No. OGRA-6(2)-1(2)/2011-DTRR

IN THE MATTER OF

SUI NORTHERN GAS PIPELINES LIMITED
FINAL REVENUE REQUIREMENT, FY 2010-11

UNDER

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

DECISION

September 21, 2011

Before:

Mr. Sabar Hussain, Acting Chairman/ Member Oil
Mir Kamal Marri, Member (Finance)
Mr. Mansoor Muzaffar Ali, Member (Gas)

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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, sale of natural gas and gas condensate (as a by-product).

1.2. The petitioner filed a petition on August 14, 2011 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 2010-11 (the said year) on the basis of accounts, as initialed by its statutory auditors.

1.3. The petitioner has submitted the 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 in terms of Section 8(2) of the Ordinance. The petitioner has made some other claims including Unaccounted for Gas UFG at 7% and Late Payment Surcharge (LPS), gain on construction contracts and income from recoating of SSGCL pipeline as non-operating incomes. The petitioner has also included Rs. 358 million (the amounts have been rounded off to the nearest million here and elsewhere in this document) exchange loss due to variation in Dollar vs. Rupee parity on account of payment of cost of gas. Out of this amount, Rs. 302 million pertains to FY 2009-10, which was erroneously omitted at that time and hence not claimed in FRR FY 2009-10. The petitioner has worked out its FRR for the said year at Rs. 197,444 million for actual sale volume of 547,502 BBTU. Based on the provisional prescribed prices and actual sale mix, the petitioner has computed a shortfall of Rs. 8,467 million for the said year thereby seeking increase in the average prescribed price by Rs. 15.46 per MMBTU.

1.4. The Authority, vide its order dated December 2, 2010, had determined the petitioner's Revised Estimated Revenue Requirement (RERR) for the said year under Section 8(2) of the Ordinance at Rs. 205,119 million for estimated sale volume of 619,621 BBTU.

1.5. The petitioner challenged the RERR in the honorable Lahore High Court (LHC) in terms of treatment of LPS as non-operating income and relaxation of UFG up to 7% on the plea that the same treatment was allowed in FRR FY 2009-10 by the Authority. The LHC granted interim relief to the petitioner. The said LHC decision was implemented by the Authority and accordingly RERR was revised at Rs. 209,478 million by increasing the average prescribed prices by Rs. 11.78 per MMBTU.

1.6. The Authority issued notice of hearing on August 29, 2011 to the petitioner and the following interveners and related parties:

a) Federal Government (FG / GoP) - GoP.

b) Mr. Zubair Ansari, Secretary, All Pakistan Textile Processing Mills Association, Faisalabad.

c) Mr. Rashid Mehmood, Secretary General, All Pakistan CNG Association, Rawalpindi.

d) Mr. Mehmood Elahi Engineers, Sui Gas Contractors, Faisalabad.

e) Nasra Gillani, Chief Executive Officer, Consumer Awareness and Welfare Association, Lahore.

1.7. The hearing was held at Islamabad Hotel, Islamabad on September 14, 2011.

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 RERR & Previous Year

Rs. Per MMBTU

Particulars	FY 2009-10 FRR	FY 2010-11 RERR	FY 2010-11 RERR (Per Court Order)	FY 2010-11 FRR (The Petition)
Units sold (BBTU)	**547,863**	**619,621**	**619,621**	**547,502**
Cost of gas sold	261.62	296.91	296.91	311.41
Transmission and distribution cost	9.93	7.33	14.37	17.28
Depreciation	12.43	13.02	13.02	13.98
Return on net average operating fixed assets	16.24	13.77	13.77	17.96
Prior Year Adjustment FRR 2008-09	15.01	-	-	-
Prior Year Adjustment FRR 2007-08	3.10	-	-	-
Other Operating income	(5.75)	(7.02)	(4.13)	(7.00)
Cost of service / Prescribed price	**312.58**	**324.02**	**333.95**	**353.63**
Current average prescribed price	312.58	324.02	333.95	338.17
Increase requested in the average prescribed price.	**-**	**-**	**-**	**(15.46)**

2.2. The petitioner has made the following submissions:

2.2.1. 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, per license condition no. 5.2 and as guaranteed by the GoP 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. 12,085 million and net addition, after accounting for deletion and depreciation, at Rs. 4,428 million, resulting in claimed increase in net operating fixed assets from Rs. 72,028

million in FY 2009-10 to Rs. 76,469 million. After adjustment of deferred credit, the average value of operating fixed assets eligible for return work out to Rs. 56,184 million and the required return at Rs. 9,832 million.

2.2.3. Total operating revenues have been claimed at Rs. 188,978 million in the petition, as against Rs. 209,478 million in RERR, as detailed below:

Table 2: Comparison of Operating Revenues with RERR & Previous Year

Rs. in million

Description	FY 2009-10	FY 2010-11			Increase / (Decrease) over RERR per Court Order	
	FRR	RERR	Per Court Order	The Petition		
Net sales at current prescribed price	171,253	200,769	206,922	185,148	(21,774)	-11%
Rental & Service Charges	1,091	1,050	1,050	1,126	76	7%
Surcharge and Interest on arrears	-	1,501	-	-	-	-
Amortization of deferred credit	1,801	1,281	1,281	2,514	1,233	96%
Other operating income	258	518	225	190	(35)	-16%
Net Operating Revenues	**174,403**	**205,119**	**209,478**	**188,978**	**(20,500)**	**-10%**

2.2.4. Net operating expenses have been claimed at Rs. 187,613 million in the petition as compared to Rs. 200,945 million provided in RERR, as detailed below:

Table 3: Comparison of Operating Expenses per the petition with RERR & Previous Year

Rs. in million

Description	FY 2009-10	FY 2010-11			Increase / (Decrease) over RERR	
	FRR	RERR	RERR (Per Court Orders)	The Petition		
Cost of gas	143,333	183,974	183,974	170,500	(13,474)	-7%
Transmission and Distribution costs	7,492	9,205	9,205	12,221	3,016	33%
UFG disallowance above allowable limit	(4,670)	(7,334)	(2,975)	(5,281)	(2,306)	78%
Gas Internally Consumed (GIC)	2,287	2,555	2,555	1,878	(677)	-26%
Depreciation	6,810	8,069	8,069	7,654	(415)	-5%
Other Charges including WPPF	330	116	116	640	524	452%
Net Operating Expenses	**165,508**	**196,586**	**200,945**	**187,613**	**(13,332)**	**-7%**

2.2.5. UFG has been reported at 10.10% (67,143 MMSCF) and UFG disallowance has been claimed at 7%, as against the upper & lower target of 5.0% and 4.25% respectively, fixed by the Authority for the said year.

2.2.6. Net result of the petitioner's above mentioned claims is that there is a shortfall of Rs. 8,467 million after allowing 17.5% return on average net operating assets, which translates to an increase of Rs. 15.46 per MMBTU in the existing average prescribed price, as tabulated below:

Table 4: Computation of Average Increase in Prescribed Price per the petition

	Description	Rs. in million
A	Net operating revenues	188,978
B	Less: Net operating expenses including WPPF	187,613
C	Shortfall / (excess) (A – B)	(1,365)
D	Return required @ 17.5% on net fixed assets in operation.	9,832
E	Total shortfall /(excess) in the revenue requirement (C + D)	8,467
F	Sales volume (BBTU)	547,502
	Increase in the existing average prescribed price (Rs./MMBTU) (E / F * 1000)	**15.46**

3. Proceedings

3.1. The petitioner was represented at the hearing by a team of senior executives led by its Managing Director, Mr. Arif Hameed, who were given full opportunity to present the petition. They made submissions in detail with the help of multimedia presentation. They also answered the questions raised by Chairman, Members and officers of the Authority.

