

IN THE MATTER OF

**SUI SOUTHERN GAS COMPANY LIMITED
FINAL REVENUE REQUIREMENT, FY 2008-09**

UNDER

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

DECISION

September 15, 2009

Before:

**Tauqir Sadiq, Chairman
Mir Kamal Marri, Member (Finance)**

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1. Background

- 1.1 Sui Southern Gas Company 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, Air-mix LPG, sale of gas condensate (as a by-product), and manufacture and sale of gas meters.
- 1.2 The petitioner filed a petition (the petition) on August 19, 2009 under Section 8(2) of the Oil and 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 2008-09 (the said year) on the basis of the accounts as initialed by its statutory auditors. The Authority admitted the petition on August 31, 2009.
- 1.3 The Authority, vide its Order dated November 20, 2008, had determined the petitioner's Revised Estimated Revenue Requirement for the said year (RERR) under Section 8(2) of the Ordinance at Rs. 117,872 million (the amounts have been rounded off to the nearest million here and elsewhere in this document) for estimated sale volume of 381,207 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 petition for determination of its FRR for the said year after incorporating the effect of actual changes in the wellhead gas prices, change in sales mix, other relevant factors in terms of Section 8(2) of the Ordinance and also has made some other claims. The petitioner has worked out its FRR for the said year at Rs. 118,282 million for actual sale volume of 356,442 BBTU. Based on the provisional prescribed prices and actual sale mix, the petitioner has computed a shortfall in its revenue requirement of Rs. 11,054 million for the said year, thereby seeking increase in the prescribed prices by Rs. 31.01 per MMBTU. The petitioner has also requested for an additional amount of Rs. 35 million on account of its Air-mix LPG Project, increasing the shortfall to Rs. 11,088 million and has requested average increase in prescribed price to Rs. 31.11 per MMBTU.
- 1.5 The Authority issued notice of hearing on September 03, 2009 to the petitioner and following interveners and related parties:



- (i) Federal Government (GoP),
- (ii) All Pakistan Textile Mills Association through Mian Mahmood Rashid, Advocate, Rashid Law Associates, Lahore,
- (iii) Mr. Ghulam Ali Shah Pasha, Additional Chief Secretary Finance, Government of Sindh, Karachi,
- (iv) Brig. (R) Iftikhar Ahmad, Acting Chairman, All Pakistan CNG Association (Regd.), Rawalpindi,
- (v) Mr. Muhammad Zubair Motiwala, Former President, Karachi Chamber of Commerce & Industry, Karachi,
- (vi) Mr. Sahibzada Muhammad Khan, Senior Member, Chamber of Commerce & Industry, Quetta,
- (vii) Mr. Muhammad Nisar Sheikhani, Chairman, SITE Association of Industry, Karachi,
- (viii) Mr. Imtiaz Haider, Group Head, Aqeel Karim Dhedi Securities (Pvt.) Limited, Karachi,
- (ix) Mr. Muhammad Arif Bilwani, Karachi.

1.6 The hearing was held on September 14, 2009, at Islamabad.

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 per the Petition with RERR & Previous Year

Particulars	Rs. per MMBTU		
	FY 2007-08	FY 2008-09	
	FRR	RERR	The Petition
Units sold (BBTU)	351,733	381,207	356,442
Cost of gas sold	196.85	277.18	287.42
UFG adjustment per target	(2.17)	(4.12)	(1.26)
Transmission and distribution cost	17.84	13.41	24.81
Depreciation	6.13	7.27	7.48
Return on net average operating fixed assets	12.42	15.41	13.89
Other operating income	(18.10)	(20.99)	(12.02)
Subsidy for LPG Air-Mix Project	0.20	0.06	0.10
Cost of service / prescribed price	213.17	288.22	320.42
Current average prescribed price	213.17	288.22	289.31
Increase requested in average prescribed price	-		31.11



2.2 The petitioner has made the following submissions:-

- 2.2.1 The petitioner has claimed the required annual return, at Rs. 4,952 million, at the rate of 17% of the value of its average net operating fixed assets (net of deferred credit, Air-Mix LPG, & meter manufacturing plant) before corporate income taxes, and interest, mark-up and other charges on debt, per license condition No. 5.2 and covenants of the loan agreement between the petitioner and the Asian Development Bank (ADB).
- 2.2.2 The petitioner has claimed a gross addition of Rs. 7,604 million in the fixed assets, and net addition, ex-depreciation and deletion, of Rs. 4,616 million, resulting in claimed increase in the net operating fixed assets from Rs. 31,290 million in FY 2007-08 to Rs. 35,906 million during the said year. The petitioner has further claimed that, after adjustment of deferred credits and assets related to Air-mix LPG Project & meter manufacturing plant, the net average operating fixed assets eligible for return work out to Rs. 29,130 million, and the required return to Rs. 4,952 million.
- 2.2.3 The net operating revenues have been claimed at Rs. 107,229 million in the petition, as against Rs. 117,872 million determined in RERR, as detailed below:

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

Description	Rs. in Million				
	FY 2007-08	FY 2008-09		Increase / (Decrease) over RERR	
	FRR	RERR	The Petition		%
Net sales at current prescribed price	74,980	109,872	102,944	(6,928)	(6)
Meter rentals	531	548	552	4	1
Late payment surcharge	425	348	-	(348)	(100)
Amortization of deferred credit	176	332	298	(34)	(10)
Sale of gas condensate	631	436	197	(239)	(55)
Meter manufacturing profit	66	104	-	(104)	(100)
Gas transportation charges	23	578	18	(560)	(97)
Income from JJVL	4,174	5,479	2,942	(2,537)	(46)
Other operating income	339	175	278	103	59
Net Operating Revenues	81,345	117,872	107,229	(10,643)	(9)

- 2.2.4 The net operating expenses have been claimed at Rs. 113,330 million in the petition as compared to Rs. 111,972 million provided in RERR, as detailed below:



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

Description	Rs. in million				
	FY 2007-08	FY 2008-09		Increase / (Decrease) over RERR	
		FRR	RERR	The Petition	
Cost of gas	69,238	105,662	102,448	(3,214)	(3)
Transmission and Distribution costs	4,870	4,882	5,456	574	12
UFG disallowance above allowable limit	(762)	(1,572)	(451)	1,121	(71)
Gas Internally Consumed (GIC)	120	177	141	(36)	(20)
Depreciation	2,157	2,771	2,668	(103)	(4)
Re-claimed items	188	-	(3)	(3)	-
Financial charges on short determination by OGRA	-	-	484	484	-
Other Charges including WPPF	1,098	52	2,587	2,535	4,875
Net Operating Expenses	76,909	111,972	113,330	1,358	1

2.2.5 The Unaccounted for Gas (UFG) has been claimed at 5.60% (23,664 MMCF) as against the upper and lower target of 5.50% and 4.80%, respectively, fixed by the Authority for the said year, with the request to consider 100% UFG of Balochistan as a pass through item, over and above the upper target of UFG.

2.2.6 The petitioner has claimed subsidy amounting to Rs. 35 million on account of Air-Mix LPG Project, being undertaken by it in accordance with the directions of the GoP.

