has already discussed in detail the reasoning for use of 5 years PIB yield, as benchmark for risk free rate, under the para 36.21 of the MYT determination for FY 2015-16 to FY 2019-20. The Petitioner has not substantiated its stance of using 10 year PIB yield as the risk free rate with any evidence or documentary support rather has made a simple statement that setting 5 year PIB yield for the purposes of setting benchmark for the risk free rate is not justified as it is normal practice to take a 10 year PIB yield as the risk free rate. The Authority cannot accept the Petitioner's request, which is not duly supported with any study or rationale, therefore, does not see any reason to reconsider its earlier decision in this regard; hence the request of the Petitioner is declined.
- 19.4 Regarding the argument of the Petitioner for relying on data of 111 firms to work out the beta, the Authority at para 36.26 of the MYT determination has explained the basis for beta assessment. The referred study was not the sole basis for the determination, the range of betas- used by the International Regulators and findings of the in house study on beta was also considered. The Authority's assessed beta primarily reflects the risk of distribution business. Here it is pertinent to mention that the sample provided by the Petitioner was also not exclusively based on distribution companies.
- 19.5 The Authority after careful review of the Petitioner's argument with respect to the actual cost of debt is of the view that the Petitioner fails to comprehend the concept for the assessment of WACC. The Authority's assessed WACC has always been an "assessment" from which the actual position of the Petitioner's might differ. WACC assessed at different points of time would reflect the market conditions which are different at respective points of times. This is not a static number and depends upon so many variables like different risks, country rating and inflation etc. Moreover, the concern of the Petitioner being unable to meet its obligations regarding debt service liability of the relent loans is not validated through the numbers indicated in the financial statements. The Authority's evaluation indicates that the assessed depreciation and interest charges not only reasonably cover the actual debt service but also provide some extra cushion for the Petitioner.
- 19.6 The point regarding floor on return on equity has been addressed in detail and with sufficient clarity in the MYT determination under para 36.32 & 36.33. As the Petitioner has failed to bring any new evidence on account of its claim, therefore the request of the Petitioner is declined.

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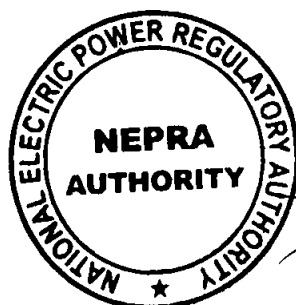




- 19.7 The Authority, while going through the submissions of the Petitioner observed that the issues raised by the Petitioner have already been deliberated in detail under para 36 of the determination dated March 08, 2016, wherein, detailed reasoning / justification has been provided. Since the Petitioner has failed to substantiate its aforementioned request with any new rationale / evidence, therefore, the request of the Petitioner is declined.
20. **Other Income (Treatment of Late Payment Charges) / Prior Year Adjustment**
- 20.1 The Petitioner has requested to treat the LPS independent of the Markup by CPPA (G) in order to cater for a situation where the amount of Markup is more than the amount recovered under LPS so that same may be allowed to be passed on to the consumer as part of power purchase cost. The Petitioner also mentioned that the Authority has decided that LPC recovered from consumers on utility bills, previously passed on to consumers through other income, shall be offset against the late payment invoices raised by CPPA (G) against respective XWDISCOs only. The Petitioner submitted that it fails to understand the reasons of not allowing the invoices of supplementary charges issued by CPPA (G) as the same decision should also be effective since the year of supplementary charges accruing i.e. 2009-10.
- 20.2 The Petitioner further submitted that it shared the following information regarding supplementary charges with Authority in February 20, 2015, however, is still waiting for invoice of supplementary charges for FY 2014-15 and once received accordingly will be shared with the Authority.

Mln. Rs.

YEAR	Supplementary Charges	LPS charged to consumers not off set against supplemental charges
2009-10	1,304.67	1,311.16
2010-11	2,740.59	1,433.41
2011-12	2,806.00	1,786.05
2012-13	2,563.25	1,225.55
2013-14	2,023.69	2,424.23
Total	13,438.22	8,180.4