3.2. The following interveners / representatives of the interveners also attended the hearing:

i) Mr. Saeed A Khokhar, Consultant Oil & Gas Energy.

ii) Mr. Muhamamd Ashiq, Deputy Director (Gas), Ministry of Petroleum & Natural Resources, Islamabad.

iii) Mr. Hassan Mehmood, Financial Analyst, Ministry of Petroleum & Natural Resources, Islamabad.

iv) Mr. Shahid H. Jafri, CFO, Sui Southern Gas Company Limited.

v) Mr. Ghulam Mustafa Qazi, Consultant, TMRC, Islamabad.

vi) Mr. Ghulam Qadir Awan, Consultant, TMRC, Lahore

vii) Mr. Karar Hussain Zahidi, Consultant, TMRC, Islamabad.

viii) Mr. Mehmood Elahi, Sui Gas Contractor, Faisalabad.

4. Determination

4.1. After detailed scrutiny of the petition, and clarifications given before, during and after the hearing by the petitioner, the Authority determines as follows:

5. Return to Licensee

5.1. The Authority is obligated under Section 7(1) of the Ordinance, to determine or approve tariff for regulated activities whose licenses provide for such determination or such approval, or where authorized by this Ordinance, subject to policy guidelines. *License Condition No. 5.2* of license granted to the petitioner, clearly states that *the Authority shall determine* total revenue requirement of the licensee to ensure that it achieves 17.5% return on its average net fixed assets in operation for each financial year, subject to the efficiency related benchmarks adjustments. The Authority, accordingly, has been determining the revenue requirement of the petitioner, providing the said return on net operating assets in accordance with the said provision of the Ordinance as well as the petitioner's license.

5.2. The Authority, may, however, in consultation with GoP and the licensee prescribe revised rate of return or a different basis for determination of return, pursuant to *Licence Condition No. 5.3* of the Licence granted to the petitioner. The Authority has developed a new tariff regime for regulated natural gas sector of Pakistan, which, in the course of legally mandatory consultation process, has been pending with GoP. The proposed tariff regime is similar to the existing tariff regime however; it has been designed to operate on market based rate of return and excludes some activities from the ambit of "regulated activities", presently carried out by the gas utilities.

5.3. In order to carry out a meaningful consultative session on the above said issue, the Authority decided to hold public hearings through which all the stakeholders including FG, SNGPL/SSGCL, consumers, interested/affected persons and parties were invited to furnish their comments. Accordingly public hearings in the matter were held in Karachi and Lahore, where effective participation of stakeholders from various sectors of economy was witnessed, and valuable and productive feedback was received. The participants and the FG were of the opinion that the matter being of very critical nature, having major impact on the overall economic scenario, needs detailed deliberations. Therefore, they requested the Authority to provide additional time for submission of detailed comments. The FG also specifically stated that the matter may not be finalized till receipt of their comments, which are awaited to date.

5.4. *In view of the above situation, the Authority has decided, to follow the existing basis of 17% return on the average net operating fixed assets while treating various income and expenditure heads per the exiting regime, in accordance with the Licence Condition No. 5.2.*

6. Operating Fixed Assets

6.1. Summary

6.1.1. Gross addition in fixed assets during the said year has been claimed at Rs. 12,085 million and net addition, after accounting for deletion and depreciation, at Rs. 4,428 million, increasing the net operating fixed assets from Rs. 72,028 million in FY 2009-10 to Rs. 76,469 million. After adjustment of deferred credit, the average value of operating fixed assets has been claimed at Rs. 56,184 million and the required return at Rs. 9,832 million. The petitioner has adjusted Rs. 13 million as net addition during the said year on account of IT related expenditures disallowed by the Authority in previous years. The computation of return on fixed assets tabulated below:-

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

Rs. in million

Description	The Petition
Net operating fixed assets at beginning	72,028
Net operating fixed assets at closing	76,469
Sub Total	148,497
Average net assets (A)	**74,249**
Deferred credit at beginning	17,842
Deferred credit at closing	18,288
Sub Total	36,130
Average deferred credit (B)	**18,065**
Average net fixed assets (A-B)	**56,184**
Return required	17.5%
Amount of return requested by the petitioner	**9,832**

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

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

Rs. in million

Particulars	FY 2009-10	FY 2010-11		Inc./(Dec.) Over RERR	
	FRR	RERR	The Petition		
Land & Building	80	120	205	85	71%
Transmission	4,551	1,034	1,739	705	68%
Compression	565	20	349	329	1645%
Distribution Development	9,570	9,124	6,598	(2,526)	-28%
Measuring & Regulating Assets		1,304	2,329	1,025	79%
Telecommunication	68	670	32	(638)	-95%
UFG assets	158	-		-	
Normal Assets	522	674	479	(195)	-29%
Land Acquisition Advance	95	-	7	7	
Intangible Assets	-	-	346	346	
Net addition in asset base	**15,610**	**12,947**	**12,085**	**(862)**	**-6.66%**

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

Table 7: Detailed Schedule of Additions per the petition

Particulars	Rs. in million
Land & Buildings	171
Civil Construction	34
Transmission	1,739
Compression System & Equipment	349
Distribution System	6,598
Measuring & Regulating Assets	2,329
Telecommunication	32
Intangible Assets (I.T related Expenditures)	346
Land Acquisition Advance	7
Normal & other Assets	
Plant & Machinery	212
Construction Equipments	104
Tools & Equipment	14
Motor Vehicle	48
Furniture & Fixture	9
Office Equipments	16
Computer Hardware	75
Scada System	1
Sub-Total	479
Total Addition For FY 2010-11	**12,085**

6.2. Transmission

6.2.1. The petitioner has claimed Rs. 1,739 million on account of capitalization of "Transmission" as against Rs. 1,034 million provided in RERR for the said year.

6.2.2. The petitioner has capitalized a number of smaller projects during the said year which primarily correspond to left over work of giga Project–IX and others. Petitioner has elaborated that it has completed different segments of transmission pipeline during the said year thereby increasing the transmission network by approximately 151 kilometers which included 24" dia River Ravi crossing, 12" dia Mandi Bahaudin- Lala Musa pipeline, 8" dia Khangarh-Alipur Kalarwali, 8" dia Piplan-Aluwali and 8" Sahiwal-Farooqa Sillanwali pipeline. The petitioner has also constructed allied installations of SMS, connected pipelines and compressions as an integral part above said extension in the network.

6.2.3. The Authority observes that the capitalization claimed under "transmission" during the said year is mostly the left over work of main projects, and is essentially required to operate the system smoothly.

6.2.4. *The Authority, in view of above, allows Rs. 1,739 million as capitalization of transmission network for the said year.*

6.3. Compression System

6.3.1. The petitioner has claimed Rs. 349 million on account of capitalization under the head "Compression", as against Rs. 20 million provided in RERR for the said year. Petitioner has explained that above amount claimed for capitalization comprises left over work of overhauling/ maintenance and rehabilitation of compressor package, which were earlier approved by the Authority during FY 2006-07 and 2007-08. The main chunk of such projects has already been capitalized during last years. Remaining left over work correlated with the current transmission extension has been completed this year.

6.3.2. The Authority observes that the blanket approval of phasing out of compressor package, multicyclone filters and some other related projects was conveyed to the petitioner earlier. During FY 2005-06 and onward the petitioner has completed major part of such projects. The claimed capitalization during the said year is left over work of the main projects, which is crucial for smooth operation.

