No. OGRA-6(2)-1(2)/2006-FRR

IN THE MATTER OF

SUI NORTHERN GAS PIPELINES LIMITED
FINAL REVENUE REQUIREMENT, FY 2005-06

UNDER

OIL AND GAS REGULATORY AUTHORITY ORDINANCE, 2002 AND NATURAL GAS TARIFF RULES, 2002

DECISION

September 18, 2006

Before:

Munir Ahmad, Chairman
Jawaid Inam, Member (Gas) / Vice Chairman
Rashid Farooq, Member Oil
M.H. Asif, Member (Finance)

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1. Background

1.1. Sui Northern Gas Pipelines Limited (the petitioner) is a public limited company, incorporated in Pakistan and listed on the stock exchanges at Karachi, Lahore and Islamabad. It is engaged in construction and operation of gas transmission and distribution pipelines and sale of natural gas.

1.2. The petitioner filed a petition (the petition) on August 14, 2006 under Section 8(2) of the Oil & Gas Regulatory Authority Ordinance, 2002 (the Ordinance) and Rule 4(3) of the Natural Gas Tariff Rules, 2002 (NGT Rules), for determination of its Final Revenue Requirement (FRR) for FY 2005-06 (the said year) on the basis of the accounts, as initialed by its statutory auditors. The Authority admitted the petition on August 28, 2006.

1.3. The Authority, vide its order dated December 31, 2005, had determined the petitioner's Second Revised Estimated Revenue Requirement (RERR2) for the said year under Section 8(2) of the Ordinance at Rs. 100,160 million for estimated sale volume of 499,479 BBTU, and prescribed prices for various categories of consumers, on provisional basis as shown in relevant columns of ***Annexure-B.***

1.4. The petitioner has submitted the present petition for determination of its FRR for the said year after incorporating the effect of actual changes in the wellhead gas prices, sale mix and other relevant factors. The petitioner has worked out its FRR for the said year at Rs. 108,168 million for actual sale volume of 539,099 BBTU. Based on the provisional prescribed prices and actual sale mix, the petitioner has computed a surplus of Rs. 765 million for the said year. The FRR would affect the prescribed prices for the said year impacting in turn the Gas Development Surcharge receivable by the Federal Government, and not the consumer prices.

1.5. The Authority issued notice of conference on August 30, 2006 to the petitioner and the following interveners and related parties:

a) Federal Government.
b) Chairman, All Pakistan CNG Association, Rawalpindi.
c) All Pakistan Textile Mills Association through Az Zaman Advocates, Islamabad.
d) Secretary, Gujranwala Chamber of Commerce and Industry, Gujranwala.

1.6. The hearing was held at OGRA office, Islamabad on September 13, 2006.

2. Salient Features of the Petition

2.1. The petitioner has submitted the following statement of cost of service per MMBTU:

Table 1: Comparison of Cost of Service with Previous Year, ERR & RERR2

					Rs. Per MMBTU
Particulars	**FY 2004-05**	**FY 2005-06**			
	FRR	**DERR**	**RERR 1**	**RERR 2**	**The Petition**
Units sold (BBTU)	**505,543**	**499,479**	**499,479**	**499,479**	**539,099**
Cost of gas	140.82	154.23	154.23	167.60	170.63
Transmission and distribution cost	10.37	12.55	12.97	13.22	11.84
Depreciation	7.21	8.47	8.47	8.47	7.54
Deferral account	-	0.76	0.34	0.34	-
Return on net average operating fixed assets	10.70	10.90	10.90	10.90	10.64
Other operating income	(4.18)	(3.83)	(3.83)	(3.83)	(3.54)
Cost of service / prescribed price	**164.93**	**183.07**	**183.07**	**196.70**	**197.11**
Revenue available at existing prescribed	164.93	183.07	183.07	196.70	198.53
(Shortfall) / Surplus in revenue	**-**	**-**	**-**	**-**	**1.42**

2.2. The petitioner has made the following submissions:

2.2.1. The annual return has been claimed at the rate of 17.5% of the value of its average net operating fixed assets (net of deferred credit) before corporate income taxes, and interest, mark-up and other charges on debt, as guaranteed by the Government of Pakistan under the covenants of the loan agreement between the petitioner and the World Bank.

2.2.2. Gross addition in fixed assets during the said year has been claimed at Rs. 5,591 million and net addition, after accounting for deletion and depreciation, at Rs. 1,331 million, increasing the net operating fixed assets from Rs. 36,975 million in FY 2004-05 to Rs. 38,306 million. After adjustment of deferred credits, the average value of operating fixed assets has been claimed at Rs. 32,763 million and the required return at Rs. 5,734 million.

2.2.3. The net operating revenues have been claimed at Rs. 108,933 million in the petition, as against Rs. 93,354 million in the RERR2, as detailed below:

Table 2: Comparison of Operating Revenues per RERR2 with the petition

		Rs. in million
Particulars	**FY 2005-06**	
	RERR 2	**The petition**
Sales at current tariff	91,439	107,027
Rental & services charges	730	745
Surcharge & interest on arrears	575	534
Amortization of deffered credit	545	473
Other operating income	65	154
Net operating revenues	**93,354**	**108,933**

2.2.4. The net operating expenses have been claimed at Rs. 102,434 million in the petition as compared to Rs. 94,716 million in RERR2, as detailed below:

Table 3: Comparison of Operating Expenses per RERR2 with the petition

		Rs. in million
Particulars	**FY 2005-06**	
	RERR 2	**FRR Petition**
Cost of gas sold	83,715	91,986
Transmission & distribution cost	4,737	4,507
Gas internally consumed (GIC)	1,621	1,583
Depreciation	4,229	4,066
Workers' participation fund	245	292
Deferral account	170	-
Net Operating Expenses	**94,716**	**102,434**

2.2.5. The Unaccounted for Gas (UFG) has been claimed at 6.59% (40,467 MMSCF) as against the upper & lower target of 6% & 5.70%, respectively, fixed by the Authority.