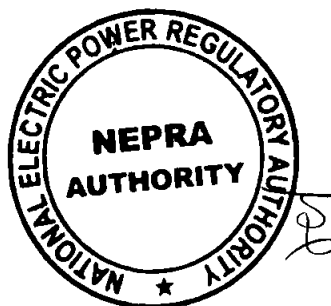




- 20.3 Accordingly, the Petitioner requested to allow previous supplementary charges since first tariff was notified because the LPC charged to consumers since the notification of first tariff has already been passed on to consumers as part of other income of Petitioner.
- 20.4 The Petitioner on account of PYA submitted that the working of negative prior year adjustment (PYA) of Rs.26,930 million has not been disclosed in the MYT determination. The Petitioner also submitted that the huge amount of negative PYA is not correct hence needs to be reviewed and since it is not aware of the working on the basis of which the Authority has assessed this figure therefore, presently it is not able to dilate upon the same, however, it reserves its right to present its point of view and reasons upon provision of the working by the Authority.
- 20.5 The Petitioner further submitted that post-retirement benefits of 70 billion to be disbursed over a period of 5 years has been disallowed by the Authority on the grounds that the Authority had been allowing the provision of post-retirement benefits to the Petitioner in the part of its O&M cost till FY 2011-12. The Petitioner argued that the Authority had only allowed the provision for post-retirement benefits for the FY 2008-09, 2009-10 and 2010-11 only, whereas, the Petitioner has requested for provision of post-retirement benefits since its creation, which may be allowed as PYA over a period of five years.
- 20.6 The Petitioner on the issue of late payment charges requested to deal LPS independent of the Markup by CPPA (G) in order to cater the situation where the amount of Markup is more than the amount recovered under LPS, so that the same may be allowed to be passed on to the consumer as part of power purchase cost.
- 20.7 CPPA (G) can charge markup to the Petitioner as per the ESA clauses 9.3 (d) of the agreement; the same is reproduced below;

"Late Payments by WAPDA or the Company, as the case may be, shall bear mark-up at a rate per annum equal to the Base Rate plus four percent (4%) per annum compounded semi-annually, and shall be computed for the actual number of Days on the basis of three hundred sixty-five (365) Day Year"

- 20.8 On the other hand the amount of LPC being charged from the defaulting consumer is a flat 10% on the outstanding bill amount. In view thereof, the Authority fails to understand, how the amount of LPC charged by CPPA(G) could be higher than the





amount of LPC billed to the consumers. Moreover, the Authority has already deliberated on the issue of LPC under para 6.15 of its MYT determination.

- 20.9 The Petitioner during the hearing of review motion informed the Authority that it now has received the supplementary charges invoice of Rs. 1,156 million from CPPA (G) for FY 2014-15 on account of late payments to CPPA (G) and requested to adjust the same. The Authority while reviewing the Financial Statements of the Petitioner for FY 2014-15 noted that it has a receivable balance of around Rs.18 billion from the CPPA (G). The Authority fails to understand the reasons of accepting invoice on account of delayed payments despite having receivables from CPPA (G). In view of the above discussion, the request of the Petitioner to allow LPC is hereby rejected.
- 20.10 On the issue of supplementary charges pertaining to the period 2010-2014, the Authority has already adjudicated on the issue of supplemental charges in detail and with sufficient clarity under para 13 of the Petitioner's MYT determination and also in the previous determinations. Since the Petitioner has raised no new arguments and has not provided any new evidence or reason to substantiate its aforementioned claim, which could formulate the basis for the Authority to reconsider its earlier decision in this regard; therefore, the request of the Petitioner is rejected.
- 20.11 The assessment of PYA has been discussed in detail under para 14 of the MYT determination along with its calculation. Moreover, the Petitioner was shared the detailed workings / calculations of the PYA immediately after the issuance of its MYT determination, however, the Petitioner instead of challenging the provided workings has only stated that the amount of PYA is not correct. Since the Petitioner has failed to substantiate its aforementioned request with any new workings / evidence, therefore, the request of the Petitioner is not accepted.
- 20.12 The Authority after going through the submission of the Petitioner regarding provision for postretirement benefits has noted that the Petitioner failed to present new information, evidence / rationale to substantiate its aforementioned request, which could form any basis for the Authority to reconsider its earlier decision in this regard; therefore, the request of the Petitioner to allow provision for postretirement benefits for the FY 2015-16 is declined. The Authority has already discussed this issue in detail and with reasonable clarity under para 31.21 to 31.24 of the Petitioner's MYT determination of March 08, 2016.