6.3.3. *The Authority, in view of above, allows Rs. 349 million under the head "Compression" for the said year.*

6.4. Distribution Development

6.4.1. The petitioner has claimed Rs. 8,927 million on account of capitalization of "Distribution Development" as against Rs. 11,463 million provided in RERR for the said year. Details of which are provided below:

Table 8: Detailed Schedule of Addition in Distribution Development per the petition

Rs. in million

Description	FY 2010-11 (RERR)	FY 2010-11 (The Petition)	Inc/Dec over RERR
Distribution System Mains	8,812	6,281	(2,531)
Rehabilitation of distribution system	312	318	6
Installation of new connections	1,095	1,325	230
Construction of SMS/TBS/DRS	399	175	(224)
Replacement of defective meters	594	828	234
Regulating System	31	-	(31)
C.P. System	220	-	(220)
Total	**11,463**	**8,927**	**(2,536)**

6.4.2. The petitioner has stated that it has initially projected Rs. 13,613 million for about 5,000 Km extension in distribution network, connections to new towns & villages and up-gradation of CMS/SMSs for the said year at the time of DERR. The Authority, however, allowed Rs. 11,463 million keeping in view historical capitalization trend and the petitioner's capacity to undertake such projects in the said year.

6.4.3. The petitioner elaborated that the FG during the said year maintained the sale prices at the level of DERR FY 2010-11 which created revenue shortfall, resulting in paucity of funds to undertake the said projects. Therefore the petitioner could only complete the ongoing projects during the said year.

6.4.4. The Authority has earlier decided in the determination of ERR for FY 2011-12 dated May 24, 2011 of the petitioner that new development phases will only be included in the asset base if and only if, the petitioner can establish availability of additional gas supply for the same. The ongoing projects, for which GoP funding has been received and work has also been initiated, will however be allowed. Since the said distribution extension pertains to existing development phases, the same is accordingly allowed for capitalization for the said year.

6.4.5. The Authority further notes that development of new towns and villages is being carried out per the honorable Prime Minister's directives. The Authority therefore, decides to allow future development phases. Since this issue is primarily of policy nature, on which FG policy guidelines are also required, the Authority is separately moving a case seeking policy advice from FG in this regard.

6.4.6. *In view of above and after due diligence and detailed examination of the submissions made by the petitioner, the Authority allows Rs. 8,927 million on account of distribution development for the said year, as sought by the petitioner.*

6.5. Normal & Other Assets

6.5.1. The petitioner has claimed Rs. 479 million under the head "Normal & other assets" as against Rs. 674 million provided in RERR for the said year. *The Authority, in view of the fact that capitalization under this head remained within the earlier allowed limit, allows Rs. 479 million as sought by the petitioner.*

6.5.2. The Authority observes that the petitioner has claimed Rs. 178 million on account of "Purchase of Land & Land Acquisition Advance", Rs. 32 million on account of telecommunication, Rs. 34 on account of civil construction as addition to fixed assets, and *the same is allowed in accordance with the previous practice.*

6.6. IT Related Expenditure

6.6.1. The petitioner has claimed Rs. 420 million comprising addition of Rs. 346 million IT related expenditure on account of its CC&B & ERP modules during said years while Rs. 74 million pertains to previous years.

6.6.2. The petitioner has elaborated that it has taken the IT project on fast track basis during the said year. Accordingly, the CC&B system has been completed and fully implemented while most of the modules of ERP system have also been completed.

6.6.3. The petitioner has also explained that it has now overcome the complaints regarding computational billing errors, incorrect GCV reporting and delay in issuance of bills, pointed out since the launch of CC&B system. The system is now fully functional and operating successfully. Also the ORACLE Financials upgrade and regional roll outs has been successfully implemented.

6.6.4. The Authority, keeping in view the claims of the petitioner, observes that although significant efforts to rectify a number of teething issues along with advancement in respect of automation of manual based gas supply system have been made, however, IT automaton is a long term project which will take time to achieve the amenable results. The Authority notes with concern that further extensive efforts to bring the billing errors, GCV issues and unbilled consumers, within acceptable limits, are required. Other modules of ERP system including Inventory, HR etc, have not been implemented within the timelines. IT system is, therefore, still not generating the automated and effective reports to assist the decision making system. Progress on Uniform System of Accounts implementation is also far from the satisfaction.

6.6.5. The Authority reiterates that IT related expenditure is a complete package for customer facilitation and automated reporting. The analysis of this package cannot be done until the petitioner establishes the ERP and CC&B benchmarks along with Key Performance Indicators and cost benefit analysis for evaluating the efficiency of this project before and after implementation. The requisite information is still pending.

6.6.6. *The Authority, therefore, directs the petitioner to submit within three months, the long awaited ERP and CC&B benchmarks, cost benefit analysis and performance indicators for measuring the efficiency of the project before and after the implementation. Also, the implementation status of the above said pending or partially implemented modules be provided within three months period.*

6.6.7. *Accordingly the Authority allows Rs. 420 million in this account on adhoc basis which will be subject to comprehensive review after the submission of requisite reports by the petitioner.*

6.6.8. *In view of the above, the Authority determines the addition in fixed assets during said year at Rs. 12,085 plus Rs. 13 million on account of previous year IT related expenditure. After adjustment of depreciation and deletion, net addition comes to Rs. 4,441 million and the closing net operating fixed assets for the said year are determined at Rs. 76,469 million.*

7. Operating Revenues

7.1. Sales Volume

7.1.1. The sales volume has dropped to 547,502 BBTU, witnessing a decrease of 12% for the said year, as against 619,621 BBTU per RERR. Category-wise comparison with previous year has been provided by the petitioner as under:

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

Volume in BBTU

Category	FY 2009-10	2010-11		Inc./ (Dec.) over RERR	
	FRR	RERR	The Petition		
Power	148,721	189,501	148,018	(41,483)	(22) %
Cement	-	-	608	608	-
Fertilizer	43,451	73,941	39,846	(34,095)	(46) %
General Industries	120,039	88,421	104,280	15,859	18 %
CNG	72,013	78,184	82,945	4,761	6 %
Commercial	25,256	27,178	25,087	(2,091)	(8) %
Domestic	138,383	162,395	146,718	(15,677)	(10) %
Total	**547,863**	**619,621**	**547,502**	**(72,119)**	(12) %

7.1.2. The petitioner has explained that gas sale volume has reduced by 12% due to lesser off-takes from various fields and decrease in gas availability owing to enhanced pilferage / non- consumers and large scale disaster to gas network, during the said year.

7.1.3. The petitioner elaborated that it has faced severe shortage of gas owing to which the demand of various categories of the consumers could not be met during the said year. The available gas, however, was supplied to consumers in accordance with the load management policy, issued by the FG. The FG, during the said year, increased the gas

supply to general industry in order to protect it from force closure, which could have lead to economic distortion in the country. Resultantly the other categories of consumers, mainly the fertilizer sector, have faced the scarcity of gas supply during the said year.

7.1.4. *In view of the justifications advanced by the petitioner, the Authority accepts the sales volume at 547, 502 BBTU for the said year.*

7.2. Sales Revenue at Existing Prescribed Prices

7.2.1. Sales revenue at existing prescribed prices has decreased to Rs. 185,148 million for the said year as compared to Rs. 206,922 million per RERR. Category-wise comparison with RERR and previous year is given below:

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

Rs. in million

Category	FY 2009-10	FY 2010-11		Inc./ (Dec.) over RERR	
	FRR	RERR	The Petition		
Power	54,400	77,094	59,769	(17,325)	-22%
Cement		-	328	328	
Fertilizer	6,144	10,394	6,248	(4,146)	-40%
General Industries	41,551	33,948	39,512	5,564	16%
CNG	33,372	39,533	42,156	2,623	7%
Commercial	10,770	12,651	11,709	(942)	-7%
Domestic	25,018	33,303	25,427	(7,875)	-24%
Total	**171,253**	**206,922**	**185,148**	**(21,774)**	**-11%**

7.2.2. The Authority observes that decrease in sale volume is due to the reasons recorded in paras 7.1.2 & 7.1.3 above.

7.2.3. The Authority also observes that the FG maintained the natural gas sale prices at the level of 1st July 2010 during the said year, which were otherwise to be increased owing to the LHC Orders in field, discussed in para 1.5 above. This resultantly has decreased sales revenue, despite increase in revenue requirement, thereby creating an unadjusted shortfall even after absorbing available GDS during the said year.