2.2.7 The net result of the petitioner's above mentioned claims is that a shortfall of Rs. 11,088 million has been computed including 17% return on average net operating fixed assets, which translates to an increase of Rs. 31.11 per MMBTU in the existing average prescribed price, as tabulated below:

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

Particulars	Rs. in Million	
	FY 2008-09	The Petition
A Net operating revenues	107,229	
B Less: Net operating expenses excluding ROA	113,330	
Subsidy Air Mix LPG Project		35
Total Expenses	113,365	
C Surplus / (Shortfall) {(A) - (B)}	(6,136)	
D Return required @ 17% on net fixed assets in operation.	4,952	
E Total (shortfall) / surplus in the revenue requirement {(C) - (D)}	(11,088)	
F Sale volume (BBTU)	356,442	
G (Increase) / Decrease requested in existing average prescribed price. Rs. / MMBTU (E/F*1000)		(31.11)



3. Proceedings

- 3.1 The petitioner was represented at the hearing by a team of senior executives led by its Deputy Managing Director, Mr. Azim Iqbal Siddiqui, 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 the members and officers of the Authority.
- 3.2 In the hearing, Mr. Tariq Ali Shah, Deputy Secretary, Finance Division representing Government of Sindh, showed deep concern over decreasing amount of GDS in the last two years. It was also proposed to keep cushion in the sale & prescribed price, so that Provincial Governments can have reasonable amount of GDS for their development projects.

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% 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 a return, pursuant to *License Condition No. 5.3* of the license 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, is pending with GoP. Pending its finalization, the Authority has decided, to follow the existing basis of 17% return on the average net operating fixed assets, in accordance with the License Condition No. 5.2.



6. Operating Fixed Assets

6.1 Summary

6.1.1 The petitioner has claimed a gross addition of Rs. 7,604 million in the fixed assets, and net addition, ex-depreciation and deletion, of Rs. 4,616 million, resulting in claimed increase in the net operating fixed assets from Rs. 31,290 million in FY 2007-08 to Rs. 35,906 million during the said year. The petitioner has further claimed that, after adjustment of deferred credits, and assets related to Air-mix LPG Project & meter manufacturing plant, the net average operating fixed assets eligible for return work out to Rs. 29,130 million, and the required return to Rs. 4,952 million, as tabulated below:

Table 5: Computation of Return on Assets per the Petition

Particulars	Rs. in million
Net operating fixed assets at beginning	31,290
Net operating fixed assets at closing	35,906
Sub-total:	67,196
Average net assets (A)	33,598
Meter manufacturing plant assets at beginning	58
Meter manufacturing plant assets at closing	51
Sub-total:	108
Average net assets (B)	54
LPG air mix assets at beginning	80
LPG air mix assets at closing	80
Sub-total:	160
Average net assets (C)	80
Deferred credit at beginning	3,820
Deferred credits at closing	4,847
Sub-total:	8,666
Average net deferred credit (D)	4,333
Average (A-B-C-D)	29,130
Return required on net operating fixed assets	17%
Amount of return requested by the petitioner	4,952

6.1.2 The Authority observes that the petitioner has excluded assets of meter manufacturing plant from the rate base for the said year, by reiterating its contention



that the business is not a regulated activity.

- 6.1.3 The Authority, in view of discussions and decision in various earlier determinations, disagrees with the petitioner's claim, and, *therefore, includes assets related to meter manufacturing plant in the rate base for the said year.*
- 6.1.4 The Authority also notes that the petitioner has adjusted Rs. 90 million in the opening balance of deferred credit owing to the adjustment per its audited accounts, thereby claiming it at Rs. 3,820 million as against Rs. 3,730 million determined in FRR for FY 2007-08. The Authority accepts the same & determines the opening balance of deferred credit at Rs. 3,820 million for the said year.
- 6.1.5 The petitioner has included Rs. 92 million on account of IT related assets pertaining to FY 2006-07 and FY 2007-08 in the rate base entitled for return for the said year, details are provided as under:

Table 6: Detail of IT Related Assets Claimed by the Petitioner

Description	Year of Expenditure	Rs. in million
		Amount
Computer Hardware	2006-07	42
Software	2006-07	23
Software	2007-08	28
Total		92

- 6.1.6 The petitioner has included Rs. 65 million on account of IT related assets pertaining to FY 2006-07, which were disallowed by the Authority in FRR FY 2006-07 dated September 14, 2007, subject to the provision of specific information in this respect.
- 6.1.7 The Authority also disallowed IT related expenditure amounting to Rs. 28 million pertaining to GIS & ERP per para 6.2.3 of the FRR FY 2007-08 dated September 23, 2008 on the premise that overall IT project is currently under Authority's comprehensive review and decision on the same will be issued separately.
- 6.1.8 The petitioner has argued that it has already submitted the information relating to need assessment and cost benefit analysis of Oracle ERP, CIS & GIS systems. However, no separate decision has yet been issued by the Authority in this respect.



The petitioner has, therefore, included IT related capital and revenue expenditure in the instant petition.

6.1.9 The Authority observes that the petitioner had incurred capital expenditure amounting to Rs. 26 million, out of total Rs. 92 million, on GIS project in FY 2006-07 & FY 2007-08. The Authority notes that GIS project is now complete, and the petitioner is anticipating handsome revenues through fees against the provision of services to various private and public entities. Such expenditure can not be allowed in the light of the Authority's latest decision, wherein the petitioner has been directed to meet all GIS related capital & revenue expenditure through fee for the provision of services to other entities.

6.1.10 *In view of above, the Authority disallows Rs. 26 million related to GIS project, and resultantlly includes balance figure of Rs. 66 (Rs. 92 M – Rs. 26 M) million in the rate base.*

6.1.11 *Consequently, the Authority determines the opening balance of net operating fixed assets at Rs. 31,264 million.*

6.1.12 Comparative analysis of additions in fixed assets as claimed by the petitioner compared with RERR is as follows:



Table 7: Summarized Schedule of Additions Compared with RERR

Particulars	Rs. in Million			
	FY 2008-09		Inc./(Dec.) over RERR	
	RERR	The Petition	Rs.	%
Land	30	4	(26)	-88
Building	100	139	39	39
Transmission line	1,399	732	(667)	(48)
Compressor	130	119	(11)	(9)
Plant & machinery	263	111	(152)	(58)
Gas distribution system	5,791	5,845	54	1
Road, pavements and related ROW	440	-	(440)	(100)
Furniture & fixtures	120	106	(14)	(11)
Computer software (Intangible)	73	40	(33)	(46)
Appliances loose tools & equipment	30	31	1	5
Telecommunication system	5	16	11	218
Vehicles	215	174	(41)	(19)
Construction equipment & vehicles	239	192	(47)	(20)
LPG Air-Mix	34	6	(28)	(82)
SCADA	77	89	12	16
Total addition	8,946	7,604	(1,343)	(15)
Less:				
Assets related to meter plant		9	9	
LPG Air-Mix	34	6	(28)	(82)
Assets related to gas activity	8,912	7,588	(1,324)	(15)

6.1.13 The petitioner has reported 39% increase under the head of "Building" mainly owing to completion of some delayed projects pertaining to previous years. The petitioner also submitted that the Authority, at the time of DERR for the said year, had restricted the said expenditure at Rs. 100 million as against its claim of Rs. 346 million. The detailed justifications / explanations for increase in the said head have been submitted with the Authority.

6.1.14 The petitioner has explained that the exorbitant increase on account of "Telecommunication system" expenditure is due to the installation of Global System for Mobile Communication (GSM) / General Packet Radio Service Remote Communication System (GPRS). The petitioner has also informed that Rs. 6 million has been incurred for the up gradation of Hicom system to Hi-path communication server. This system is likely to result in daily saving of revenues in terms of petroleum, oil & lubricants, overtime, manpower and travel time. It will also be beneficial for online monitoring of consumer's meter stations and reduction in visits for low pressure complaints.