2.2.6. The net result of the petitioner's above mentioned claims is that there is a surplus of Rs. 765 million after allowing 17.5% return on average net operating assets, which translates to a decrease of Rs. 1.42 per MMBTU in the existing average prescribed price, as tabulated below:

Table 4: Comparison of Average Increase in Prescribed Price per RERR2 with the petition

			Rs. in million
	Particulars	FY 2005-06	
		RERR2	The Petition
A	Net operating revenues	100,160	108,933
B	Less: Net operating expenses including WPPF	94,716	102,434
C	Surplus / (shortfall) (A – B)	5,444	6,499
D	Return required @ 17.5% on net fixed assets in operation.	5,444	5,734
E	Total surplus /(shortfall) in the revenue requirement (C - D)	-	765
F	Sales volume (BBTU)	499,479	539,099
G	**Rs / MMBTU Increase requested in the existing average prescribed price to meet the total shortfall in revenue requirement (E ÷ F)**	**-**	**(1.42)**

3. Proceedings

3.1. The petitioner was represented at the hearing by a team of senior executives led by its Managing Director, Mr. Abdul Rasheed Lone, who were given full opportunity to present the petition. They made submissions in detail with the help of multimedia presentation. Federal Government was represented by Mr. Dawood Khan, Deputy Secretary, Cabinet Division. However, no intervener was present.

4. Determination

4.1. After detailed scrutiny of the petition, the detailed information subsequently provided and clarifications given during the conference by the petitioner, the Authority determines as follows:

5. Return to Licensee

5.1. The petitioner has requested for determination of its revenue requirement for the said year allowing return on average net operating fixed assets at the rate of 17.5% in accordance with the covenants agreed with the World Bank and guaranteed by the Government of Pakistan. The Federal Government has issued an order on October 11, 2002 under Section 47 of the Ordinance, that till such time that an appropriate rate of return is determined by OGRA in consultation with the Federal Government and the licensees, the Authority shall determine the revenue requirement of the petitioner per the covenants stipulated in the loan agreement with the World Bank. The Authority has developed and proposed a new tariff regime for regulated natural gas sector of Pakistan, which is currently in the process of consultation with the stakeholders. Pending its finalization, and approval by the Federal Government, the Authority is obliged to follow the above basis of 17.5% of the average net operating fixed assets, which is also provided in the petitioner's license condition No. 5.2, for the determination of FRR for the said year.

6. Operating Fixed Assets

6.1. Summary

6.1.1. The petitioner has claimed a gross addition in fixed assets during the said year at Rs. 5,591 million and net addition after accounting for depreciation at Rs. 1,331 million, increasing the net operating fixed assets from Rs. 36,975 million in FY 2004-05 to Rs. 38,306 million. After adjustment of deferred credits, the average value of operating fixed assets has been claimed at Rs. 32,763 million and the required return at Rs. 5,734 million, as tabulated below:-

Table 5: Computation of Return on Operating Fixed Assets per petition

	Rs. in million
Description	**The Petition**
Net operating fixed assets at beginning	36,975
Net operating fixed assets at closing	38,306
Subtotal	75,281
Average net assets (A)	**37,641**
Deferred credit at beginning	4,431
Deferred credit at closing	5,323
Subtotal	9,754
Average deferred credit (B)	**4,877**
Average net fixed assets (A-B)	**32,763**
Return required on net operating assests	17.5%
Amount of return requested by the petitioner	**5,734**

6.1.2. Comparative analysis of additions in fixed assets with the RERR2 and the previous year is as follows:

Table 6: Summarized Schedule of Additions Compared with RERR & Previous Year

					Rs in million
Particulars	**FY 2004-05**	**FY 2005-06**		**Inc. / (Dec.) over RERR2**	
	FRR	**RERR2**	**The Petition**		
Transmission	4,274	1,741	1,331	(410)	(24)%
Distribution Development	2,890	4,500	4,041	(459)	(10)%
Plant & Machinery etc.	328	340	214	(126)	-37%
MIS Project	-	90	5	(85)	(94)%
Net addition in asset base	**7,492**	**6,672**	**5,591**	**(1,081)**	**(16)%**

6.1.3. The petitioner has provided further breakdown of the major items of additions as detailed below:

Table 7: Detailed Schedule of Additions per petition

		Rs. in million
S.No.	**Asset Description**	**The Petition**
A	**Transmission**	
	PVIII	
1	Transmission system-Prior years adjustments	93
2	Compression-Leftover jobs	177
3	Contruction equipment	128
	Subtotal	**398**
	PVII	
4	Transmission system-Prior years adjustments	7
5	Compression-Leftover jobs	19
6	Freehold Land (Project VII / VIII)	84
	Subtotal	**110**
	Other Project	
7	8" dia 28.55 km Shakardara Lachi Line	111
8	10" dia 25.50 km Bestway Cement	163
9	12" dia 60 km Rawat Murree	257
10	8" dia 33.29 km DG Khan Cement	98
11	CNG Station at Lillah Town	31
	Subtotal	**660**
12	Rehabilitation of Compressor Packages	41
13	Centaur Gas Turbine Recondition	122
	Subtotal	**163**
	Total Transmission	**1,331**
B	**Distribution Development**	
14	Distribution Development	3,924
15	Sales Meter's station / regulatory stations	88
16	Cathodic Protection	29
	Total Distribution Development	**4,041**
C	**Other Assets**	
17	Plant machinery, transport, furniture, electrical appliances, computers,	204
18	Distribution office building- Peshawer (Prior year costs)	10
	Total Other Assets	**214**
D	**MIS - Phase II ERP Implementation**	
19	MIS	5
	Total MIS Project	**5**
	Grand Total	**5,591**

6.2. Transmission

i. CNG Station at Lillah Town

6.2.1. The petitioner has claimed Rs. 31 million for the CNG station established on account of first phase of Lillah Town CNG project. The petitioner has submitted that the first phase of the said project was completed prior to Federal Government's March 22, 2006 decision to the effect that no subsidy would be given on supply of LNG / CNG / LPG through local pipeline networks.

