



Registrar

National Electric Power Regulatory Authority
Islamic Republic of Pakistan

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No. NEPRA/SAT-I/TRF-362/ 12563

July 25, 2017

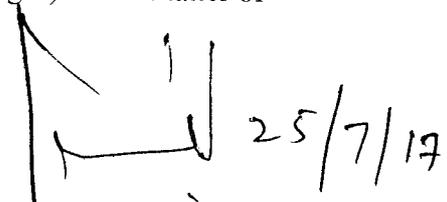
Chief Executive Officer
K-Electric Limited (KEL)
KE House, Punjab Chowrangi,
39 – B, Sunset Boulevard, Phase-II
Defence Housing Authority
Karachi.

Attention: Syed Moonis Abdullah Alvi, Chief Financial Officer

Subject: Decision on the Review Proceedings in the matter of Adjustment of Arrears

Enclosed please find herewith Decision of the Authority (05 pages) in the matter of adjustment of arrears for information.

Encl: As above


(Syed Safer Hussain)

DECISION ON THE REVIEW PROCEEDINGS IN THE MATTER OF ADJUSTMENT OF ARREARS

1. National Electric Power Regulatory Authority ("NEPRA" or "the Authority") while in the process of determining new Multi Year Tariff ("MYT") determination of K-Electric Limited ("KEL") deemed it necessary to review its all previous tariff adjustment decisions allowed to KEL during the previous MYT tariff regime, i.e. from September, 2002 till June 30, 2016. While doing so it was noticed that certain adjustment, related to settlement of arrears between Government of Pakistan ("GOP") and KEL, was allowed in Jan-Mar, 2009 quarterly adjustment decision dated June 30, 2009 ("the Decision"). On this account, a total amount of Rs. 4.62 billion or equivalent to Ps 41.33/kWh was included in KEL's tariff.
2. At the outset, the plain reading of the Decision revealed as if an inadvertent error in the text part has occurred by not mentioning the adjustment of Ps 41.33/kWh for recovery of Rs. 4.62 billion for a definite period of time. Accordingly, the Authority decided to initiate suo moto proceedings for the review of its Decision.
3. In accordance with provisions of the Regulation 3(1) of NEPRA Review Procedure Regulation 2009, KEL was sent a letter to explain its position within a notice period of 7 days. KEL replied vide its letter dated September 29, 2016 primarily advocating that the adjustment of Ps 41.33/kWh represented variations in the power purchase rate and was rightly made under the tariff adjustment mechanism. Such adjustment, according to KEL, was neither inadvertent nor erroneous. The Decision, as per KEL, was reached consciously and after due deliberation.
4. It was also decided by the Authority to hold a hearing on the subject. Being the key stakeholders, Ministry of Water & Power ("MoW&P") and Ministry of Finance ("MoF") were also informed to attend the hearing to present their viewpoint on the subject. The hearing was conducted on November 17, 2016 which was attended by the representatives of KEL and MoW&P.
5. The amount of Rs. 4.62 billion was incorporated in KEL's tariff 8 years back in 2009 when a different MYT regime was in place. Therefore, it is pertinent to discuss the then applicable determination, adjustment mechanism and key related decisions that took place before issuance of the Decision. A summary showing the chronological order of the related events is stated hereunder;