6.2 IT Related Expenditure

6.2.1 The petitioner has incurred Rs. 169 million in respect of capital and revenue IT related



expenditure during the said year. The amount has been booked by the petitioner under various heads, break-up of which is as under:

Table 8: Detail of IT Related Expenditure per the Petition

Nature of Expenditure	Expenditure Type	Head of Account	Rs. in million
Capital	Computer and Ancillary Equipment	Furniture & Equipment	45
	Computer Software	Intangible Asset	40
		Sub-total:	85
Revenue	Software Licence & Dev. Charges	Legal & Prof. Charges	20
	Software Maint. Charges	Repair & Maintenance	43
	Computer Rep. & Maintenance	Repair & Maintenance	21
		Sub-total:	84
Total			169

6.2.2 The Authority observes that the petitioner has claimed Rs.7 million under “computer software” and Rs. 4 million as part of “software maintenance charges” pertaining to GIS.

6.2.3 *The Authority, per the discussion in para 6.1.9 above, excludes Rs. 11 million from computation of Revenue Requirement for the said year.*

6.2.4 *The Authority, in view of the above, allows IT - related expenditure at Rs. 158 million, as under:-*

Table 9: IT Related Expenditure Determined by the Authority

S No.	Particulars	Rs. in million
	Capital Expenditure	
1	Computers & ancillary equipment	45
2	Computer software	33
	Revenue Expenditure	
1	Software Licence & Dev. Charges	20
2	Software Maint. Charges	39
3	Computer Rep. & Maintenance	21
	Total	158



6.3 Assets Relating to Meter Manufacturing Business

- 6.3.1 The petitioner has excluded addition of Rs. 9 million pertaining to meter manufacturing business from the rate base of the said year.
- 6.3.2 *The Authority, per the discussion in paras 6.1.2 & 6.1.3 above, maintains its earlier decision of treating the meter manufacturing business as operating activity, and therefore includes the same into operating assets for the said year.*
- 6.3.3 *The Authority, after due diligence and detailed examination of the submissions made by the petitioner, provisionally determines the additions in fixed assets at Rs. 7,606 million for the said year.*

6.4 Fixed Assets Determined by the Authority

- 6.4.1 *Depreciation expense claimed by the petitioner would reduce by Rs. 11 million as a result of adjustments discussed & decided in para 6.1.10 & 6.2.4 above.*
- 6.4.2 *After adjustment of depreciation per para 6.4.1 above, the closing net operating fixed assets for the said year are determined at Rs. 35,884 million, subject to adjustments, if any, based on findings of cost and procurement audit proposed to be instituted by the Authority.*

7. Operating Revenues

7.1 Sales Volume

- 7.1.1 Sales volume has decreased by 6%, from 381,207 BBTU determined in RERR to 356,442 BBTU in the petition. Category-wise comparison with previous year has been provided by the petitioner as under:



Table 10: Comparison of Category-wise gas Sales per the Petition with RERR and Previous Year

Category	Volume in BBTU				
	FY 2007-08	FY 2008-09		Inc. / (Dec.) over RERR	
	FRR	RERR	The Petition		%
Cement	3,255	3,637	4,122	485	13
CNG Stations	16,283	18,560	20,611	2,051	11
Captive Power	40,477	45,125	44,170	(955)	(2)
Commercial	9,642	9,937	9,115	(822)	(8)
Al-Tuwairqi Steel	-	8,847	-	(8,847)	(100)
DHA desalination plant	1,711	5,293	682	(4,611)	(87)
Domestic	63,770	65,290	62,296	(2,994)	(5)
Fertilizer	20,988	27,102	26,157	(945)	(3)
General Industries	78,708	77,498	67,806	(9,692)	(13)
Habibullah Coastal Power	7,756	7,624	7,971	347	5
Power	109,144	112,294	113,512	1,218	1
Total-	351,734	381,207	356,442	(24,765)	(6)

7.1.2 The petitioner has explained that gas sales volume has decreased by 6% mainly due to lesser off-takes from various gas fields. The petitioner further submitted that regular supply of gas from Sinjhor and Zarghun gas fields was anticipated at the time of DERR, however, delay in gas supply from these fields has also contributed towards decrease in sales volume for the said year.

7.1.3 The petitioner has elaborated that 87% lesser sale to DHA desalination plant is due to the fact that the said plant closed down effective September, 2008 owing to technical reasons. Also, Al-tuwairqi steel did not start its operations resulting in nil sales to this customer. The petitioner has also asserted that law and order situation, global recession and financial crunch have also resulted in lower gas sales to textile, industrial and commercial consumers.

7.1.4 *The Authority accepts the total sales volume at 356,442 BBTU for the said year.*

7.2 Sales Revenue at Existing Prescribed Prices

7.2.1 Sales revenue at existing prescribed prices claimed in the petition is Rs. 102,944 million. Category-wise comparison with RERR and previous year is given below;



Table 11: Comparison of Category-wise Sale Revenues per the Petition with RERR and Previous Year

Category	Rs. in million				
	FY 2007-08	FY 2008-09		Inc. / (Dec.) over RERR	
	FRR	RERR	The Petition	Rs.	%
Cement	1,053	1,570	1,807	237	15
Fertilizer	1955	3,083	2,768	(315)	(10)
CNG Stations	4,541	7,005	8,033	1,028	15
Captive Power	9,918	14,710	14,682	(28)	(0.19)
Habibullah Coastal Power	1,899	1,938	2,093	155	8
Commercial	2,763	5,511	3,507	(2,004)	(36)
Al-Tuwairqi Steel	-	2,905	-	(2,905)	(100)
DHA Desalination Plant	-	1,347	172	(1,175)	(87)
General Industries	18,570	25,261	22,723	(2,538)	(10)
Domestic	7,516	9,959	8,997	(962)	(10)
Power	26,765	36,583	38,163	1,580	4
Total:-	74,980	109,872	102,944	(6,928)	(6)

7.2.2 The Authority observes that reduction in sale revenue for the said year, as compared to RERR, is due to the reasons mentioned in paras 7.1.2 and 7.1.3 above.

7.2.3 *The Authority determines the sales revenue at Rs. 102,944 million for the said year.*

7.3 Other Operating Income

i. Summary

7.3.1 The petitioner has claimed other operating income at Rs. 4,285 million in the petition as against Rs. 8,000 million provided in RERR. Detailed breakup is compared below:

Table 12 Comparison of Other Operating Income per the Petition with RERR and Previous Year

Description	Rs. in Million				
	FY 2007-08	FY 2008-09		Increase / (Decrease) over RERR	
	FRR	RERR	The Petition		%
Meter rentals	531	548	552	4	1
Late payment surcharge	425	348	-	(348)	(100)
Amortization of deferred credit	176	332	298	(34)	(10)
Sale of gas condensate	631	436	197	(239)	(55)
Meter manufacturing profit	66	104	-	(104)	(100)
Gas transportation charges	23	578	18	(560)	(97)
Income from JJVL	4,174	5,479	2,942	(2,537)	(46)
Other operating income	339	175	278	103	59
Net Operating Revenues	6,365	8,000	4,285	(3,715)	(46)

ii. Meter Manufacturing Profit (MMP) & Late Payment Surcharge(LPS)