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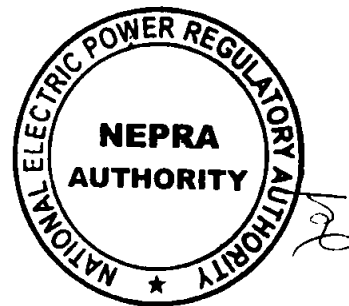
21. Extra-ordinary Events (Z Factor)

21.1 The Petitioner delineated that in its Multi Year Tariff Petition it suggested a Z factor for costs incurred as a result of force majeure events such as earthquakes, flooding, acts of terrorism etc., however, in the absence of provision for such events; adjustments restricted strictly to the CPI-X factor, it would not be able to recoup the costs required to undertake necessary repairs. The Petitioner further submitted that since replacement of any equipment, as a result of such damage, shall be covered through proposed investments, it is anticipated that major costs falling under Z factor will comprise repair & maintenance costs. The Petitioner also stated that the Authority allowed a cost of insurance of Rs. 24.16 Million in the other expenses, which covers grids and vehicles only and no other distribution infrastructure and if the Petitioner intends to cover its other assets along-with more insurance coverage, then it has to mitigate its commercial risk through its profits. The Petitioner is of the view that the cost of insurance of Rs.24.16 million allowed by the Authority is quite on lower side and as regards the more insurance coverage and mitigation of commercial risk through profit, since it has a regulated business and any earning beyond the determined revenue requirement is deducted/adjusted by the Authority in the next year tariff determination under the head of Prior Year Adjustment (PYA), therefore, in such circumstances, it will not be able to finance the loss caused by extraordinary events out of its profits. The Petitioner accordingly has requested the Authority to review the same.

21.2 The Authority while allowing the insurance cost of Rs. 30.6 million considered its financial statements. The argument of the Petitioner that it is not sufficient is not valid since it has not substantiated it with any evidence or argument. On the basis of aforementioned, it can be construed that the issue raised by the Petitioner is not based on facts is not accepted , therefore, the plea of the Petitioner in this regard being not maintainable.

22. Performance Standards

22.1 The Petitioner submitted that it provided a comprehensive year wise analysis about improvement in SAIFI, SAIDI and other performance standards to be achieved through investments under MYT regime, however, the Authority has set performance standards in terms of SAIFI and SAIDI, which are not possible to be achieved. The Petitioner has provided the comparison of both the targets as under;

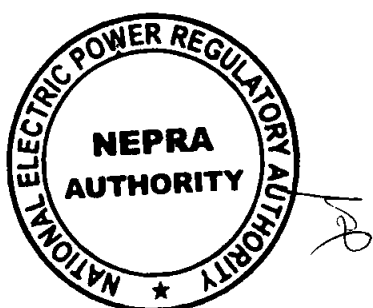




Description	Existing 2015	2016	2017	2018	2019	2020
SAIDI (Minutes)						
Proposed	3010.29	2709.26	2438.33	2194.50	1975.05	1777.55
Determined		13	10.4	8.32	6.65	5.32
SAIFI (Numbers)						
Proposed	52.49	47.24	42.52	38.27	34.44	30.99
Determined		14	11.2	8.96	7.17	5.74

22.2 The Petitioner in support of its claim provided the following reasons: -

- Lengthy 11-KV feeders with extensive load, resultantly voltage drop at certain feeders are very high.
- Non-provision of adequate vehicles equipped with buckets and necessary T&P, due to insufficient budget on account of less tariff.
- The short fall in generation is also creating low voltage problems.
- Overloaded 11 KV feeders.
- Theft incidents of transformer and distribution HT lines.
- Low frequency
- Overloading of transformers after load shedding spell of abnormal duration.
- Distribution transformer life.
- Cultural evils (banners installation on poles during Election campaign and other festivals etc.)
- Firing during ceremonies.
- Unforeseen incidents (accidents, switching by consumer at sectionalized T-Off at their own).





- Lengthy 11kv feeders.
- Birdage near slaughter houses.
- Old aged 11 KV Panel (deterioration due to repeated switching).
- Extension in load by general consumer without approval resulting in overloading of Transformers/ system, hence causing interruptions.

22.3 In view thereof, the Petitioner has requested to re-set the targets/ performance standards of SAIFI/ SAIDI.

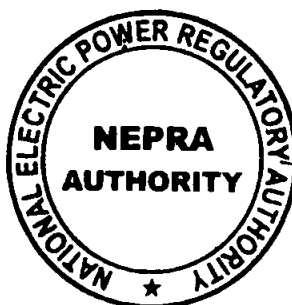
22.4 The Authority has already started the process of introducing an amendment in the Performance Standards and would be finalized shortly. However, till the process is not completed, the Authority directs the Petitioner to follow the currently notified Performance Standards (PSDR-2005). In case the Performance Standards are amended and are subsequently approved, the Petitioner will comply with the amended Performance Standards. This has already been addressed under para 47.3 of the MYT determination.