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- NEPRA approved MYT of KEL dated September 10, 2002. In the instant determination, base rate was approved as well as quarterly adjustment mechanism for different components of tariff was prescribed. This adjustment mechanism remained applicable till June, 2009 and then was modified through NEPRA's determination dated December, 2009.
- Under the adjustment mechanism prescribed in the 2002 determination, the variation in KEL own generation's fuel component as well as variation in the power purchase rate were adjusted on quarterly basis. For working out the quarterly adjustment figure in Ps./kWh, the impact of both the variations and units sold was to be taken of one year (three months actual and nine months projections). In line with the spirit of performance based MYT, approved adjustment mechanism did not ensure full recovery of actual fuel/power purchase cost of KEL at any point in time, rather the risk of over/under recovery of cost was borne by the KEL.
- In the 2002 MYT determination, NEPRA also decided to keep the quarterly adjustments at certain limits, i.e. the variation in KEL's own generation's and power purchase cost were set at 2.5% and 1.5% respectively. The leftover amount of variations, if any, was used to be adjusted in the subsequent quarterly tariff adjustments. It is also worth mentioning here that under 2002 mechanism, all the legitimate variations were used to be made the permanent part of KEL's tariff.
- In view of the KEL's non recovery of its revenues on timely basis, NEPRA decided to remove the aforesaid cap of 4% and that decision become effective from July 01, 2008. All the previous balance/left over amount, not passed on to the consumers due to cap, was incorporated in the KEL's tariff in the Jul-Sep, 2008 quarterly adjustment decision.
- It is pertinent to mention here that NEPRA vide its decision dated April 14, 2004 decided that National Transmission and Despatch Company Limited ("NTDCL") shall charge KEL on marginal rate, however KEL disputed that decision and continued to make payment to NTDC on fixed rate i.e. Rs. 3.69/kWh. Resultantly, the actual arrears (difference between marginal and fixed cost) reached to around Rs. 35 billion upto July, 2008. For the aforesaid disputed amount between NTDC and KEL, a committee was formed by GOP. While allowing the adjustment for the quarter Jul-Sep quarter 2008, NEPRA decided not to include the

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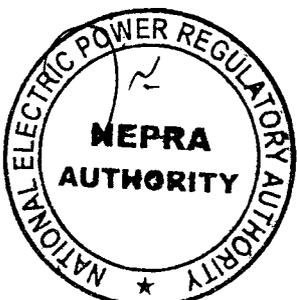


variations due to this disputed amount, despite removal of 4% cap, till the resolution of this issue by the committee formed by GOP.

- Economic Coordination Committee (ECC) dated August 26, 2008 decided to treat KEL at par with other DISCOs for tariff purpose. NEPRA's determination of NTDCL was accordingly revised on September 29, 2008 while allowing NTDCL to charge KEL on the basis of basket rate. The said decision was notified on October 30, 2008; hence, the Authority started applying basket rates from November 01, 2008.
- During the processing of the adjustment request for the quarter Jan-Mar, 2009, KEL informed the Authority that ECC dated April 08, 2009 on the summary submitted by the MoW&P on the resolution of issues related to KEL has decided that the difference between average Distribution Companies ("DISCOs") rate and the threshold of Rs. 3.69/kWh for the period from August to October 2008 amounting to Rs 3.157 billion plus the difference of reconciled and agreed payable arrears between NTDCL and KE ending July, 2008 amounting to around Rs. 1.465 billion will be claimed by KEL from NEPRA as regulatory shortfall through forthcoming quarterly tariff adjustment. KEL requested the Authority that the effect of this additional cost may be allowed. Upon the said request of KEL, the Authority decided to include this amount in the decision for the quarter ending March, 2009.

The key points of KEL's response submitted during the proceedings of the subject case are summarized hereunder:

- The adjustment represents variations in the power purchase rate and was rightly made under the tariff adjustment mechanism.
- Such adjustment was neither inadvertent nor erroneous. The decision was reached consciously and after due deliberation.
- NEPRA now is considering changing its opinion. It is respectfully stated that this thought is based on misunderstanding of both the ECC decision and NEPRA's previous determinations.
- NEPRA's tariff determinations were a key factor in determining and influencing KE's shareholders'/investors' investment strategy. It is worth emphasizing that relying on the



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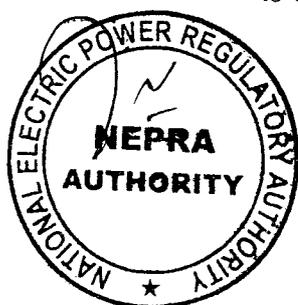
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NEPRA determinations, KE shareholders/ investors took a number of significant steps and made large investments. If there was even a slight suggestion that NEPRA may change its opinion, investors would have been deterred from making such large investments and would have applied for a further increase in the tariff. As the shareholders/ investors have already taken a number of steps and made investments by relying on NEPRA's determinations, NEPRA is in law, estopped from resiling from its earlier determinations and from misinterpreting the same.