- 7.3.2 The petitioner has claimed MMP (Rs. 39 million) & LPS (Rs. 576 million) as non-operating income in the instant petition, however, the same were claimed at Rs. 104 million & Rs. 348 million as operating income at the time of RERR for the said year.
- 7.3.3 The petitioner has submitted that the Authority has so far relied on the directive obtained by it under Section 47 of the Ordinance, which was issued to facilitate OGRA, in the absence of NGT Rules and the petitioner's license, etc, for determination of revenue requirement for FY 2001-02 and FY 2002-03. GoP directed to follow the existing tariff regime till such time an appropriate rate of return is determined by OGRA in consultation with it. Under this directive of GoP, OGRA is required to assess the revenue requirement per the ex-PDA practices and ADB covenants, provided these practices should be consistent with the Ordinance.
- 7.3.4 The petitioner has argued that OGRA was obligated to implement the directive with reference to ex-PDA practice only to the extent that was lawful & consistent with the provisions of the Ordinance.
- 7.3.5 MMP is a non-core business activity and does not fall under the regulated activities per the provisions of the Ordinance. The Authority had also accepted MMP as non-operating income in principle, since it proposed to treat it as non-operating income under the new tariff regime.
- 7.3.6 LPS is also a non-regulated income as it is an interest income being financial compensation for delayed payment of gas dues by defaulting consumers. The Authority had also proposed to treat it as non-operating income in the new tariff regime.
- 7.3.7 The Authority notes that issue of MMP & LPS was not brought up by the petitioner at the time of submission of its petition for ERR for the said year, hence the principle of estoppel is applicable.
- 7.3.8 Even otherwise, the Authority had already decided the issue of LPS & MMP in its various earlier determinations after considering the points raised by the stakeholders, and in pursuance of the directive of the GoP issued on October 11, 2002 under Section 47 of the Ordinance. The Authority is of the firm view that treatment of any



component of the tariff regime (e.g. LPS & MMP) can not be changed in isolation, while the petitioner continues to get return @17% on fixed assets as stipulated in loan covenant. The tariff regime is a package and has to be enforced in totality. These issues can, however, be sorted out while finalizing the new tariff regime. The Authority observes that no new argument has been advanced to warrant any change in this decision.

7.3.9 *In view of above, the Authority maintains its earlier decision and includes Rs. 615 million (Rs. 39 M+ Rs. 576 M) as operating income for the said year.*

iii. Sale of Gas Condensate

7.3.10 The petitioner has claimed income from sale of gas condensate at Rs. 197 million as against Rs. 436 million determined in RERR for the said year.

7.3.11 The petitioner has submitted that ex-PDA's practice of treating sale of gas condensate as operating income is inconsistent with the Ordinance, since condensate is defined as crude oil & not natural gas under the provisions of the Ordinance; hence it is a non-operating income.

7.3.12 The petitioner has argued that LHF was provided to it free of cost by Badin field producer as per the terms of the agreement. Therefore, the Authority's argument that LHF's activity is financed through gas price is not justified. Moreover, transporting gas through the petitioner's transmission network upto LHF facility does not disqualify condensate for separate treatment as crude oil.

7.3.13 The petitioner has also requested the Authority to revisit its approach and consider segregation of non-regulated income from regulated income in tariff calculations. The petitioner has asserted to develop some rationale for allocating / apportioning expenditure from the common cost if any from such non-regulated income.

7.3.14 The Authority notes that issue of sale of gas condensate was not brought up by the petitioner at the time of submission of its petition for ERR for the said year, hence the principal of estoppel is applicable.

7.3.15 The Authority observes that condensate is extracted as a by-product from the natural



gas at LHF plant. During extraction, gas shrinkage occurs along-with reduction in calorific value. It is, therefore, established that condensate extraction is not a stand-alone independent project rather it is an additional source of revenue for the petitioner that emerged while carrying out the principal activity of transmission, distribution and sale of natural gas. Furthermore, the petitioner also claims benefit by adding gas consumed at the plant in the net sales while calculating UFG.

7.3.16 *In view of the above, the Authority disagrees with the petitioner's contention and, therefore, maintains treatment of sale of gas condensate as operating income and determines the same at Rs. 504 million for the said year.*

iv. Royalty from Jamshoro Joint Venture Limited (JJVL)

7.3.17 The petitioner has requested that royalty from JJVL amounting to Rs. 1,657 million be treated as non-operating income. The petitioner has argued that it had the right to process LPG under its GSA with gas producer, prior to the commissioning of JJVL plant. As per the terms of agreement with JJVL, the royalty was payable to the petitioner from the target commissioning date of JJVL plant, irrespective of actual start of its commercial operations, and it will remain payable to it till the entire term of this agreement.

7.3.18 The petitioner is of the view that compensation amount is payable on account of reduction in calorific value of Composite Associated Gas Mixture (CAGM), while the royalty is payable against its right to process CAGM available at the facility. The very purpose of royalty is to provide incentive rather than to increase petitioner's profitability.

7.3.19 The petitioner has also asserted that royalty has not been included as income from regulated activity in the Ordinance and NGT Rules, which confirms that it is a non-regulated income from a non-core activity.

7.3.20 The petitioner has further argued that the said pipeline was not laid to supply gas to JJVL plant therefore it should not be treated as an investment for recovery of royalty. Royalty income started accruing in the income stream of the petitioner without any incremental investment, after execution of agreement with JJVL, since gas was already



available at plant location.

7.3.21 Gas transmission & distribution 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 as defined in the Ordinance, NGT Rules and the petitioner's license.

7.3.22 The Authority notes that the reasons advanced now by the petitioner are not new and repetition of its previous position. The Authority has time and again reviewed and analysed the submissions of the petitioner in its various earlier decisions. The Authority has always given a conscious thought to the submissions of the petitioner and after analyzing / considering the arguments from all stakeholders, has decided to treat royalty from JJVL as operating income.

7.3.23 *In view of above, the Authority maintains its decision of treating royalty from JJVL amounting to Rs. 1,657 million, as operating income for the said year.*

v. Gas Transportation Income

7.3.24 The petitioner has claimed gas transportation income at Rs. 18 million for the said year compared with Rs. 23 million determined in FRR for FY 2007-08. The petitioner has explained that gas transportation income is recovered on the basis of contractual arrangements / pipeline rental agreements with OGDCL for the use of 40 Km segments from Paish Bogi to Pirkoh, and with SNGPL for use of Bhit, Zamzama and Hassan gas pipeline. The petitioner, at the time of finalization of accounts, recognizes these rental arrangements as leases in terms of IFRIC-4. In accordance with the requirements of IFRIC-4, the pipelines are recognized as net investment in finance leases and the related depreciation, operating cost and return are also reclassified and recorded as recoveries, in their respective heads. Based on above, Rs. 18 million has been recorded as gas transportation income as against total income of Rs. 565 million on this account for the said year.

7.3.25 *The Authority accepts the gas transportation income at Rs. 18 million for the said year.*

vi. Other Income



7.3.26 The petitioner has claimed other income for the said year at Rs. 278 million as against Rs. 175 million in RERR. Detailed breakup with comparison is as under:

Table 13: Comparison of Other Income per the Petition with RERR and Previous Year

Particulars	Rs. in million				
	FY 2007-08	FY 2008-09		Inc./ (Dec.) over RERR	
	FRR	RERR	The Petition		%
Recoveries from consumers	19	30	45	15	49
Profit on disposal of fixed assets	0.27	20	(13)	(33)	(164)
Liquidated damages recovered	3	20	-	(20)	(100)
Income from sale of net investment in finance lease	230	-	214	214	-
Income from sale of tender documents	3	1	1	0.28	28
Notional income on IAS 19 provision	65	91	-	(91)	(100)
Realized gain on foreign transaction	0.15	-	-	-	-
Advertising Income	4	9	-	(9)	(100)
Others	14	5	31	27	589
Total Other Income	339	175	278	103	59

7.3.27 The Authority observes that increase in other income by 59% is mainly due to the inclusion of "Income from sale of net investment in finance lease", which was previously booked under "Gas Transportation Income" as explained in para 7.3.24 above.

a. Notional Income on IAS 19 Provision & Advertising Income

7.3.28 The petitioner has claimed notional income on IAS-19 provision (Rs. 105 million) and advertising income (Rs. 6 million) as non-operating incomes, and has excluded the same from other operating income offered for the said year.