6.2.2. The petitioner has informed that the project was carried out per the directives of President of Pakistan and that it would not incur any further expenditure on such projects.

6.2.3. The Authority had also decided in its Regulatory Meeting No. 24 of 2005, held on October 28, 2005 to convey "No Objection in Principle", Lillah Town being a "Pilot Project".

6.2.4. ***The Authority, taking into account the above mentioned position, allows the capital expenditure of Rs. 31 million, so far incurred, as one time revenue expense (not making it a part of rate base).***

6.3. Distribution Development

ii. New Towns & Villages

6.3.1. The petitioner has claimed Rs. 733 million on account of new towns and villages commissioned during the said year. The Authority observes that out of Rs. 733 million, part of the cost within the GOP criteria amounting to Rs. 596 million has been incurred by the petitioner from its own resources, and the remaining cost amounting to Rs. 137 million has been met through Government Grants. ***Therefore, the Authority treats Rs. 137 million as part of deferred credit for the said year.***

6.4. Determination of Fixed Assets

6.4.1. The value of additions in assets claimed by the petitioner and allowed by OGRA (per discussion above), for the said year, is as under:

Table 8: Summary of Asset Additions Determined by OGRA

Particulars	Requested by Petitioner	Allowed By OGRA
		Rs. in million
Transmission	1,331	1,300
Distribution development	4,041	4,041
Other assets	214	214
MIS project	5	5
Net addition in asset base	**5,591**	**5,560**

6.4.2. ***After adjustment of additions in deferred credit per para 6.3.1 above, the closing balance of deferred credit is determined at Rs. 5,456 million for the said year.***

6.4.3. The Authority observes that the petitioner has changed the rate of depreciation on meters from 6% to 10%, without convincing justification, and obtaining prior approval of the Authority and the Federal Government. Therefore, the depreciation on meters is reworked at 6% and reduced by Rs. 304 million.

6.4.4. Depreciation expense claimed by the petitioner is also reduced by Rs. 1 million as a result of treating Rs. 31 million on account of CNG Station at Lillah Town as revenue expenditure for the said year as discussed in para 6.2.1 to para 6.2.4 above.

6.4.5. ***In view of the above, the depreciation expense is allowed at Rs. 3,761 million with the direction that the petitioner should separately file formal application for revision of depreciation rate on meters with the Authority, giving detailed justifications.***

6.4.6. The Authority observes that it had directed the petitioner vide its determination dated October 12, 2005 to provide:

a) its statutory auditors' certificate on the basis of detailed cost audit confirming the cost that could be reasonably attributed to each asset capitalized during a year, on the basis of reasonable levels of efficiency and cost effectiveness, if it falls within any of the under-mentioned categories:

- **Transmission**:

   - Construction Machinery
   - Pipelines (new / replacements)
   - Compressors / turbines
   - SCADA
   - Telecommunication
- **Distribution:**
   - Pipelines (supply mains, extensions etc.) <u>excluding</u> the jobs with total value of less than Rs. 10 million.

b) its auditors' certificate confirming procurement of assets and services being transparent, cost effective and in accordance with the PPR 2004, be limited to the following:

- Construction machinery
- Pipeline
- Regulators
- Valve and Fittings
- Coat and Wrap Materials
- Compressors / Turbines
- SCADA
- Service contracts excluding those valued at less than Rs. 50 million.

6.4.7. The certificate provided by the petitioner in this respect states that the audit has been done on test check basis and that cost effectiveness & reasonable level of efficiency for assets capitalized during the year could not be ascertained as the required technical expertise co uld not be arranged.

6.4.8. The Authority notes that the certificate provided by the petitioner's statutory auditors is not in line with the above-mentioned directions and does not fulfill OGRA's requirement.

6.4.9. ***The Authority directs the petitioner to provide with in three months of issuance of this Order, the requisite certificate of statutory auditors to the entire satisfaction of OGRA.***

6.4.10. ***In view of above, the Authority provisionally determines the additions in fixed assets claimed by the petitioner at Rs. 5,560 million. After adjustment of depreciation expense per para 6.4.5 above, the closing net operating fixed assets for the said year are determined at Rs. 38,580 million, subject to adjustments, if any, after the provision of auditors' certification within the stipulated timeframe.***

7. Operating Revenues

7.1. Sales Volume

7.1.1. The sales volume has increased by 8% to 539,099 BBTU, as against 499,479 BBTU per RERR2 2005-06. Category-wise comparison with previous years has been provided by the petitioner as under:

Table 9: Comparison of Category-wise Sales Volume per petition with RERR2 & Previous Year

				volume in BBTU	
Category	**FY 2004-05**	**FY 2005-06**		**Inc./ (Dec.) over RERR 2**	
	FRR	**RERR 2**	**FRR Petiiton**		
Power	190,348	201,641	207,837	6,196	3%
Cement	8,086	8,508	9,222	714	8%
Fertilizer	41,639	47,147	43,622	(3,525)	(7)%
General Industries	138,536	115,913	151,358	35,445	31%
Commercial	18,528	17,481	19,891	2,410	14%
Domestic	108,405	108,789	107,169	(1,620)	(1)%
Total	**505,542**	**499,479**	**539,099**	**39,620**	**8%**

7.1.2. ***The Authority accepts the sales volume for the said year at 539,099 BBTU as detailed above.***

7.2. Sales Revenue

7.2.1. Sales revenue (net of sales tax) per petition is Rs. 107,898 million at existing sale prices. Category-wise comparison with RERR2 and previous year is given below:

Table 10: Comparison of Category-wise Sales Revenue per petition with RERR2 & Previous Year

Category	FY 2004-05 FRR	FY 2005-06 RERR 2	FY 2005-06 FRR Petition	Inc. / (Dec.) over RERR 2	%
				Rs. in million	
Power	36,690	40,644	48,197	7,553	19%
Cement	1,755	1,932	2,386	454	23%
Fertilizer	3,916	4,647	4,732	85	2%
General Industries	26,142	22,848	34,051	11,203	49%
Commercial	3,984	3,877	5,082	1,205	31%
Domestic	12,224	12,773	13,450	677	5%
Total	**84,711**	**86,720**	**107,898**	**21,178**	**24%**