23. Industrial Tariff Rates (Peak and Off Peak)

23.1 The Petitioner has submitted that an analysis of the industrial tariff slabs (Peak and Off Peak) determined by the Authority in the MYT determination reveals an abnormal difference between the Peak and Off Peak rates of Industrial Tariff whereby the reduction in the off Peak rates in comparison with Peak rates is on higher side i.e. decrease in Peak & Off-Peak rate is Rs. 1.15/- & Rs. 2.24/- respectively. The difference between Peak & Off-Peak rates is approximately 1:2 which should be logical and peak rates be reduced to match the off peak rates.

23.2 The Petitioner also pointed out that the average difference between Peak and Off Peak industrial rates in the last determined tariff of Petitioner by Authority was 40% which has now increased to 51% in various industrial categories. The Petitioner requested that the ratio between difference of Peak and Off Peak rates be reviewed and rationalized.

23.3 The Authority while preparing the schedule of tariff to be charged from the consumers, ensures 100% recovery of the revenue requirement of the Petitioner and in case there is any under or over recovery, the same is adjusted through prior year adjustment. Therefore, the plea of the Petitioner to reduce the gap between peak and off-peak rates does not merit consideration





24. Security Deposit Rates

- 24.1 The Petitioner has submitted that the Authority rejected its proposal made in the MYT petition regarding revision in the security deposit rates and to withdraw the option allowed to B-3 & B-4 industrial customers to submit bank guarantee instead of cash security deposits without any cogent reasons. The Petitioner further submitted that the proposal should have been duly considered on its own merit regardless of the fact that other XWDISCOs raised the issue or not. The Petitioner also suggested that revision in security deposit rates should be made a regular part of the revision in electricity tariffs of a distribution company.
- 24.2 The Authority has already adjudicated on the issue of security deposit in para 54.8 of the MYT determination and since the Petitioner has not brought any new evidence in this regard, therefore the request of the Petitioner is declined.

25. PHPL Loans

- 25.1 The Petitioner has again requested for necessary relief on account of loans obtained by the government through PHPL.
- 25.2 The issue of PHPL loans has already been addressed under para 17 of the MYT determination. Since the Petitioner has failed to bring any new evidence in this regard, therefore the request of the Petitioner is declined.

26. Impact on revenue/sale to industrial consumers on account of self-generation not considered.

- 26.1 The Petitioner mentioned that all of its major industrial consumers, especially of the textile sector, are on self-generation and as such only utilize the Petitioner as a standby source of electricity to be used during the months of shortage of gas or other technical shutdown, otherwise they do not purchase electricity from the Petitioner almost throughout the year. The Petitioner also stated that now upon availability of RLNG they will remain on self-generation almost throughout the year and this will impact the revenues of the Petitioner drastically. The Petitioner also referred its letter dated March 07, 2016 whereby it brought this matter in the knowledge of the Authority.
- 26.2 The Petitioner accordingly has to amend the "Billing Demand" clause in two part tariffs to include higher of the following:

- i. Actual maximum demand recorded during the month.
- ii. 50% of the sanctioned load.