7.3.29 The petitioner has submitted that ex-PDA had not added notional income on IAS-19 provision as part of its operating revenues, therefore, inclusion of the same by the Authority is not in accordance with the spirit of GoP directive of the year 2002.

7.3.30 The petitioner has submitted that the Authority has been delaying the treatment of MMP & LPS as non-operating subject to the receipt of policy guidelines from GoP in this respect. On the contrary, the Authority has been including notional income on IAS-19 provision as part of revenue requirement, which is a deviation from ex-PDA practice, without obtaining any advice / directive from GoP.

7.3.31 The petitioner has also argued that, by nature, this return is an interest income, which



is expressly excluded from the definition of operating income in the ADB loan covenants.

7.3.32 The petitioner has also requested to exclude advertising income from operating income, since this is a non-core income, not directly attributable to regulated activities of the petitioner.

7.3.33 The Authority notes that issue of treating advertising income & notional income on IAS -19 provision as non-operating incomes, was not raised by the petitioner at the time of submission of its petition for ERR for the said year, hence the principle of estoppel is applicable. Also, these incomes were offered as operating incomes in all earlier petitions by the petitioner.

7.3.34 In view of the above, the Authority disagrees with the petitioner's contention and, therefore, maintains treatment of advertising income and notional income on IAS -19 provision as operating income.

b. Liquidated Damages Recovered

7.3.35 The petitioner has requested to treat liquidated damages recovered amounting to Rs. 16 million as non-regulated income, since this is not directly related to the petitioner's core business of transmission, distribution and sale of natural gas.

7.3.36 The petitioner has submitted that liquidated damages are recovered from its suppliers on account of delayed supplies as per the terms of their respective purchase orders etc. The clause for payment of liquidated damages triggers when a supplier fails to deliver goods within the agreed time frame / schedule of supplies agreed. The petitioner has, therefore, requested to discontinue ex-PDA's practice of treating liquidated damages as operating income since it is a non core income.

7.3.37 The petitioner has also mentioned that the Authority has been rightly allowing liquidated damages to other sister utility i.e. SNGPL as non operating income since FY 2004-05.

7.3.38 The Authority observes that liquidated damages accrued on account of delayed supplies of material by the supplier resulted in delayed completion of project, thereby affecting the interests of shareholders as well as consumers. The consumers would be



bearing the burden of additional costs on account of this delay and the shareholder's suffered as return on the asset was delayed.

7.3.39 The Authority also notes that it has been allowing 50% of the liquidated damages to SNGPL since its decision dated October 26, 2005 of FRR for FY 2004-05.

7.3.40 *In view of above, the Authority allows 50% of the liquidated damages recovered in order to split the gain between consumers and shareholders equally. The Authority, therefore, includes Rs. 8 million as an operating income for the said year.*

7.3.41 *In view of the above, the Authority determines other income at Rs. 397 million as against Rs. 278 million claimed by the petitioner for the said year.*

7.3.42 *Keeping in view the discussion from para 7.3.2 to 7.3.41 above, the Authority determines the total other operating income at Rs. 6,982 million for the said year as against Rs. 4,285 million claimed by the petitioner, as detailed below:*

Table 14 Summary of Other Operating Income Determined by the Authority

S.no	Particulars	Rs. in million	
		Claimed by the Petitioner	Determined by the Authority
1	Meter rentals	552	552
2	Late payment surcharge	-	576
3	Amortization of deferred credit	298	298
4	Sale of gas condensate	197	504
5	Meter manufacturing profit	-	39
6	Gas transportation charges	18	18
7	Income from JJVL	2,942	4,600
8	Other operating income:		
	IAS 19 provision	-	105
	Advertising income	-	6
	Liquidated damages recovered	-	8
	Remaining items of other operating income	278	278
	Total operating revenues	4,285	6,982

8. Operating Expenses

8.1 Cost Of Gas

8.1.1 The cost of gas per petition is Rs. 102,448 million, compared with Rs. 105,662 million determined in RERR, lower by Rs. 3,214 million (3%).

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 SNGPL at Rs. 251.73 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. 259.06 per MMBTU as under:

Table 15: Weighted Average Cost of Input Gas

Company	MMCF	BBTU	Rs in million	Rs / MMBTU
SSGCL	423,194	403,144	132,710	329.19
SNGPL	652,493	607,202	129,026	212.49
Total	1,075,687	1,010,346	261,736	259.06

8.1.3 The above increase in weighted average cost of gas, compared to RERR, is mainly due to increase in US \$ exchange rate from Rs. 75 per RERR to Rs. 81. Further, the working is now based on payments actually made by the petitioner and SNGPL for purchase of gas in accordance with wellhead gas prices as notified by the Authority.

8.1.4 *The Authority, in view of the above discussion, accepts the cost of gas sold at Rs. 102,448 million for the said year.*

8.2 Unaccounted for Gas (UFG)

8.2.1 The petitioner has claimed Unaccounted for Gas (UFG) at 5.60% (23,664 MMSCF) for the said year, as follows:

Table 16: Comparison of Unaccounted for Gas per Petition with RERR & Previous Year

Particulars	Volumes in MMCF		
	FY 2007-08	FY 2008-09	
	FRR	RERR	The Petition
Gas Purchases	408,484	435,501	422,387
Gas Sales	381,391	406,596	389,347
	27,093	28,905	33,040
Less: 100% UFG for Balochistan - a pass through item			9,376
UFG	27,093	28,905	23,664
UFG (%age of purchase)	6.63%	6.64%	5.60%

8.2.2 The petitioner has submitted that it could not achieve the desired results of its UFG reduction plan, 2005 despite its level best efforts. The petitioner, at that time,



anticipated to reduce UFG to the level of 5% in FY 2010-11, which shows that the problem is graver than considered previously.

- 8.2.3 The petitioner has pleaded that selling price has considerably increased, which has prompted the poor consumers to use gas through line punching, direct use etc, resulting into enhanced UFG through theft.
- 8.2.4 The deteriorating law & order situation in Balochistan, particularly in the remote areas, has accelerated the UFG during the period, especially from FY 2006-07 onwards.
- 8.2.5 The petitioner is also required to extend the network in remote areas of Sindh & Balochistan in order to meet GoP objectives to provide cheap and environment friendly fuel to maximum population. In such areas, gas theft through line punching, meter tampering and direct connection is a common practice and people steal gas without any fear. The petitioner, whenever tried to disconnect such conspicuous customers, law & order situation erupted especially in Balochistan. The petitioner has already conveyed such instances to the Authority and GoP.
- 8.2.6 The petitioner has submitted that increasing theft, especially in Balochistan, is a dominant factor in its overall UFG. The petitioner has recently separately provided the information on gas theft to the Authority, which further substantiates its submissions.
- 8.2.7 The petitioner has requested to review UFG target on these ground realities, since it will adversely impact with irreparable losses, jeopardizing its whole operations as a going concern.
- 8.2.8 The petitioner has, therefore, requested to allow 9,376 MMCF, being the volume of UFG related to Balochistan, outside the tariff formula.
- 8.2.9 The Authority observes that the petitioner has been allowed substantial amount of expenditure for UFG control related activities and security expenses on continuous basis, especially for Balochistan region. This high level of UFG shows that funds



through gas price mechanism have not been properly utilized by the petitioner, which is an evidence of unprofessional and reckless spending.