7.2.2. The sales revenue has increased as a consequence of increase in sales volume as stated in Para 7.1.1 above. ***The Authority accepts the sales revenue at Rs. 107,898 million for the said year.***

7.3. Other Operating Income

i. *Summary*

7.3.1. The petitioner has claimed other operating income at Rs. 1,906 million for the said year as against Rs. 1,915 million per RERR2 FY 2005-06. Item-wise comparison is as under:

Table 11: Comparison of Other Operating Income per petition with RERR & Previous Years

Category	FY 2004-05 FRR	FY 2005-06 RERR 2	FY 2005-06 FRR Petition	Inc. / (Dec.) over RERR 2	%
				Rs. in million	
Rental & services charges	699	730	745	15	2%
Surcharge & Interest on arrears	647	575	534	(41)	(7)%
Amortization of deferred credit	398	545	473	(72)	(13)%
Other operating income	368	65	154	89	137%
Total	**2,112**	**1,915**	**1,906**	**(9)**	**(.47)%**

ii. *Amortization of Deferred Credit*

7.3.2. Amortization of deferred credit has been claimed by the petitioner at Rs. 473 million. The Authority has decided in para 6.3.1 above to treat expenditure amounting to Rs. 137 million as deferred credit for the said year. ***Accordingly,***

income realized as the amortization of deferred credit is increased by Rs. 4 million and determined at Rs. 477 million.

iii. ***Other Operating Income***

a) ***Credit Balances Written Back***

7.3.3. The petitioner has claimed "credit balances written back" amounting to Rs. 3 million as non-operating income. The Authority notes that these balances relate to the reversal of long outstanding balances of expenses payable / booked by the petitioner. These were treated as operating expenses at the time of incurrence; therefore, their reversal also qualifies as operating income.

7.3.4. ***The Authority, in view of the above, recognizes credit balances written back amounting to Rs. 3 million as operating income.***

b) ***Transmission Income for Gas Supplied to POL, PPL & ARL***

7.3.5. The Authority observes that the petitioner has included Rs. 7.85 million for the said year in operating income on account of transmission of gas for Pakistan Petroleum Limited (PPL), Pakistan Oil Fields (POL) & Attock Refinery Limited (ARL).

7.3.6. The petitioner is obligated per its license condition 11.2 to enter into all contracts on arm's length basis and seek such approvals from the Authority of such contracts, as may be required under the Ordinance or the Rules.

7.3.7. The Authority notes that the petitioner has not obtained approval for the above-mentioned transmission agreements, thus violating a license condition.

7.3.8. ***The Authority directs the petitioner to immediately seek OGRA's approval of the said agreements / contracts for transmission of gas.***

8. Operating Expenses

8.1. Cost of Gas

8.1.1. The cost of gas per petition is Rs. 91,986 million compared to Rs. 83,715 million per RERR2, higher by Rs. 8,271 million (9.88%).

8.1.2. The Authority allowed input cost of gas on the basis of combined weighted average cost of gas purchases by the petitioner and SSGCL at Rs. 156.51 per MMBTU in RERR2 in accordance with the Agreement for Equalization of Cost of Gas dated 22nd September, 2003, between the petitioner and SSGCL. On the basis of the actual audited results, weighted average of input cost of gas for the said year works out at Rs. 159.20 per MMBTU as under:

Table 12: Weighted Average Cost of Input Gas

Company	MMCF	BBTU	Rs in million	Rs./ MMBTU
SSGCL	385,362	375,590	65,138	173.4290
SNGPL	624,952	586,633	88,043	150.0823
Total	**1,010,314**	**962,223**	**153,181**	**159.1954**

8.1.3. The above increase in cost of gas, compared to RERR2, is due to increased off-takes from various fields and increased wellhead gas prices, calculated on the basis of actual payments made during the said year.

8.1.4. The Authority observes that the petitioner has included the sales tax on gas sales paid to the Government of Azad Jammu and Kashmir (AJK) amounting to Rs. 1.502 million in the computation of cost of gas for the said year.

8.1.5. The Authority notes that the Government of Pakistan (GoP) through its letter dated July 19, 2004, had informed the petitioner that it was not bound to make separate sales tax registration in AJK as the supply of gas is made from Pakistan. Further, OGRA, vide its letter dated August 03, 2006, had also advised the petitioner to take up the matter directly with the GoP, being a policy issue. The GoP, vide Ministry of Petroleum and Natural Resources letter No. NG (1) -16 (91) / 03 – AJK dated September 09, 2006, has since advised that SNGPL is liable to be registered for sales tax purposes in accordance with Sales Tax Rules, 2004 as in force in the State of Azad Jammu and Kashmir.

8.1.6. The Authority observes that as discussed and decided in paras 8.3.8 to 8.3.12 of this order, GIC has been determined at Rs. 1,559 million, as against the petitioner's claim of Rs. 1,583 million, increasing the cost of gas by Rs. 24 million.

8.1.7. ***The Authority, in view of the above, determines the cost of gas sold at Rs. 92,009 million after excluding the payment of sales tax to AJK, in accordance with the GoP advice.***

8.2. Unaccounted for Gas (UFG)

8.2.1. The petitioner has claimed the Unaccounted for Gas (UFG) at 6.59% (40,467 MMSCF) for the said year, as follows:

Table 13: Comparison of Unaccounted for Gas per petition with RERR2 & Previous Year

				lumes in MMCF
	FY 2004-05	**FY 2005-06**		**Inc. / (decr.) from RERR 2**
Particulars	**DTRR**	**RERR 2**	**The Petition**	**MMCF**
Gas Purchases	575,914	567,575	613,854	46,279
Gas Sales	536,384	533,629	573,387	39,758
UFG	39,530	33,946	40,467	6,521
UFG %	**6.86%**	**5.98%**	**6.59%**	**0.61%**

8.2.2. The Authority, in its RERR for the said year, had fixed the UFG upper & lower targets at 6% & 5.70% respectively, with the conditions that the petitioner would be entitled to retain the savings in the event of actual performance being better than the lower target, fully bear UFG above the upper target from its own profits and UFG between the lower & upper target be adjusted in the revenue requirement to the extent of 50% & the balance 50% be absorbed by the petitioner from its own profit.