7.2.4. *In view of above, the Authority accepts the sales revenue at Rs. 185,148 million for the said year as claimed by the petitioner.*

7.3. Other Operating Income

i. Summary

7.3.1. The petitioner has claimed other operating income at Rs. 3,830 million for the said year as against Rs. 2,556 million per RERR. Item-wise comparison is as under:

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

Rs. in million

Description	FY 2009-10	FY 2010-11			Increase / (Decrease) over RERR	
	FRR	RERR	Per Court Order	The Petition		
Rental & Service Charges	1,091	1,050	1,050	1,126	76	7%
Surcharge and Interest on arrears	-	1,501	-	-	-	0%
Amortization of deferred credit	1,801	1,281	1,281	2,514	1,233	96%
Other operating income	258	518	225	190	(35)	-16%
Net Operating Revenues	**3,150**	**4,350**	**2,556**	**3,830**	**1,274**	**50%**

ii. Late Payment Surcharge

7.3.2. The petitioner has claimed LPS (Rs. 1,537 million) as non-operating income in the instant petition; however, the same was claimed at Rs. 1,501 million as operating income at the time of DERR for the said year.

7.3.3. The petitioner has reiterated its stance that LPS is a non-regulated income as it is an interest income being financial compensation for delayed payment of gas dues by defaulting consumers. It was highlighted that delayed / non payment by the consumers results in financing activities requiring the company to borrow additional funds to offset shortfall in cash flow. LPS, therefore, is not an operating activity but in fact a financing activity and thus cannot form part of operating income.

7.3.4. The petitioner has further elaborated that under the stay order of the Honorable LHC, it has been clearly directed that the treatment of late payment surcharge will continue as non-operating, as allowed by the Authority in FRR FY 2009-10, till final decision is announced by the Court.

7.3.5. *The Authority in view of the discussion at para 5.4 above has been following the existing basis of 17.5% return on the average net operating fixed assets while treating various income and expenditure heads per the exiting regime, in accordance with the License Condition No. 5.2.*

7.3.6. *The Authority, however, notes that the revenue requirement for the said year is subjudice and interim stay in the matter is in field. Therefore the Authority, in*

accordance with the interim relief granted by the Honorable LHC, decides to treat LPS as non-operating for the said year on provisional basis, subject to final decision of the LHC.

iii. Other Operating Income:

7.3.7. The petitioner has claimed Rs. 190 million on account of other operating income as against Rs. 258 million per FRR FY 2009-10, detailed as under;

Table 12: Comparison of Other Operating Income per the petition with RERR & Previous Year

Rs. in million

Description	FRR FY 2009-10			FY 2010-11 (The petition)		
	Operating	Non-Operating	Total	Operating	Non-Operating	Total
Net gain on sale of fixed assets	21	-	21	9		9
Insurance claim	2	-	2	2		2
Sale of tender documents	2	-	2	2		2
Sale of Scrap	29		29	60		60
Liquidated damages recovered	36	36	72	100	100	200
Bad debts recoveries	31	-	31	14	-	14
Take or pay Income from industrial consume	-	633	633	-	630	630
Gain on construction contracts	115	115	230	-	258	258
Gain on coating of pipeline for SSGC	-	-	-	-	517	517
Miscellaneous	22		22	3	8	11
Net Operating Revenues	**258**	**784**	**1,042**	**190**	**1,513**	**1,703**

7.3.8. The petitioner has pleaded that the Authority, under the law, has the jurisdiction to determine Revenue Requirement of a licensee only with reference to "regulated activities". In case of a licensee engaged in the business of transmission and distribution of natural gas, the position is even clearer. Sections 8 (1) and 8 (2) specifically relate to Revenue Requirement of a licensee of natural gas "engaged in transmission, distribution and the sale of natural gas to a retail customer of natural gas". This makes it clear that the Authority has no jurisdiction to even consider matters which do not fall within the "regulated activity" which, in the instant case, arise from distribution and transmission of natural gas. Since the gain on construction contracts, do not arise from "regulated activity", therefore, the Authority has no jurisdiction to deal with the same or include them as part of Revenue Requirement of the petitioner.

7.3.9. The petitioner has submitted that the Authority, per FRR FY 2004-05 dated October 26, 2005, had decided that 50% of gain on construction contracts be treated as operating income. The petitioner has argued that License issued by the Authority does not impose any restriction on the petitioner to explore new business opportunities and undertake activities which are outside the scope of regulated activities. License condition 5.1 and the Ordinance, limits the scope and power of OGRA to the extent of

regulated activities only. Therefore, gain on construction contracts, being non-regulated income, should not be made part of tariff computation.

7.3.10. The Authority observes that the petitioner has treated the entire income on account of gain on construction contracts, gain on the coating of pipeline for SSGCL and some portion of "miscellaneous" as non-operating and excluded the same from the revenue requirement for the said year.

7.3.11. The Authority notes that the claimed treatment by the petitioner for above said incomes is unjustified, illogical and without rationale. Income on account of construction contract and coating of pipeline could only be earned by utilizing the petitioner's construction equipment, human resource, management time and above all goodwill cost, which is perpetually financed by gas consumers. Had the petitioner intended to treat the above as independent non-regulated activity, it should have incorporated a separate entity as a special purpose vehicle. In the present arrangement, if the entire income on this account is treated non-operating, it will tantamount to dual earning of regulated fixed assets beyond the guaranteed return, and that too at the cost of consumers.

7.3.12. *The Authority, in view of that above decides to maintain its earlier decision to treat 50% of the said incomes as operating. This treatment appreciates the petitioner to undertake such projects and safeguard the public interest in terms of return on assets built through public finance. Resultantly, income under the head "other operating income" works out to Rs. 586 million for the said year.*

8. Operating Expenses

8.1. Cost of Gas

8.1.1. The cost of gas per petition is Rs. 170,500 million(net of GIC), compared with Rs. 183,974 million determined in RERR, lower by Rs. 13,474 million (7%).

8.1.2. The Authority had determined input cost of gas on the basis of combined weighted average cost of gas purchased by the petitioner and SSGCL at Rs. 270.68 per MMBTU in RERR in accordance with the agreement for equalization of cost of gas dated 22nd September, 2003, between these two companies. On the basis of their actual audited results, weighted average of input cost of gas for the said year works out at Rs. 271.51 per MMBTU as under:

Table 13: Weighted Average Cost of Input Gas

Company	MMCF	BBTU	Rs in million	Rs./ MMBTU
SSGCL	397,739	381,039	127,755	335.28
SNGPL	672,460	634,404	147,947	233.21
Total	**1,070,199**	**1,015,443**	**275,702**	**271.51**

8.1.3. The WACOG has now been computed based on payments actually made by the petitioner and SSGCL for purchase of gas in accordance with wellhead gas prices as notified by the Authority.

8.1.4. *In view of the above, the Authority determines cost of gas sold for the said year at Rs. 170,500 million.*

8.2. Unaccounted for Gas

8.2.1. The petitioner has reported UFG at 10.10% (67,144 MMSCF) for the said year, as follows:

Table 14: Comparison of UFG per the petition with RERR & Previous Year

		Volumes in MMCF
Particulars	**FY 2010-11 RERR**	**FY 2010-11 (The Petition)**
Total Gas Purchases	738,072	673,037
Gas Internally Consumed	10,333	8,366
Gas Available for Sales	727,739	664,671
Gas Sales	675,336	597,528
UFG (MMCF)	62,736	67,143
UFG %	**8.62%**	**10.10%**

8.2.2. The petitioner has requested to fix UFG target at 7% in line with the decision of the Authority in FRR FY 2009-10 and honorable LHC stay order on the petitioner's RERR for the said year.