8.2.10 The Authority maintains its earlier decision of fixing upper & lower targets of UFG at 5.50% & 4.80% respectively, with the condition that the petitioner would be entitled to retain the savings in the event of performance being better than the lower target, fully bear UFG above the upper target from its own profits whereas UFG between the lower & upper target be adjusted in the revenue requirement to the extent of 50% and the balance 50% be borne by the petitioner from its own profit.

8.2.11 The Authority, however, is planning to undertake a comprehensive impact assessment study of the UFG benchmarks introduced by it. Any change in the benchmark, if required, will be considered on the completion of the said study.

8.2.12 *In view of above, the Authority determines UFG volume at 33,040 MMCF i.e. 7.82% including UFG in Balochistan as part of tariff formula.*

8.2.13 The Authority observes that the petitioner has calculated the UFG disallowance of Rs. 451 million at Rs. 25477 per MMBTU instead of WACOG of Rs. 259.06 per MMBTU for the said year.

8.2.14 *The Authority, therefore, disallows UFG above the benchmark for the said year per its earlier decision mentioned above, which will reduce the operating expenditure by Rs. 2,707 million.*

8.3 Transmission & Distribution (T & D) Cost

i. Summary

8.3.1 The petitioner has claimed that the transmission and distribution cost has increased by 10% i.e. from Rs. 5,059 million provided in RERR to Rs. 5,548 million, as compared below:

Table 17: Comparison of T & D Cost per the Petition with RERR & Previous Year



Particulars	Rs. in million					
	FY 2007-08	FY 2008-09		Inc./(Dec.) over RERR		
	FRR	RERR	The Petition	Rs.	%	
Salaries, wages, and benefits (HR cost)	3,551	3,758	4,136	378	10	
Stores, spares and supplies consumed	377	470	429	(41)	(9)	
Material used on consumers installations	26	132	165	33	25	
Electricity	64	79	73	(6)	(8)	
Rent, rate and taxes	61	73	71	(2)	(3)	
Legal and professional charges	111	49	63	13	29	
Travelling	59	65	67	2	3	
Insurance	59	78	64	(14)	(18)	
Postage and revenue stamps	63	73	69	(3)	(5)	
Repairs and maintenance	484	487	643	157	32	
License and tariff regulation fee to OGRA	44	64	59	(5)	(7)	
Meter reading by contractors	35	48	35	(14)	(29)	
Collecting agent commission	2	3	0.26	(3)	(92)	
Security expenses	224	173	180	7	4	
Gas bills collection charges	127	142	138	(4)	(3)	
Gas bills stubs processing charges	14	16	15	(1)	(6)	
Provision for doubtful debts	130	146	249	103	71	
Advertisement	38	45	38	(6)	(14)	
Provision for slow moving obsolete stores	5		-	-		
Others	94	76	73	(3)	(4)	
Sub-total expenses	5,568	5,976	6,566	590	10	
Add: Project Cost						
Interstate Gas Company Limited (ISGSL)	97		37	37		
Expenditure relating to LNG project	50	53	18	(35)	(66)	
	5,715	6,029	6,621	592	10	
Less: Recoveries / Allocations	712	1,021	1,065	44	4	
Recoveries / Refund of Services	188		218	218		
ISGSL prior year disallowance		471		(471)	(100)	
Net T&D exp. before gas internally consumed	4,814	4,537	5,338	801	18	
Add: Gas internally consumed	120	177	141	(36)	(20)	
Loss due to sabotage activity	55	-	69	69	100	
ISGSL prior year disallowance		345		(345)		
Total T&D expenditure	4,990	5,059	5,548	489	10	

8.3.2 Various components of T & D cost are discussed in the following paragraphs:

ii. Human Resource (HR) Cost

8.3.3 The petitioner has claimed HR benchmark cost for the said year at Rs. 4,136 as against Rs. 3,758 million provided in RERR.

8.3.4 The petitioner has calculated the HR cost benchmark by taking the actual HR cost of FY 2004-05 as base figure, indexed to increase in number of consumers with 60% weightage, increase in network with 20% weightage, gas sales volume with 20% weightage, alongwith inflation adjustment to the extent of 50% of CPI.

8.3.5 The Authority observes that it had introduced the HR benchmark on experimental basis for three years i.e. FY 2004-05 to FY 2007-08. Subsequently, the Authority per its decision on motion for review of DERR FY 2005-06 dated October 12, 2005, decided



that the said benchmark will be reviewed after the results for FY 2007-08 become available.

8.3.6 The Authority further observes that while determining the ERR for FY 2009-10, it had provisionally revised the HR cost benchmark taking the actual HR cost of FY 2007-08 as base figure while indexing the same to the following:

- *50% increase in number of consumers*
- *20% increase in sale volume*
- *20% increase in T & D network*
- *50% CPI adjustment of previous year HR benchmark cost*

The above stated benchmark was subject to the condition that only 50% over and above the benchmark will be adjusted in the revenue requirement.

8.3.7 The provisional benchmark was to be finalized after consultation with gas utilities. The Authority notes that the petitioner has computed the HR benchmark cost for the said year based on previously fixed parameters based on FY 2004-05 HR cost, instead of adopting the Authority's said decision in this regard.

8.3.8 The Authority, based on the submissions of both the gas utilities, is of the view that reduction in the weightage on account of increase in no. of consumers from 60% to 50% per the above stated decision has squeezed the HR cushion beyond a reasonable limit. The Authority, therefore, decides to reinstate the weightage on account of increase in no. of consumers again to 60% while keeping FY 2007-08 as base year intact. The weightage for increase in sale volume and T & D network will stay at 20% each respectively. The revised benchmark will remain applicable for three year period i.e. FY 2008-09 to FY 2010-11.

8.3.9 *In view of above, the Authority re-computes the HR cost benchmark at Annexure-D and allows Rs.4,154 million (including IAS-19) being the HR cost for the said year.*

iii. Repair & Maintenance

8.3.10 The petitioner has claimed Rs. 643 million on account of repair & maintenance, as against Rs. 487 million according to RERR, showing significant increase of 32%.



8.3.11 The petitioner has submitted that it has spent huge amount on the repair / maintenance of leakages and ruptures of T & D network in order to control the UFG. The petitioner has further explained that the Authority, in DERR for the said year, had reduced the expenditure on this account by 40%. However, the actual expenditure has increased due to the devaluation of rupee v/s US\$.

8.3.12 *The Authority, in accordance with the discussion and decision in paras 6.2.2 & 6.2.3 above, disallows Rs. 4 million on account of software maintenance charges and determines the repair & maintenance expense at Rs. 639 million for the said year.*

iv. Material Used on Consumers Installations

8.3.13 The petitioner has claimed Rs. 165 million on account of material used on consumers installations, as against Rs. 132 million according to RERR, showing an increase of 25%.

8.3.14 The petitioner has attributed the increase claimed under the above head mainly to inflation and increase in steel prices. Also, the number of jobs executed during the said year was more than envisaged in the original petition.