8.2.3. The petitioner has submitted that it has not been able to achieve the targeted UFG level for the said year, and has therefore deducted Rs. 681 million from its revenue requirement on account of UFG above the upper target.

8.2.4. The Authority notes that the petitioner has taken higher volume of GIC for calculating the UFG for the said year. As determined in para 8.3.9, the Authority adopts GIC volume at 10,449 MMCF, on the basis of which revised computation of UFG is as under:

Table 14: UFG Calculation

Particulars	**The Petition**	**Determined by OGRA**
	MMCF	MMCF
Opening Balance	2,801	2,801
Net Purchases	625,735	625,735
Less Closing Balance	(2,974)	(2,974)
Available for Sale	625,562	625,562
Gas Blown Off Due to Rupture in Transmission Sytem	(351)	(351)
Gas Blown Off Due to Rupture in Distribution Sytem	(11)	(11)
Gas Carried for PPL	(130)	(130)
Gas Carried for POL	(653)	(653)
Gas Internally Consumed (GIC)		
Metered	10,564	10,449
Unmetered	-	-
Total GIC	10,564	10,449
Available for External Sale	**613,853**	**613,968**
Sales		
Metered:		
Actual Billed	574,194	574,194
Minimum Billing	-	
Sticky / Stopped	331	331
Estimated	475	475
Gas Sold But Not Billed	-	-
Sub Total	**573,388**	**573,388**
Unmetered:		
Accrued Sales -Not Yet Billed	-	-
Total Sales	**573,388**	**573,388**
UFG in MMCF	**40,465**	**40,580**
UFG in Percentage	**6.59%**	**6.61%**

8.2.5. The Authority notes that the UFG volume statements submitted by the petitioner are not audited by the petitioner's external auditors.

8.2.6. The Authority adopts the UFG level of 40,580MMCF i.e; 6.61% tentatively, subject to adjustment on the basis of UFG audit to be commissioned by the Authority. Accordingly, the Authority provisionally disallows UFG above the UFG benchmark for the said year per its earlier decision mentioned above, which will reduce the operating expenditure by Rs. 700 million.

8.3. Transmission and Distribution Cost

i. Summary

8.3.1. The transmission and distribution cost is higher by 4% i.e. from Rs. 6,466 million per RERR2 to Rs. 6,739 million per the petition, as compared below:

Table 15: Comparison of T & D Cost with RERR2

				Rs. in million
Particulars	**FY 2005-06**		**Increase / (Decrease) over RERR 2 05-06**	
	RERR 2	**The Petition**	**Rs.**	**%**
Human Resource Cost	3,792	3,563	(229)	(6) %
Stores and Spares consumed	212	229	17	8 %
Fuel and Power	163	122	(41)	(25) %
Repair and Maintenance	320	386	66	21 %
Rent, Rate, electricity and Telephone	96	97	1	1 %
Insurance	162	135	(27)	(17) %
Traveling	66	71	5	7 %
Stationery, telegram and postage	45	42	(3)	(6) %
Dispatch of gas bills	17	21	4	22 %
Transport expenses	188	253	64	34 %
Legal and Professional services	22	24	2	10 %
Security expenses	115	183	68	59 %
Gathering charges of gas bills collection data	21	20	(1)	(3) %
Stores and spares written off -scrapping of meters	-	42	42	100 %
Provision for doubtful debts	200	174	(26)	(13) %
Provision for doubtful receivables	-	13	13	100 %
Loan from deceased employee written off	-	0.044	0.044	100 %
Gas bills collection charges	49	195	146	298 %
OGRA fee	90	70	(20)	(22) %
Other expenses	158	242	84	53 %
Subtotal Expenses	**5,717**	**5,882**	**166**	**3 %**
Allocated to fixed capital expenditures	(872)	(726)	146	(17) %
Net T&D Expenses before Gas Internally Consumed	**4,845**	**5,156**	**312**	**6 %**
Add: Gas internally consumed	1,621	1,583	(38)	(2) %
Total T&D Expenditure	**6,466**	**6,739**	**274**	**4 %**

8.3.2. Various components of operating cost are discussed in detail in the following paras.

ii. Human Resource Cost

8.3.3. The petitioner has claimed a decrease of 6% on account of HR cost for the said year from Rs. 3,792 million per RERR2 FY 2005-06 to Rs. 3,563 million per the petition.

8.3.4. The Authority notes that it had fixed a benchmark for HR cost (including all costs for permanent, contractual and casual / temporary employees) taking the actual HR cost of FY 2004-05 as base figure and indexed to increase in number of consumers with 60% weightage, increase in network with 20% weightage, gas sales volume with 20% weightage and allowed inflation adjustment to the extent of 50% of CPI subject to the condition that if the actual HR cost is higher than the benchmark HR cost, 50% of the amount will be adjusted in the revenue requirement and the balance 50% shall be absorbed by the petitioner from its own profits.

8.3.5. The Authority observes that the petitioner has booked cost of casual labour amounting to Rs. 60 million under the head "Repair & Maintenance" although, apparently the benchmark for HR cost covers these expenses therefore, the Authority directs the petitioner to provide its details so that its exact nature id ascertained. If found necessary, the Authority will re-adjust the HR cost for the said year, in FY 2006-07.

8.3.6. The Authority observes that the HR cost claimed by the petitioner is in excess by Rs. 10 million from the benchmark HR cost for the said year of Rs. 3,553 million.