8.2.3. The petitioner has also included unmeasured gas (6,883 MMCF) on account of minimum billing and pilferage by non- consumers (6,607 MMCF), as part of UFG for the said year. The petitioner has elaborated that it has no control over these two issues which are continuously contributing towards high UFG. Unmeasured gas evolves due to inherent limitation in measurement and minimum billing formula while gas pilfered by non- consumers is unavoidable since no legislation is in place to initiate legal proceeding against the persons involved.

8.2.4. The petitioner, during the hearing, submitted that UFG target should be reviewed keeping in view the ground realities including size and age of network, rise in gas sale prices, change in sale mix, high UFG in certain areas e.g. Khyber Pakhtunkhwa (KPK) and South Punjab, uneconomic expansion, etc, since these will adversely impact the petitioner's profitability and will jeopardizing its viability as a going concern.

8.2.5. The petitioner asserted that over the last decade there has been a constant shift from bulk sales toward retail. Since the petitioner has little control over the choice of consumer category and has to comply with the directives of the Federal Government for supply of gas to the domestic sector, especially in remote areas, the increase in UFG is inevitable and cannot be attributed to any inefficiency, imprudence or even willfulness on the petitioner's part. Therefore, penalizing the petitioner on this account would be against law and equity.

8.2.6. The petitioner stated that high 'UFG' in remote areas like KPK and Interior Punjab was not given due weightage by the Authority. It is almost impossible to control the UFG in these areas with the prevailing law and order situation and no improvement seems likely in the near future. Provision of Gas to these areas is financially unviable for the Company, although the same would and should be a requirement of the State's social responsibility. During the past few years KPK has not only been politically volatile but is also facing a serious law and order situation which has made it impossible for the Company to control UFG in that province. Officers of the Company have been continuously facing death threats creating a feeling of deep insecurity amongst Company personnel which has resulted in requests for transfers in many cases.

8.2.7. The petitioner also highlighted that clause 13.1.2 of the License infact directs it to provide gas to customers only if the same is technically and economically viable. The fact that the GoP in pursuance of its socio economic objectives requires the petitioner to continue to provide gas to economically unviable areas, which by no stretch of imagination can be a ground for burdening the petitioner with the consequences of the same. The extension in distribution development is also responsible for the shift of gas to bulk sector, where UFG is low or zero, to the highly UFG prone retail sector. It is evident from the record that till 2006 there were only 1,013 towns and villages connected to the Company's network, which has now increased beyond 2,000.

8.2.8. The petitioner stressed on theft by non consumers, which is a major area of concern, contributing substantially towards UFG. In the past, efforts were made to control this menace. However, since OGRA was not inclined to consider these cases as ground for

reduction in disallowance for UFG, the efforts could not continue on a consistent basis. In FY 2009-10 it was decided by the petitioner that once again renewed efforts, with full force, should be undertaken to detect theft by non consumers and for this purpose special task forces were made. As a result of these efforts a record number of cases were detected and proceedings in accordance with the law and procedure, prescribed and advised by OGRA, were undertaken.

8.2.9. The petitioner demanded that since it has complied with all the relevant law and procedures, benefit of the volume detected should be given to it. The said volume should be deducted from the total UFG and no penalty in the form of disallowance should be imposed on it. It is of utmost importance to appreciate that these non consumers have been detected and disconnected inspite of violence against staff of the petitioner who continued to perform their duties regardless of peril to their lives.

8.2.10. The petitioner further stated that from the above discussion of facts and the applicable law, it is evident that on its part the Company has made all possible efforts to keep the UFG within acceptable limits and the reasons for which the UFG benchmarks have not been met have always been beyond the control of the Company. Moreover, the disallowances have actually eroded the company's financial position thereby limiting its ability to raise funds at reasonable rates from the market and to take effective measure to control UFG.

8.2.11. The Authority, in accordance with the Ministry of Petroleum & Natural Resource's, directives decides to allow gas sale volume in respect of non consumers as part of UFG. The Authority, however, disallows the petitioner's claim on account of unmeasured gas as part of minimum billing on the rationale that the same is not metered and hence does not qualify for inclusion in the UFG computations, in view of the UFG definition provided in the NGTR as well as the petitioner's historical practice in the instant matter.

8.2.12. The Authority further observes that the petitioner has wrongly calculated the UFG at 10.10% (67,144 MMCF) for the said year. The petitioner has included the gas sale volume in respect of purging and ruptures on account of third party damages, which is not admissible as decided in earlier determinations. The actual UFG in fact reaches to 11.21% (74,592 MMCF). Accordingly, UFG disallowance over and above 7% level, per the interim decision of the honorable LHC, comes to Rs. 7,178 million as below:

Table 15: Calculation of UFG Disallowance

		Volume in MMCF	MMCF AS PER OGRA PARAMETERS -
1	**Gas Purchases**		
	Metered Gas Purchased As Per Books	672,985	672,985
	Gas taken out / put into	688	688
	Gas carried for PPL and POL	(636)	(636)
A	**Gas Available for Sale**	673,037	673,037
	Gas sold and internally consumed		
	(i) Compression	6,667	6,667
	(ii) Residential Colonies	101	101
	(iii) Coating Plant	169	169
	(iv) Rupturs (Sabotage)	242	242
	(v) Other usage - De- pressurization purging etc	8	-
	Gas Used in the Transmission System	*7,188*	*7,179*
	(i) Free Gas Facility	397	397
	(ii) Co-Generation	70	70
	(iii) Rupturs (Sabotage)	155	155
	(iv) Rupturs (Third party damages)	80	-
	(v) Purging	476	-
	Gas Used in the Distribution System	*1,178*	*622*
B	Total GIC	**8,366**	**7,801**
C	**Gas Available for Sale**	**664,671**	**665,236**
	Gas Sold (Billed)	581,901	581,901
	Unbilled volume in law & order affected and flood hit areas	2,136	2,136
	under measured volume in respect of minimum cases - Domestic	6,883	-
	Pilfered volume detected against non-consumers	6,607	6,607
D	**TOTAL**	**597,527**	**590,644**
	UFG Volume (C-D)	**67,144**	**74,592**
	UFG %age (E/A)*100	10.10%	11.21%

Calculation of UFG		**Per Petitioner at 7%**	**Per OGRA at 7%**
Working Of Penalty		7.0%	7.0%
Gas Purchases / Available for Sales (MMCF)		664,671	665,236
UFG Above the target of 7%	7%	46,527	46,567
UFG Diallowance above the target		**20,617**	**28,025**
Total UFG Disallowance		20,617	28,025
Avg. Cost Of Purchases Rs. Per MCF		256.14	256.14
Disallowance in Million Rs.		**5,281**	**7,178**

8.3. Transmission and Distribution Cost

i. Summary

8.3.1. The transmission and distribution cost is higher by 20% i.e. from Rs. 11,759 million per RERR to Rs. 14,099 million per the petition, as compared below:

Table 16: Comparison of T & D Cost with RERR and Previous Year

Rs. in million

Particulars	FY 2009-10	FY 2010-11		Increase / (Decrease) Over RERR after Disallowance	
	FRR	RERR	The Petition	Rs.	%
Human Resource Cost	5,218	6,049	8,002	1,953	32 %
Cost of Reinstated Employees	100	553	579	26	5 %
Gas Internally Consumed	2,287	2,555	1,878	(676)	(26) %
Stores and Spares Consumed	494	511	404	(107)	(21) %
Repair and Maintenance	791	813	638	(175)	(22) %
Fuel and Power	165	197	178	(19)	(9) %
Stationery, Telegram and Postage	101	117	103	(14)	(12) %
Dispatch of gas bills	64	68	67	(1)	(1) %
Rent, Rate, Electricity and Telephone	200	224	226	2	1 %
Traveling	125	159	139	(21)	(13) %
Transport expenses	503	444	482	38	9 %
Insurance	146	166	175	9	6 %
Legal and Professional Services	44	39	55	16	41 %
Consultation for ISO 14001 & OHSAS 18000	3	3	2	(1)	(21) %
Gas bills collection charges	252	287	283	(4)	(1) %
Gathering charges of gas bills collection data	21	34	21	(13)	(37) %
OGRA fee	109	174	168	(5)	(3) %
Advertisement	67	74	61	(13)	(17) %
Bank Charges	21	23	21	(2)	(8) %
Uniforms & protective clothing's	11	10	13	3	28 %
Staff training and recruiting	12	6	3	(3)	(48) %
Security expenses	182	232	190	(42)	(18) %
SNG training insititute	5	9	8	(1)	(12) %
Provision for doubtful debts	180	180	1,639	1,459	811 %
Sponsorship of chairs at University	3	5	3	(2)	(33) %
5 Year special training programme	5	-	15	15	
Budget for UFG control related activities	6	-	2	2	
Out Sourcing of call centre complaints management	9	15	13	(3)	(17) %
Stores spares written off	9	-	2	2	
Cost of Gas Blown off	71	-	123	123	
Contribution to Inter State Gas System Limited	49	145	59	(86)	(59) %
Other expenses	55	73	65	(8)	(11) %
Subtotal Expenses	**11,307**	**13,162**	**15,616**	**2,453**	**19%**
Allocated to fixed capital expenditures	(1,528)	(1,403)	(1,517)	(114)	8 %
Toal	**9,779**	**11,759**	**14,099**	**2,340**	**20%**

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 an increase of 32% on account of HR cost for the said year, from Rs. 6,049 million provided in RERR to Rs. 8,002 million (including impact of IAS-19) per the petition.

8.3.4. The petitioner has submitted that existing HR cost benchmark was revised for the period of three years starting from FY 2008-09 without any consultation with the utility companies. Resultantly it has put the petitioner at complete disadvantage creating a sense of frustration among its employees. The Authority now in its determination of ERR FY 2011-12 has accepted the fact that current HR benchmark has outlived its useful life and become redundant. The Authority further acceded that there is now a complete shift in the tendency of the parameters earlier adopted to compute the existing HR cost benchmark. Gas sale volumes, number of consumers and extension in T&D network have now become irrelevant and inappropriate factors owing to depleting gas supply reserves.

8.3.5. The petitioner elaborated that the Authority has now invited the two Utility Companies to submit proposals for revision of the existing benchmark. SNGPL has already submitted its proposal vide its letter dated August 04, 2011 and has also claimed the benchmark for the said year on the proposed revised basis.

8.3.6. The petitioner, during the public hearing on 14th September, 2011 had also pleaded that CBA with the employees union is pending since July 01, 2009. In FY 2009-10, due to non-availability of funds in HR benchmark allowed by OGRA, the petitioner was constrained to provide a petty amount of Rs. 36 million. During the said year, a provision of Rs. 1,247 million for CBA, covering the period FY 2009-2011, has been included. Total demand of the CBA union however comes to Rs. 1,974 million. Accordingly, the petitioner has requested to enhance the HR benchmark for the current year to the extent of Rs. 1,974 million enabling the petitioner to meet the above said requirement. CBA union representative also emphasized this issue and requested to relax the HR benchmark in order to compensate the genuine demands of the hardworking and industrious manpower, pending since last year.

8.3.7. The Authority observes that the HR benchmark was implemented after carrying out detailed analysis and exhaustive discussions with the utilities and has, therefore, proved to be reasonably fit. The HR benchmark has been tested in terms of effectiveness and efficiency since its introduction, which reveals that the composition of HR benchmark cost remained quite successful, tight enough to control this cost

and relaxed enough to provide a cushion for extra funding and the incentive for cost optimization. The Authority is also vigilant to the change in business dynamics and contributive factors forming the HR benchmark cost. Accordingly, it has decided to review the existing HR benchmark effective FY 2011-12 and has sought fresh proposals from the gas utilities to review the same. For the said year, the existing basis for HR benchmark will, however, remain intact.

8.3.8. The Authority observes that the HR benchmark cost has not been optimized in true sense and benefits have not been shared reasonably, which resultantly has created an impression of disparity and anomalies among the employees in different cadres. Had the petitioner strived for cost optimization by shedding the extra fat and deadwood available in the system, it should have sufficient provision to meet the demand of its CBA and executives in total.

8.3.9. The Authority also notes with grave concern that the petitioner has put the subordinate staff at complete disadvantage since the CBA demand has not been negotiated since last two years. This has not only impaired the financial capacity of the field workers but has also unmotivated them for efficient working. If this situation is maintained, it will further aggravate the bleak financial position of the company, which is already at the brink of loss in view of over 12% UFG and excessive financial cost for the said year. The Authority in this uncertain and dismal situation of the company decides to provide a financial relief as a short term measure on this score by excluding the CBA demand and 10-C and agreement bonus from HR benchmark cost for FY 2009-11. This treatment provides sufficient funding to meet the demand of CBA amounting to Rs. 1.7 billion. *The Authority further elucidates that this treatment does not change the existing composition of HR benchmark and also has no bearing/consideration for the future benchmark effective FY 2011-12.*

8.3.10. *The Authority further directs the petitioner to ensure that the said amount of Rs. 1.7 billion is only spent on account of CBA, for which documentary evidence must be provided to OGRA, within sixty days of issuance of this Order.*

8.3.11. *The Authority, in view of above, re-computes the HR cost benchmark for the said year at Annexure-B and allows Rs. 6,478 million (including IAS-19 and differential of FY 2009-10) on account of HR cost for the said year.*

iii. Cost of Reinstated Employees

8.3.12. The petitioner has requested to allow expenditure amounting to Rs. 579 million on account of salaries and wages of reinstated employees, over and above the HR cost benchmark for the said year, as against Rs. 553 million provided in RERR.

8.3.13. The petitioner has submitted that the cost under this head pertains to sacked employees reinstated on the GoP directives. The services of these employees are being optimally utilized as per the utilization plan and have been found satisfactory. The petitioner has also explained that quarterly progress reports pertaining to the third quarter of the said year has been submitted.

8.3.14. The Authority observes that in DERR for the said year, it had allowed the projected expenditure under this head, over and above the HR cost benchmark, subject to submission of quarterly progress report on the effective utilization of additional manpower. The petitioner has recently submitted progress report for the quarter ending March 31, 2011, which however is far from adequate.

8.3.15. *The Authority in view of the Sacked Employees (Re-instated) Ordinance, 2009 and Federal Government directives thereof decides to provisionally allow Rs. 579 million on account of reinstated employees for the said year, subject to submission of satisfactory quarterly reports to assess judicious and effective utilization of additional workforce, in accordance with the Authority's directives at para 8.5.3 & 8.5.4 of the determination of ERR for the said year.*

iv. Legal and Professional Charges

8.3.16. The petitioner has projected expenditure of Rs. 55 million on account of legal and professional charges for the said year as against Rs. 39 million provided in RERR, showing an increase of 41%. Historical comparison is given below:

Table 17: Detailed Comparison of Projected Legal & Professional Charges with Previous Years

Rs. in million

Particulars	FY 2009-10	FY 2010-11	FY 2011-12	Inc/(dec) Over RERR FY 2010-11	
	FRR	RERR	The Petition	Rs.	%
Legal	18	18	37	18	101%
Professional	12	11	5	(6)	-52%
Tax	5	4	3	(0)	-1%
Audit	3	2	4	2	80%
Software development charges	-	-	-	-	0%
Apprenticeship / Scholarship / Traini	5	1	3	2	136%
Others	1	3	2	(1)	-22%
	44	**39**	**55**	**16**	**41%**

8.3.17. The petitioner has explained that 101% increase under the sub-head "legal" is mainly due to payment of Rs. 13.5 million made to law firm to plead the case of revenue requirement against OGRA in the High court. Increase in litigation cases is owing to increase in number of consumers, deteriorating law & order situation, rapid growth in demand of gas and rise in tariff. Fee of advocates and ancillary expenses have also contributed towards increased expenditure during the said year.