- The shareholders/investors of KE had a legitimate expectation that NEPRA will not under the thin guise of "*inadvertent omission*" re-open past and closed transactions by misreading its determinations and the ECC decision.
- An isolated decision by NEPRA to change its determination and adjust tariffs and make recoveries at revised rates will adversely affect KE and its shareholders/investors. Such an action can and will disrupt all norms of due process and will be expropriatory in nature. It has a potential of delaying and may even jeopardize new as well as existing KE projects. This may, in turn, have significant adverse implications on KE's overall business plan and can put its services to its consumers in serious jeopardy.
- We are confident that NEPRA being a prudent regulator, keeping the interests of KE and consumers, will dismiss the matter as it lacks any factual and legal grounds and will also severely damage investor confidence and KE's future business plan.

Findings of the Authority

6. The Authority after thorough review of the case, response of KEL in the matter as well as analyzing the then applicable determination and corresponding tariff adjustment mechanism give its findings as follows;
 - i) In pursuance to the ECC decision dated August 26, 2008, KEL was to be treated at par with Discos and the amount of Rs. 4.62 billion (equivalent of Ps. 41.33/kWh) approved by ECC in its decision dated April 08, 2009 on account of settlement of outstanding arrears between GOP and KEL was the difference between basket and fixed rates of NTDCL starting from July, 2004 to October, 2008. Being the difference of two rates in the light of aforesaid ECC decision, the



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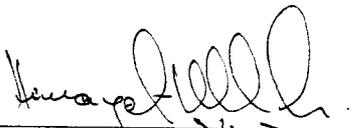
Authority considered the said amount as legitimate cost of KEL as variations for which the then applicable mechanism was devised and approved. Accordingly, the Authority decided to adjust the said arrears along with other fuel cost variations in the tariff of KE on permanent basis strictly in accordance with applicable adjustment mechanism in the Decision.

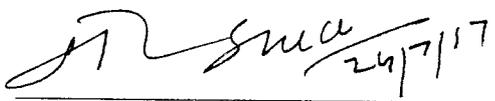
- ii) It is also worth mentioning here that NEPRA did not adjust an amount of Rs. 6.754 billion in the tariff of KE, referred in the same decision of ECC for adjustment, as the applicable adjustment mechanism did not have provision for such gain/loss of revenue calculated on actual or implied basis.

Decision of the Authority

7. In view of the above, the Authority concludes that the adjustment of Rs. 4.62 billion made in KEL's tariff through the Authority's Decision was well considered and conscious decision of the Authority and therefore does not warrant any further action in the matter. Accordingly, the review proceedings are disposed of.

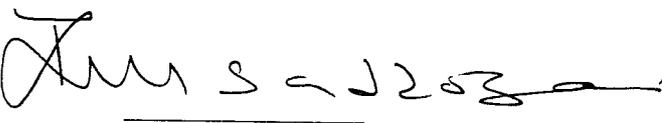
Authority


Himayat Ullah Khan
Member

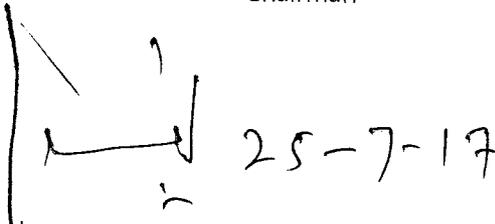

Maj (R) Haroon Rashid
Member


Syed Masood ul-Hassan Naqvi
Member


Saif Ullah Chattha
Vice Chairman
21-7-2017


Brig (R) Tariq Saddozai
Chairman




25-7-17