8.3.7. ***In view of the above, the Authority deducts Rs. 5 million from the HR cost claimed by the petitioner, after equally sharing the excess cost between the consumers and the petitioner; and provisionally determines it at Rs. 3,558 million for the said year, subject to adjustment, if any, per para 8.3.5 above.***

iii. Gas Internally Consumed

8.3.8. The petitioner has claimed cost of the gas internally consumed (GIC) for the said year at Rs. 1,583 million as against Rs. 1,621 million per RERR2 2005-06, showing decrease of 2%. Historical comparison of GIC is provided below:

Table 16: Comparison of Gas Internally Consumed with RERR2 & Previous Year

					Rs. in million
Particulars	FY 2004-05	FY 2005-06		Inc. / (Dec.) over RERR 2 2005-06	
	FRR	RERR 2	FRR Petition		
Compression	1,209	1,503	1,466	(37)	(2) %
Free gas facility	78	90	104	14	15%
Others (incl H.O.)	11	21	14	(7)	(34) %
	1,299	**1,621**	**1,583**	**(38)**	**(2) %**

8.3.9. The Authority notes that although the GIC volumes are confirmed to be metered by the petitioner, yet it has provided three different GIC volume figures, i.e. 10,449 MMCF, 10,589 MMCF and 10,952 MMCF, in various statements submitted alongwith the petition, raising doubts about its authenticity.

8.3.10. The Authority, therefore, adopts the lowest submitted GIC volume of 10,449 MMCF subject to its verification by the external auditors of the petitioner.

8.3.11. It has been noted that the ratio of GIC to gas purchased has shown downward trend as under:

Table 17: Ratio of GIC to Gas Purchased

			Volumes in MMCF
FY	GIC	Gas purschased	Ratio of GIC to Gas Purchased
2003-04	9,712	494,766	1.96
2004-05	10,558	586,737	1.80
2005-06 (FRR)	10,449	624,779	1.67

This is indicative of the fact that after addition of larger diameter pipelines, the GIC is going down, as expected.

8.3.12. ***In view of the above discussion, the Authority determines the cost of GIC at Rs. 1,559 million.***

iv. Stores and Spares Written-off –Scrapping of Meters

8.3.13. The petitioner has claimed Rs. 42 million during the said year on account of stores and spares written off-scrapping of meters, which is compared below with previous years.

Table 18: Comparison of Provision for Unserviceable Meters with RERR2 & Previous Year

					Rs. in million	
Particulars	**FY 2003-04**	**FY 2004-05**	**FY 2005-06**		**Inc. / (Dec.) over RERR 2**	
	FRR	**FRR**	**RERR2**	**FRR Petition**		
Provision for unserviceable meters	25	-	-	42	42	100 %

8.3.14. The Authority observes that, admittedly, proper inventory record and tracking system of meters are not being maintained by the petitioner. OGRA's team had also visited the petitioner's meter service workshop previously and had arrived at similar conclusion. The petitioner has also not submitted the basis of computation of the claimed amount.

8.3.15. ***In view of above, the Authority provisionally disallows the expense under the head stores and spares written-off (scrapping of meters) subject to adjustment, if any, on receipt of the required information.***

v. Provision for Doubtful Receivables

8.3.16. The petitioner has claimed an amount of Rs. 13 million on account of Provision against Doubtful Receivables. The petitioner has submitted that this expense pertains to the Central Excise Duty (CED) imposed and recovered by the Excise Department for the said year against which no expense was projected at the time of RERR2 2005-06.

8.3.17. The Authority observes that the petitioner has paid the said duty under duress and the matter is under arbitration, yet to be finalized.

8.3.18. ***In view of the above, the Authority provisionally disallows the claimed expense of Rs. 13 million for the said year under this head, which will be considered once***

final decision of the tax authorities in this respect is communicated to the petitioner.

vi. Other Expenses

a) Loan to Deceased Employees Written-off

8.3.19. The petitioner has claimed Rs. 0.044 million on account of loan to deceased employees, written-off during the said year, as operating expense.

8.3.20. The petitioner, subsequently, informed that the said expense has been erroneously claimed by it.

8.3.21. ***The Authority, therefore, disallows Re. 0.044 million on account of loans to deceased employees written-off for the said year.***

b) Others

8.3.22. The petitioner has claimed Rs. 8 million as other expenses for the said year, but has not provided break-up of these expenses. It, however, has informed that it is the petty cash expenditure incurred at various company locations and comprises of thousands of petty cash vouchers. It has undertaken to provide break-up after acquiring the details from the regions.

8.3.23. ***The Authority, due to lack of justification, provisionally disallows 50% of the expense i.e. Rs. 4 million on this account for the said year subject to adjustment, if any, on the basis of the details provided by the petitioner in respect of all such expenses that fulfill the requirement of Rule 17 (1) (H) OF NGT Rules, 2002.***

vii. Remaining Items of Transmission & Distribution Cost

8.3.24. The items of transmission and distribution cost, except those dealt with in para's .3.1 to 8.3.23 above, are claimed by the petitioner at Rs. 2,260 million as against Rs. 1,885 million per RERR 2 2005-06, showing increase of 20%. The comparative analysis is given below:

Table 19: Remaining Items of Transmission & Distribution Expenses

				Rs. in million
Particulars	**FY 2005-06**		**Increase / (Decrease) over RERR 2 05-06**	
	RERR 2	**The Petition**	**Rs.**	**%**
Stores and Spares consumed	212	229	17	8 %
Fuel and Power	163	122	(41)	(25) %
Repair and Maintenance	320	386	66	21 %
Rent, Rate, electricity and Telephone	96	97	1	1 %
Insurance	162	135	(27)	(17) %
Traveling	66	71	5	7 %
Stationery, telegram and postage	45	42	(3)	(6) %
Dispatch of gas bills	17	21	4	22 %
Transport expenses	188	253	64	34 %
Legal and Professional services	22	24	2	10 %
Security expenses	115	183	68	59 %
Gas bill collection charges	49	195	146	298 %
Gathering charges of gas bills collection data	21	20	(1)	(3) %
Provision for doubtful debts	200	174	(26)	(13) %
OGRA fee	90	70	(20)	(22) %
Other expenses	118	238	120	102 %
Total T&D Expenditure	**1,885**	**2,260**	**375**	**20 %**

8.3.25. The petitioner has submitted that the increase is owing to ongoing expansion in its T&D network, increased activities for UFG control, increased rentals and fuel cost.