- 26.3 The Petitioner also suggested to revise the rates of Fixed Charges per KW per month upward with some corresponding adjustment in variable charges so that the power customers using Petitioner's supply as back-up only should pay reasonable level of capacity costs.
- 26.4 The Petitioner did not raise this issue in its MYT Petition, and has only raised this issue now in the MLR. Considering the limited scope of the Review Motion, whereby a motion seeking review of any order of the Authority is competent only upon discovery of new and important matter of evidence or on account of some mistake or error apparent on the face of record, the point raised by the Petitioner being not in the scope of MLR is not accepted.
27. **Application of TOU Principle**
- 27.1 The Petitioner has stated that the Authority created the new tariff category of "A-3 General Category" on the ground that TOU tariff should not be applied to those connections/consumers which operate only during off-peak hours due to nature of their working hence should be charged under normal applicable tariff without TOU rates otherwise it will result in loss of revenue without any contribution towards chopping of peak load on the system. However, the Authority while deciding the consumer categories falling under "A-3 General Category" did not include the banks and private offices whereas both of them also operate only during off-peak hours. The Petitioner also submitted that the Steel Melters under industrial category also as a routine practice avoid operating their furnaces in peak hours to avoid peak rates which has huge impacts on revenues because such consumers have a cumulative load of approximately more than 200-MW.
- 27.2 Firstly, the consumer categories which were included in A3 category were previously included in the residential categories, whereby no fixed charge was applied to them. The categories which the Petitioner is referring to are already paying fixed charges. Hence, even though they can manage their load pattern yet, they are bound to pay fixed charges on the capacity they use. Hence the Petitioner's pleadings being without any cogent reasons do not merit consideration.
28. **Reassessment of Efficiency Factor (X)**
- 28.1 The Petitioner submitted that the Authority's determined efficiency factor (X) of 5.9%, when applied, as per the mechanism provided by the Authority, will not result in sufficient increase on the base amount of O&M to cover the Petitioner's legitimate and prudent costs even despite improved efficiency. Further, the

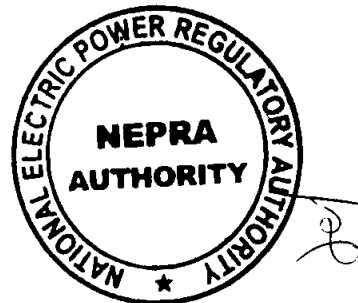
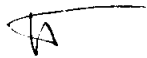


details of working / study conducted by the Authority in this regard has not been shared with the Petitioner. Accordingly, the Petitioner has suggested to conduct a separate consultative session for all the XWDISCOs in order to arrive at a just and informed efficiency factor (X) and the corresponding efficiency factor (X) be fixed for respective XWDISCOs accordingly.

- 28.2 The Authority has discussed with reasonable clarity the methodology of setting up the efficiency benchmarks under para 31.44 & 31.45 of the MYT determination, therefore, the Authority does not see any reason to conduct a consultative session of XWDISCOs in this regard. Further, the Authority in order to save the Petitioner from any negative adjustment on account of O&M cost, has clarified that the efficiency factor X, in any year of the control period, should not be greater than 30% of increase in CPI for the relevant control year. Thus, 5.9% efficiency factor would only apply if 30% of CPI increase in any year is more than 5.9%. If 30% of CPI increase in any year, is less than 5.9%, then the efficiency factor would be 30% of the increase in CPI, in any year, during the control period. Thus the Petitioner's plea of not having sufficient increase in the base amount of O&M to cover its legitimate and prudent costs even despite improved efficiency is not sustainable.

29. **Order**

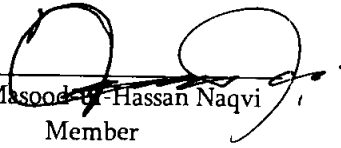
- 29.1 Having heard the Petitioner in support of its review petition, the Authority observed that in terms of rule 16(6) of NEPRA Tariff Rules, 1998 read with regulation 3(2) of the NEPRA (Review Procedure) Regulations, 2009, a motion seeking review of any order of the Authority is competent only upon discovery of new and important matter of evidence or on account of some mistake or error apparent on the face of record. The perusal of a determination sought to be reviewed clearly indicates that all material facts and representation made were examined in detail and there is no occasion to amend the impugned determination. No error inviting indulgence as admissible in law has been pleaded out. Therefore, the Authority is convinced that the review would not result in the withdrawal or modification of its determination.
- 29.2 From what has been discussed above, the Authority is of the considered view that the grounds agitated in the motion for leave for review are not sufficient enough justifying the modification of the impugned determination, hence the motion for leave for review is declined.






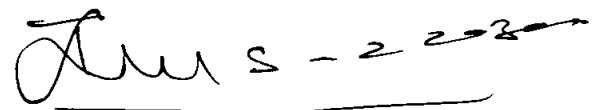
Decision of the Authority in the matter of
motion for leave for review filed by Lahore Electric Supply Company Limited (LESCO) against the
Determination of the Authority for FY 2015-16 to FY 2019-20

AUTHORITY

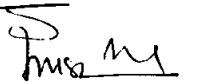

Syed Masood Hassan Naqvi
Member


Maj (R) Haroon Rashid
Member

Himayat Ullah Khan
Vice Chairman


Brig (R) Tariq Sadozai
Chairman




19.05.16