8.3.18. The Authority observes that the petitioner was already allowed exorbitant increase under this sub-head last year on the same grounds particularly for legal suits against the permanent defaulters to recover bad debts. The recoveries from the defaulters however have not exhibited the satisfactory results. The Authority further notes that the petitioner should endeavor to settle the outstanding issues with OGRA instead of spending exorbitant amount of public money in excessive litigation and that too against the public interest.

8.3.19. *The Authority, in view of above, allows Rs. 37 under the sub-head "Legal" and determines the total expenditure under this head at Rs. 55 million for the said year subject to comprehensive review of each component of head "legal & professional charges". The petitioner is further directed to furnish comprehensive progress report on substantive gains made in recovery of bad debts and its overall impact on run away provision for doubtful debts.*

v. Provision for Doubtful Debts.

8.3.20. The petitioner has claimed the provision for doubtful debts for the said year at Rs. 1,639 million as against Rs. 180 million provided in RERR, showing an increase of 811%. Historical comparison of provision for doubtful debt is as under:

Table 18: Comparison of Provision for Doubtful Debts with RERR & Previous Year

Rs. in million

Particulars	FY 2009-10	FY 2010-11	FY 2011-12	Inc/(dec) Over RERR FY 2010-11	
	FRR	RERR	The Petition	Rs.	%
Provision for doubtful debts	180	180	1,639	1,459	811%

8.3.21. The Authority notes that the sale revenue & sale volume for the said year has decreased compared with RERR for the said year.

8.3.22. The Authority observes that the petitioner had been repeatedly directed through its various earlier determinations to make concerted efforts to curtail this ever increasing

expenditure in order not to pass this avoidable cost to consumers. However, this phenomenal increase in provision points to continued lack of action to evolve effective mechanism to ensure timely recovery of bills. This cannot be allowed to continue.

8.3.23. The Authority also observes that the petitioner has spent a significant amount on outsourcing of bill recovery mechanism as well as litigation proceedings on account of recovery of dues from the defaulters. Commensurate impact in terms of decrease in provisioning has, however, never been observed. This status quo strengthens the Authority findings that the fundamental flaws exist in petitioner's own management policies resulting to inefficiencies in various areas and particularly on this account.

8.3.24. *In view of above, the Authority restricts the provision for doubtful debts at the level of FRR FY 2009-10 and allows Rs. 180 million for the said year.*

vi. Cost of Gas blown off

8.3.25. The petitioner has claimed Rs. 123 million on account of cost of gas blown off due to third party damages and terrorist activities during the said year.

8.3.26. The Authority observes that 477 MMCF gas has been lost during the said year due to ruptures, out of which 397 MMCF has been reckoned towards terrorist activities and remaining 80 MMCF gas losses has occurred due to third party damages. The sabotage due to terrorist activities is uncontrollable factor; however, the third party damages could have been avoided if the petitioner had undertaken concerted efforts and put in place an effective system.

8.3.27. *The Authority therefore allows Rs. 102 million on this account and disallows 80 MMCF gas lost due to third party damages for the said year.*

vii. Remaining Items of Transmission & Distribution Cost

8.3.28. The items of transmission and distribution cost, except those dealt with in para's 8.3.3 to 8.3.27 above, are claimed by the petitioner at Rs. 3,701 million as against Rs. 4,938 million provided in RERR, showing decrease of 25%. The comparative analysis is given below:

Table 19: Remaining Items of Transmission & Distribution Cost

Rs. in million

Particulars	FY 2009-10	FY 2010-11		Increase / (Decrease) Over	
	FRR	RERR	The Petition	Rs.	%
Gas Internally Consumed	2,287	2,555	1,878	(676)	(26) %
Stores and Spares Consumed	494	511	404	(107)	(21) %
Repair and Maintenance	791	813	638	(175)	(22) %
Fuel and Power	165	197	178	(19)	(9) %
Stationery, Telegram and Postage	101	117	103	(14)	(12) %
Dispatch of gas bills	64	68	67	(1)	(1) %
Rent, Rate, Electricity and Telephone	200	224	226	2	1 %
Traveling	125	159	139	(21)	(13) %
Transport expenses	503	444	482	38	9 %
Insurance	146	166	175	9	6 %
Consultation for ISO 14001 & OHSAS 18000	3	3	2	(1)	(21) %
Gas bills collection charges	252	287	283	(4)	(1) %
Gathering charges of gas bills collection data	21	34	21	(13)	(37) %
OGRA fee	109	174	168	(5)	(3) %
Advertisement	67	74	61	(13)	(17) %
Bank Charges	21	23	21	(2)	(8) %
Uniforms & protective clothing's	11	10	13	3	28 %
Staff training and recruiting	12	6	3	(3)	(48) %
Security expenses	182	232	190	(42)	(18) %
SNG training insititute	5	9	8	(5)	(60) %
Sponsorship of chairs at University	3	5	3	10	192 %
5 Year special training programme	5	-	15	15	
Budget for UFG control related activities	6	-	2	2	
Out Sourcing of call centre complaints management	9	15	13	(3)	(17) %
Stores spares written off	9	-	2	2	
Contribution to Inter State Gas System Limited	49	145	59	(86)	(59) %
Other expenses	55	73	65	(8)	(11) %
Subtotal Expenses	**5,695**	**6,341**	**5,218**	**(1,116)**	**-18%**
Allocated to fixed capital expenditures	(1,528)	(1,403)	(1,517)	(114)	8 %
Toal	**4,168**	**4,938**	**3,701**	**(1,237)**	**-25%**

8.3.29. The petitioner has reported the saving in almost all the expenditure heads cited above, except a few expense heads where nominal increase has been observed.

8.3.30. Saving in GIC is due to lesser consumption of gas in compressors during the said year.

8.3.31. 21% saving in "Stores, Spares & Supplies consumed" is due to decrease in compression activities owing to diversion of gas from northern part thereby decreasing the compression from south. Further, various metering equipments have not been consumed during the said year due to their unavailability. This has resulted in decrease in stores consumed for the said year.

8.3.32. Saving in "Repair & Maintenance" activities is due to non availability of recoating material, which was to be imported from abroad during the said year.

8.3.33. The Authority observes with grave concerns that decrease in "Stores, Spares and supplies" and "Repair & Maintenance" at the cost of performance and sharp increase

in UFG is not acceptable at all. The resources could not be mobilized due to delay in procurement of main material and resultantly it has made the system inoperative during the whole financial year. Accordingly, the Authority notes that upward rise in UFG in the instant petition is correlated to reduction in rectification of leakages and failure to undertake the UFG related activities during the said year.

8.3.34. The Authority expresses deep apprehension on the state of affairs of the petitioner and feels that not only financial indicators are debilitating, but all the priorities and entire paradigm is shifting identical to state owned sick units. This phenomena points to lack of unity of command, proper controls and non professional attitude, outcome of which is not different to financial impairment which may lead the petitioner as defunct organization.

8.3.35. The Authority critically evaluates that it has emphasized the petitioner on all the matters leading to collapse, however no positive reaction to overcome the aggravated situation, shows that the petitioner is gradually loosing its capability. The Authority therefore draws the attention of higher management to be resilient to the present state, streamline the issues and remove the bottlenecks in the systems which are not only eroding the profitability of the petitioner but also loss to national exchequer.