8.3.26. ***The Authority accepts the remaining items of T&D cost at Rs. 2,260 million.***

viii. Transmission & Distribution Cost Determined by Authority

8.3.27. In view of the above, the Authority determines transmission & distribution cost for the said year at Rs. 6,651 million against Rs. 6,739 million claimed by the petitioner, as follows:

Table 20: Summary of T&D Cost Determined by the Authority

		Rs. in million
Particulars	**Requested by the Petitioner**	**Determined by OGRA**
Human resource cost	3,563	3,558
Stores and spares consumed	229	229
Fuel and power	122	122
Repair and maintenance	386	386
Rent, rate, electricity and telephone	97	97
Insurance	135	135
Traveling	71	71
Stationery, telegram and postage	42	42
Dispatch of gas bills	21	21
Transport expenses	253	253
Legal and professional services	24	24
Security expenses	183	183
Gathering charges of gas bills collection data	20	20
Stores and spares written off -scrapping of meters	42	-
Provision for doubtful debts	174	174
Provision for doubtful receivables	13	-
Loan from deceased employee written off	0.044	0.044
Gas bills collection charges	195	195
OGRA fee	70	70
Other expenses	242	238
Subtotal Expenses	**5,882**	**5,818**
Allocated to fixed capital expenditures	(726)	(726)
Net T&D Expenses before Gas Internally Consumed	**5,156**	**5,092**
Add: Gas internally consumed	1,583	1,559
Total T&D Expenditure	**6,739**	**6,651**

8.4. Workers Profit Participation Fund (WPPF)

8.4.1. The petitioner has claimed WPPF at Rs. 292 million. However, due to adjustments in the components of revenue requirements as discussed in paras 6 to 8.3 above, WPPF is recalculated and allowed at Rs. 236 million.

9. Decision

9.1. ***In view of the justifications submitted and arguments advanced by the petitioner in support of its petition, scrutiny by the Authority and reasons recorded in earlier paras, the Authority recapitulates and decides:***

9.1.1. ***to allow addition in fixed assets at Rs. 5,560 million and to reduce depreciation expense by Rs. 305 million;***

9.1.2. ***to increase deferred credit closing balance by Rs. 133 million;***

9.1.3. ***to increase operating income by Rs. 7 million;***

9.1.4. ***to restrict the UFG per the benchmark and make a downward adjustment of Rs. 700 million in the operating expenses;***

9.1.5. ***to decrease the T&D expenses to Rs. 6,651 million as against Rs. 6,739 million claimed by the petitioner;***

9.1.6. ***to determine cost of gas at Rs. 92,009 million;***

9.1.7. ***to reduce WPPF to Rs. 236 million as against Rs. 292 million claimed by the petitioner;***

9.2. ***In exercise of its powers under Section 8(2) of the Ordinance, the Authority determines the final revenue requirement for the said year at Rs. 107,765 million as against petitioner's claim of Rs. 108,168 million, (thus, reducing it by Rs. 403 million), as tabulated below:***

Table 21: Components of FRR for FY 2005-06 as Determined by the Authority

		Rs. in million
Estimated Revenue Requirement FY 2005-06	**Claimed by the Petitioner**	**Determiend by the Authority**
Cost of gas	91,986	92,009
Disallowance on account of UFG	(681)	(700)
Transmission & distribution cost	5,156	5,092
Gas internally consumed	1,583	1,559
Exchange Loss	32	32
Deprectiation	4,066	3,761
CNG Station Lillah Town	-	31
Workers participation fund	292	236
Return on net operating fixed assets	5,734	5,746
Total Estimated Revenue Requirement	**108,168**	**107,765**

9.3. ***The petitioner's actual net operating income is Rs. 108,940, and thus there is a surplus of Rs. 1,175 million vis a viz its revenue requirement for the said year. In order to adjust this surplus, the Authority hereby revises the average prescribed price downwards by Rs. 2.18 per MMBTU (Annexure-A). Revised prescribed prices for each category of retail consumers for FY 2005-06 are attached and marked Annexure-B.***

(M.H. Asif)	(Rashid Farooq)	(Jawaid Inam)
Member (Finance)	Member (Oil)	Member Gas) / Vice Chairman

(Munir Ahmad)

Chairman

Islamabad,
September 18, 2006

A. Revenue Requirement for FY 2005-06

	Particulars	RERR 2	The Petition	Additions / (deductions) by OGRA	Determined by OGRA
					Rs. in million
	Gas sales volume -MMCF	533,630	571,481		571,481
	BBTU	499,479	539,099		539,099
	Calorific Value	936	943		943
"A"	**Net Operating revenues**				
	Net sales at current prescribed price	91,439	107,027	-	107,027
	Rental & service charges	730	745		745
	Surcharge and interest on arrears	575	534	-	534
	Amortization of deferred credit	545	473	4	477
	Other operating income	65	154	3	157
	Total income "A"	**93,354**	**108,933**	**7**	**108,940**
"B"	**Less Expenses**				
	Cost of gas sold	83,715	91,986	22.5	92,009
	UFG (disallowance) / alloawance	(108)	(681)	(19)	(700)
	Transmission and distribution cost	4,845	5,156	(64)	5,092
	Gas internally consumed	1,621	1,583	(24)	1,559
	Depreciation	4,229	4,066	(305)	3,761
	Defferal account / price adjustment account	170	-		-
	CNG Station at Lillah Town		-	31	31
	(W.P.P.F)	245	292	(56)	236
	Exchange loss on purchase of gas from E&P Companies		32		32
	Total expenses "B"	**94,717**	**102,434**	(469)	**102,019**
"C"	**Operating profit / (loss)(A - B)**	**(1,363)**	**6,499**	**476**	**6,921**
	Return required on net assets:				
	Net assets at beginning	36,140	36,975	-	36,975
	Net assets at ending	38,580	38,307	273	38,580
		74,720	75,282		75,555
	Average fixed net assets (I)	**37,360**	**37,641**		**37,778**
	Deferred credit at beginning	5,325	4,432		4,432
	Deferred credit at ending	7,180	5,323	133	5,456
		12,505	9,755		9,888
	Average net deferred credit (II)	**6,253**	**4,878**		**4,944**
"D"	**Average operating assets (I-II)**	**31,108**	**32,764**		**32,834**
	Return required on net assets	17.5%	17.5%		17.5%
"E"	Amount of return required	5,444	5,734		5,746
"F"	Excess / (shortfall) over return required	(6,806)	765		1,175
	Total Revenue Requirement	**100,161**	**108,168**	(403)	**107,765**
					Rs. / MMBTU
	(Increase) / Decrease in average prescribed price (Rs. / MMBTU)	-	**1.42**		**2.18**