8.3.15 *In view of above, the Authority accepts the petitioner's claim on account of material used on consumers installations at Rs. 165 million for the said year.*

v. Legal & Professional Charges

8.3.16 The petitioner has claimed Rs. 63 million on account of legal & professional charges, as against Rs. 49 million determined in RERR, showing an increase of 29%. Historical comparison of legal & professional charges is given below:



Table 18: Comparison of Legal & Professional Charges per the Petition with RERR & Previous Year

Particulars	Rs. in million				
	FY 2007-08	FY 2008-09		Inc./(Dec.) over RERR	
	FRR	RERR	The Petition	Rs.	%
Legal charges	71	27	47	20	76
Professional charges	39	22	15	(7)	(32)
Total	111	49	63	13	29

8.3.17 The petitioner has submitted that increase reported under the head of legal charges is mainly due to the expenses incurred on account of ICC Arbitration in the matter of Habibullah Coastal Power Company (HCPC). The petitioner has informed that it has filed an appeal with Singapore High Court against the Arbitral Award by International Court of Arbitration. The petitioner has submitted that out of Rs. 47 million under the head of legal charges, Rs. 43 million has been incurred on HCPC matter as against Rs. 19 million claimed on this account in the original petition.

8.3.18 The Authority, in view of its latest decision on the matter of HCPC, provisionally disallows Rs. 43 million on this account for the said year subject to the final outcome of the petitioner's appeal pending with Singapore High Court.

8.3.19 *In view of above, the Authority determines Rs. 20 million on account of legal and professional charges for the said year.*

vi. Provision for Doubtful Debts

8.3.20 The petitioner has claimed Rs. 249 million on account of provision for doubtful debts, as against Rs. 146 million per RERR, for the said year, showing huge increase of 71%.

8.3.21 The petitioner has contested the earlier decision of the Authority per DERR for the said year, wherein it had restricted the provision at the level of FY 2006-07 i.e. Rs. 146 million. The petitioner has submitted that increase in actual disconnections of defaulting consumers has resulted in higher provision for the said year.

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

8.3.23 The Authority observes that the petitioner had been repeatedly directed by the



Authority, through its various earlier determinations, to make concerted efforts to curtail this ever-increasing expenditure on this account 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.

8.3.24 *In view of above, the Authority restricts the provision for doubtful debts at the level of RERR and allows Rs. 146 million for the said year.*

vii. Remaining Items of T & D Cost

8.3.25 Expenditure on remaining items of T & D cost, which have not been discussed above, is Rs. 1,366 million as against Rs. 1,458 million provided in RERR, as detailed below:

Table 19: Summary of Remaining T & D Expenses per the Petition with RERR & Previous Year

Particulars	Rs. in million				
	FY 2007-08	FY 2008-09		Inc./(Dec.) over RERR	
	FRR	RERR	The Petition	Rs.	%
Stores, spares and supplies consumed	377	470	429	(41)	(9)
Electricity	64	79	73	(6)	(8)
Rent, rate and taxes	61	73	71	(2)	(3)
Travelling	59	65	67	2	3
Insurance	59	78	64	(14)	(18)
Postage and revenue stamps	63	73	69	(3)	(5)
License and tariff regulation fee to OGRA	44	64	59	(5)	(7)
Meter reading by contractors	35	48	35	(14)	(29)
Collecting agent commission	2	3	0.26	(3)	(92)
Security expenses	224	173	180	7	4
Gas bills collection charges	127	142	138	(4)	(3)
Gas bills stubs processing charges	14	16	15	(1)	(6)
Advertisement	38	45	38	(6)	(14)
Provision for slow moving obsolete stores	5		-	-	
Others	94	76	73	(3)	(4)
Interstate Gas Systems Pvt. Ltd. (ISGSL)	97		37	37	
Expenditure relating to LNG	50	53	18	(35)	(66)
Total T&D expenditure	1,413	1,458	1,366	(92)	(6)

8.3.26 *The Authority accepts the remaining items of T&D cost at Rs. 1,366 million.*

8.3.27 *In view of the discussion in paras ii to vii above, the Authority determines the operating cost for the said year at Rs. 5,275 million as against Rs. 5,407 million claimed by the petitioner, as follows:*



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

Particulars	Rs. in million	
	Requested by the Petitioner	Determined by the Authority
Salaries, wages, and benefits (HR cost)	4,136	4,154
Material used on consumers' installations	165	165
Repair & maintenance	643	639
Legal & professional charges	63	20
Provision for doubtful debts	249	146
Loss due to sabotage activities	69	69
Remaining Items of T & D Cost	1,366	1,366
Sub-total expenses	6,690	6,558
Less: Recoveries / Allocations	1,283	1,283
Net T&D exp. before gas internally consumed	5,407	5,275
Add: Gas internally consumed	141	141
Total T&D Expenditure	5,617	5,485

8.4 Reclaimed Items

8.4.1 The petitioner has reduced its revenue requirement for the said year by Rs. 3 million pertaining to the adjustments for FY 2006-07 & FY 2007-08, as detailed below:



Table 21: Details of Reclaimed Items per the Petition

Particulars	Year of Expenditure	Rupees in million	
		The Petition	
(A) IT RELATED EXPENDITURE			
(i) Revenue Expenses			
- IT related training expenditure	2006-07	10	
- IT Repair Software & Hardware Maintenance	2006-07	12	
- Software Development and Maintenance	2006-07	16	
- Software Maintenance	2007-08	4	
Sub-Total			41
(ii) Depreciation on IT related assets			
	2006-07	21	
	2007-08	31	
Sub-Total			52
(iii) Return on IT related assets			
- For FY 2006-07	2006-07	4	
- For FY 2007-08	2006-07	5	
- For FY 2007-08	2007-08	2	
Sub-Total			11
TOTAL (A)			104
(B) Adjustment related to FY 2007-08			
(i) Impact of adjustments by auditors on Final Revenue Requirement For FY 2007-08 (excluding WPPF)			
WPPF impact on adjustments by auditors		(51)	
Sub-Total			(56)
(ii) Adjustments in DFRR FY 2007-08			
Sub-Total			(142)
TOTAL (B)			(198)
(C) Liquidated Damages (from FY 2004-05 to FY 2007-08)			
			92
NET RE-CLAIMED ITEMS FOR TARIFF CALCULATION (A+B+C)			(3)

8.4.2 The petitioner has claimed revenue expenditure of Rs. 38 million pertaining to IT related assets, which was disallowed by the Authority in its determination of FRR for FY 2006-07 dated September 14, 2007 subject to the provision of specific information in respect of IT.

8.4.3 The petitioner has also claimed Rs. 4 million pertaining to software maintenance charges of GIS & ERP, which was disallowed by the Authority in its determination of FRR for FY 2007-08 dated September 23, 2008 on the premise that overall IT project is currently under Authority's comprehensive review and decision on the same will be



issued separately.