8.3.36. *Expenditure under the remaining items of T&D cost seems to be reasonable, the Authority, therefore, allows the same and determines it at Rs. 3,701 million.*

8.3.37. *Based on the above, the Authority determines total transmission and distribution cost for the said year at Rs. 11,095 million, as against Rs. 14,099 million claimed by the petitioner.*

8.4. Foreign Currency Exchange Loss

8.4.1. The petitioner has claimed Rs. 358 million on account of exchange loss occurred due to payment to the producers on account of cost of gas, during the said year. The petitioner has explained that only Rs. 56 million pertains to the said year while Rs. 302 million pertains to FY 2009-10, which was erroneously omitted at that time and hence not claimed.

8.4.2. The Authority observes that the exchange loss has primarily occurred due to payment to foreign gas producers and is an unavoidable expenditure, duly vetted from initialed accounts.

8.4.3. The Authority observes that the petitioner's claim pertaining to previous years unnecessarily swells the costs to be paid by the consumers of this year. The Authority will discourage the practice of cumulative claims in future.

8.4.4. *In view of above, the Authority allows the exchange loss claimed by the petitioner amounting to Rs. 358 million under this head for the said year.*

8.5. Workers Profit Participation Fund (WPPF)

8.5.1. The petitioner has claimed WPPF at Rs. 282 million for the said year. However, due to adjustments in the components of revenue requirement as discussed above, WPPF is recalculated and allowed at Rs. 90 million.

9. Decision

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

(i) determines the other operating income at Rs. 586 million;
(ii) addition in fixed assets at Rs. 4,428 million;
(iii) allow closing balance of fixed assets at Rs. 76,469 million;
(iv) accept the cost of gas at Rs. 170,500 million;
(v) allow the UFG at 7% based on which disallowance on this account comes to Rs. 7,178 million;
(vi) allows T&D cost at Rs. 9,217 million as against Rs. 12,221 million claimed by the petitioner;
(vii) accept the GIC at Rs.1,878 million;
(viii) determines the WPPF at Rs. 105 million as against Rs. 382 million claimed by the petitioner;

9.2. In exercise of its powers under Section 8(2) of the Ordinance, the Authority determines the FRR for the said year at Rs. 192,365 million as against petitioner's claim of Rs. 197,444 million, as tabulated below:

Table 20: Components of FRR for FY 2010-11 as Determined by the Authority

Rs. in Million

Description	Demanded by the Petitioner	Determined by the Authority
Cost of Gas	170,500	170,500
Transmission & Distribution Cost	12,221	9,217
GIC	1,878	1,878
UFG Disallowance	(5,281)	(7,178)
Depreciation	7,654	7,654
Return on Assets	9,832	9,832
Foreign Currency Exchange loss on gas purchase	358	358
Other Charges Including WPPF	282	105
Total	**197,444**	**192,365**

9.3. The petitioner's actual net operating income is Rs. 189,374 million, which is short of revenue requirement of Rs 192,365 million for the said year by Rs. 2,991 million. Since no GDS is available to adjust this shortfall, the Authority therefore decides to adjust this amount in RERR FY 2011-12.

Mansoor Muzaffar Ali
(Member Gas)

Mir Kamal Marri
(Member Finance)

Sabar Hussain
Acting Chairman / (Member Oil)

Islamabad, September 21, 2011

A. Final Revenue Requirement for FY 2010- 11

Million Rs.

	Particulars	FRR FY 2010-11 (The Petition)	Adjustments	Determined by the Authority
	Gas sales volume -MMCF	581,935	-	581,935
	BBTU	547,502	-	547,502
	Calorific Value	941	-	941
"A"	**Net Operating revenues**			
	Net sales at current prescribed price	185,148	-	185,148
	Rental & service charges	1,126	-	1,126
	Surcharge and interest on arrears	-	-	-
	Amortization of deferred credit	2,514	-	2,514
	Other operating income	190	396	586
	Total income "A"	**188,978**	**396**	**189,374**
"B"	**Less Expenses**			
	Cost of gas sold	170,500	-	170,500
	UFG (disallowance) / allowance	(5,281)	(1,897)	(7,178)
	Transmission and distribution cost	12,221	(3,005)	9,217
	Gas Internally Consumed	1,878	-	1,878
	Depreciation	7,654	-	7,654
	Workers Profit Participation Fund	282	(177)	105
	Foreign Currency Exchange loss on gas purchase	358	-	358
	Total expenses "B"	**187,612**	**(5,079)**	**182,533**
"C"	**Operating profit / (loss)(A - B)**	**1,366**	**5,475**	**6,841**
	Return required on net assets:			
	Net assets at begining	72,028	-	72,028
	Net assets at ending	76,469	-	76,469
		148,497	-	148,497
	Average fixed net assets (I)	**74,249**		**74,249**
	Deferred credit at begining	17,842	-	17,842
	Deferred credit at ending	18,288	-	18,288
		36,130		36,130
	Average net deferred credit (II)	**18,065**	**-**	**18,065**
"D"	**Average operating assets (I-II)**	**56,184**	**-**	**56,184**
	Return required on net assets	17.5%		17.5%
"E"	Amount of return required	9,832	-	9,832
"F"	**Excess /(shortfall) over return required**	**(8,466)**	**5,475**	**(2,991)**
"G"	**Average Increase/(Decrease) in Prescribed Price (Rs/MMBTU)**	**15.46**	**-**	**5.46**
"H"	**Revenue requirement**	**197,444**	**(5,079)**	**192,365**
"I"	**Average Prescribed Price (Rs/MMBTU)**	**353.63**	**-**	**343.63**

B. Computation of H.R Benchmark Cost for FY 2010-11

Million Rs

Description	FY 2009-10 Revised	FY 2010-11 Per Petitioner	FY 2010-11 Per OGRA
Total HR cost Actual (Excluding CBA demand & bonuses, IAS-19)	4,665	6,786	6,172
BASIS OF BENCHMARK			
T & D Network (km)	83,182	89,441	89,441
Total No. of consumers	3,712,601	3,964,350	3,964,530
Sale Volume (MMCF)	586,741	581,935	581,935
CPI	11.73%	13.92%	13.92%
Per unit cost factor (T & D Network) (Rs.) (Base Year) - Rs/km	61,478	133,352	61,478
Per unit cost factor (consumer base) (Rs.) (Base Year) -Rs/Consumer	1,305	2,264	1,305
Per unit cost factor (Sale volume base) (Rs.) (Base Year) -Rs/MMCF	6,886	1,244	6,886
Indexation Factors			
Increase based on CPI	50%	50%	50%
Increase on account of increase in T & D Network	20%	20%	20%
Increase on account of increase in consumers	60%	60%	60%
Increase on account of sale volume	20%	20%	20%
Increase based on 50% CPI	285	-	386
Increase on account of increase in T & D Network (20% weightage) (Rs. mil)	1,023	2,385	1,100
Increase on account of increase in consumers (60% weightage) (Rs. mil)	2,906	5,385	3,103
Increase on account of sale volume (20% weightage) (Rs. mil)	808	1,448	801
Benchmark HR Cost	**5,022**	**9,218**	**5,390**
Excess/(saving) to the Licensee (50%) (Rs. in mil)	(178)	(1,216)	391
Total benchmark H.R. Cost allowed (After Adjustment of 50% Excess/(saving) + CBA demand and bonuses)	**5,201**	**8,002**	**6,220**
Add: IAS -19 Provision			175
Differential FY 2009-10			**178**
Less: CBA in excess of Rs. 1.7 Billion			(95)
Total Allowed for FY 2010-11			**6,478**