B. Prescribed Prices Determined by OGRA

		Rupees per MMBTU			
		Provisional	Final	Provisional	Final
		01.07.2005 to 31.12.2005		01.01.2006 to 30.06.2006	
(i)	**Domestic Consumers:**				
	For domestic consumers, including residential colonies, mosques, churches, temples, madrassas, other religious places and hostels attached thereto, Government and semi-Government offices, hospitals, Government guest houses, Armed Forces messes and langars, universties, colleges, schools, private educational institutions, orphanages and other charitable institutions.				
	First slab (upto 100 cubic metres per month).	**73.95**	**73.95**	**80.98**	**80.98**
	Second slab (over 100 upto 200 cubic metres per mor	**127.62**	**127.62**	**147.41**	**147.41**
	Third slab (over 200 upto 300 cubic metres per mon	**204.17**	**204.17**	**235.84**	**235.84**
	Fourth slab (All over 300 cubic metres per month).	**265.59**	**265.59**	**306.79**	**306.79**
	For hostels and residential colonies to whom gas is supplied through bulk meters.				
	All off-takes at flat rate of	**127.62**	**127.62**	**147.41**	**147.41**
(ii)	**Commercial Consumers:**				
	All establishments registered as commercial units with local authorities or dealing in consumer items for direct commercial sale like cafes, milk shops, tea stalls, canteens, barber shops, laundries, tandours, places of entertainment like cinemas, clubs, theaters and private offices, clinics, maternity homes, etc.				
	All off-takes at flat rate of	**234.67**	**231.56**	**271.07**	**267.48**
(iii)	**Ice Factories:**				
	All off-takes at flat rate of	**234.67**	**231.56**	**271.07**	**267.48**
(iv)	**Industrial Consumers:**				
	All consumers engaged in the processing of industrial raw material into value added finished products irrespective of the volume of gas consumed including hotel industry but excluding such industries for which a separate rate has been prescribed.				
	All off-takes at flat rate of	**208.56**	**205.79**	**240.91**	**237.72**
(v)	**Captive Power :**				
	All off-takes at flat rate of	**208.56**	**205.79**	**240.91**	**237.72**
(vi)	**CNG Stations:**				
	All off-takes at flat rate of	**208.56**	**205.79**	**240.91**	**237.72**
(vii)	**Cement Factories:**				
	All off-takes at flat rate of	**240.28**	**237.09**	**277.55**	**273.87**

viii)	`	**Fertilizer Factories:**				
(1)	**Pak American Fertilizer Limited, Daudkhel.**					
	(a)	**For gas used as feed stock for fertilizer**				
		Commodity charge.				
		All off-takes at flat rate of	**36.77**	**36.77**	**36.77**	**36.77**
	(b)	**For gas used as fuel for generating steam and electricity and for usage in**				
		Commodity charge.				
		All off-takes at flat rate of	**208.56**	**205.79**	**240.91**	**237.72**
(2)	**Pak Arab Fertilizer Limited, Multan.**					
	(a)	**For gas used as feed stock for fertilizer**				
		Commodity charge.				
		All off-takes at flat rate of	**83.24**	**83.24**	**83.24**	**83.24**
	(b)	**For gas used as fuel for generating steam and electricity and for usage in**				
		Commodity charge.				
		All off-takes at flat rate of	**208.56**	**205.79**	**240.91**	**237.72**
(3)	**Dawood Hercules Chemicals Limited, Chichoki Malian, Sheikhupura District:**					
	(a)	**For gas used as feed stock for fertilizer**				
		Commodity charge.				
		All off-takes at flat rate of	**83.24**	**83.24**	**83.24**	**83.24**
	(b)	**For gas used as fuel for generating steam and electricity and for usage in**				
		Commodity charge.				
		All off-takes at flat rate of	**208.56**	**205.79**	**240.91**	**237.72**
(4)	**Pak-China Fertilizer Limited/Hazara Phosphate Plant Limited, Haripur.**					
	(a)	**For gas used as feed stock for fertilizer**				
		Commodity charge.				
		All off-takes at flat rate of	**88.34**	**88.34**	**88.34**	**88.34**
	(b)	**For gas used as fuel for generating steam and electricity and for usage in**				
		Commodity charge.				
		All off-takes at flat rate of	**208.56**	**205.79**	**240.91**	**237.72**

(ix)		**Power Stations:**					
	(a)	*WAPDA's Power Stations and other electricity utility companies excluding WAPDA's Natural Gas Turbine Power Station, Nishatabad, Faisalabad.*					
		All off-takes at flat rate of	**208.56**	**205.79**	**240.91**	**237.72**
	(b)	*WAPDA's Natural Gas Turbine Power Station, Nishatabad, Faisalabad.*					
		Commodity Charge					
		All off-takes at flat rate of	**208.56**	**205.79**	**240.91**	**237.72**
		Fixed charge (Rupees per month).	**390,000**	**390,000**	**390,000**	**390,000**
	(c)	Liberty Power Limited.					
		All off-takes at flat rate of	**262.03**	**262.03**	**303.25**	**303.25**