- 8.4.4 The petitioner has asserted that it has already provided the requisite information. However, no separate decision has yet been issued by the Authority for IT related expenditure. The petitioner has, therefore, included Rs. 41 million pertaining to IT as reclaimed items for the year.
- 8.4.5 The Authority observes that the petitioner has claimed Rs. 3 million under “IT repair software & hardware maintenance” & “software maintenance charges” pertaining to GIS.
- 8.4.6 The Authority, per the discussion in para 6.2.3 above, excludes Rs. 3 million from computation of Revenue Requirement for the said year.
- 8.4.7 The petitioner has also claimed depreciation and return amounting to Rs. 63 million on its assets per the discussion in para 6.1.5 above.
- 8.4.8 The Authority, per the discussion and decision in paras 6.1.9 & 6.1.10 above, disallows Rs. 20 million in respect of depreciation and return on assets for FY 2006-07 & FY 2007-08 from computation of Revenue Requirement for the said year.
- 8.4.9 The petitioner has informed that its statutory auditors had reported differences amounting Rs. 56 million in the general & subsidiary ledgers, affecting the company’s financial statements for FY 2007-08. The petitioner has, therefore, claimed reduction of Rs. 56 million on this account from the revenue requirement for the said year.
- 8.4.10 The petitioner has also incorporated the reduction of Rs. 142 million as reclaimed items owing to the adjustments in GIC, sale of gas condensate & WPPF for FY 2007-08 on the basis of audited accounts.
- 8.4.11 The petitioner has claimed Rs. 92 million on account of liquidated damages recovered for FY 2004-05 to FY 2007-08 per the discussion in paras 7.3.35 to 7.3.37 above.
- 8.4.12 *The Authority has discussed the issue relating to liquidated damages recovered in paras 7.3.38 to 7.3.40 above and therefore includes 50% of claimed (i.e. the Rs. 46 million) as re-claimed items for the said year.*
- 8.4.13 *In view of above, the Authority reduces the revenue requirement for the said*



year by Rs. 71 million on account of reclaimed items.

8.5 Financial Charges on Short Determination

- 8.5.1 The petitioner has included Rs. 484 million being financial charges on short determination by the Authority, out of which Rs. 236 million pertain to short determination on account of cost of gas for the said year.
- 8.5.2 The petitioner has submitted that cost of gas has increased sharply owing to the higher wellhead prices and exchange losses. However, the Authority, in its decision dated November 20, 2008, determined the cost of gas on lower side in anticipation of US\$ v/s rupee parity at Rs. 75 for the period from January, 2009 to June, 2009. Oil prices were estimated at US\$ 99.08 per barrel and US\$ 529.31 per M.ton for Crude Oil and HSFO respectively whereas actual prices for the period from June to November 2008 averaged at US\$ 106.51 per barrel and US\$ 546.36 per M.ton for Crude Oil and HSFO respectively. Actual exchange rate as on December 31, 2008 was Rs. 78.90 (applicable to notifications effective January, 2009).
- 8.5.3 The petitioner has asserted that it was compelled to borrow additional funds on a very high cost to pay the gas bills of E&P Companies and meet other operating expenses due to the short determination by the Authority, thus increasing the financial charges and affecting its profitability.
- 8.5.4 The petitioner has requested the Authority to take a sympathetic view to compensate it, as its profitability has been severely affected due to increased financial charges in the wake of liquidity crunch. Also, this impact will continue in FY 2009-10, which also needs to be considered.
- 8.5.5 The petitioner has, therefore, claimed Rs. 484 million on account of financial charges as part of revenue requirement for the said year.
- 8.5.6 The Authority observes that it had already allowed "Prior year cost of gas adjustment" of Rs. 4.57 / MMBTU as part of WACOG, while determining ERR of SSGCL for FY 2009-10 vide its decision dated May 15, 2009. The said adjustment was allowed to meet the shortfall arising from exchange rate variations as well as fluctuation in international prices of crude oil & furnace oil.



8.5.7 The Authority also clarifies that financial charges do not form part of revenue requirement of the petitioner in the prevailing tariff regime, and hence, not permissible.

8.5.8 *In view of above, the Authority disallows Rs. 484 million being financial charges for the said year.*

8.6 **Other Charges including Workers Profit Participation Funds (W.P.P.F)**

8.6.1 The petitioner has claimed Rs. 2,636 million including Rs. 331 million on account of W.P.P.F for the said year.

8.6.2 The petitioner has claimed Rs. 2,003 million on account of "Exchange loss on payment of gas purchases" under the head of "Other Charges". The petitioner has explained that volatile fluctuation in the currency market has resulted in exchange losses in respect of payment of gas purchased.

8.6.3 *Consequent upon the deduction / adjustments in the various components of revenue requirement as discussed above, W.P.P.F. is reduced by Rs. 270 million for the said year.*

8.6.4 *In view of the above discussion, the Authority's determines other charges including W.P.P.F at Rs. 2,366 million, for the said year.*

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 detailed reasons recorded in earlier paras, the Authority recapitulates and decides to:

9.1.1 **accept the opening balance of deferred credit at Rs. 3,820 million;**

9.1.2 **determine addition in fixed assets at Rs. 7,606 million and depreciation charge at Rs. 2,657 million;**

9.1.3 **determine the balance of average net operating fixed assets (net of deferred credits & LPG Air mix) at Rs. 29,161 million as against Rs 29,130 million claimed by the petitioner for the said year. Consequently, the return required by the petitioner on its average net operating fixed assets is determined at Rs. 4,957 million;**



- 9.1.4 determine operating income at Rs. 6,982 million as against Rs. 4,285 million offered by the petitioner;
- 9.1.5 accept the cost of gas at Rs. 102,448 million;
- 9.1.6 determine the UFG cut at Rs. 2,707 million per benchmark;
- 9.1.7 determine the T&D expenses at Rs. 5,275 million as against Rs. 5,407 million claimed by the petitioner;
- 9.1.8 accept the GIC at Rs. 141 million;
- 9.1.9 determine other charges including W.P.F. to Rs. 2,366 million as against Rs. 2,636 million claimed by the petitioner; and
- 9.1.10 reduce the revenue requirement by Rs. 71 million as against Rs. 3 million per the petition on account of re-claimed items;
- 9.2 *In exercise of the powers under Section 8(2) of the Ordinance, the Authority determines the final revenue requirement of the petitioner for the said year at Rs. 115,100 million as against petitioner's claim of Rs. 118,317 million, as tabulated below:*

Table 22: Components of FRR for the Said Year as Determined by the Authority

			<i>Rs. in million</i>
S.no	Particulars	Claimed by the Petitioner	Determined by the Authority
1	Cost of gas	102,448	102,448
2	Adjustment of UFG per target	(451)	(2,707)
3	Transmission & distribution cost	5,407	5,275
4	Reclaimed items	(3)	(71)
5	Financial charges on short determination by OGRA	484	-
6	Gas internally consumed	141	141
7	Depreciation	2,668	2,657
8	Other charges including WPPF	2,636	2,366
9	Return on average net operating fixed assets	4,952	4,957
10	Additional revenue requirement for Air-Mix LPG Project	35	35
Total estimated revenue requirement		118,317	115,100

- 9.3 *The petitioner's actual net operating income is Rs. 109,926 million and thus there is a shortfall of Rs. 5,174 million, vis-à-vis its revenue requirement of Rs. 115,100*



million for the said year. The Authority decides to recoup this shortfall to the extent of Rs. 1,289 million through increase in average prescribed price by Rs. 3.62 per MMBTU. However, the remaining shortfall of Rs. 3,885 million will be adjusted in RERR FY 2009-10. Revised prescribed prices for each category of retail consumers for FY 2008-09 are attached and marked Annexure-C.

(Mir Kamal Marri)
Member (Finance)

(Tauqir Sadiq)
Chairman

Islamabad,
September 15, 2009

A. Final Revenue Requirement for FY 2008-09

			<i>Rs. in Million</i>
Particulars	The Petition	Adjustment	Determined by OGRA
Gas sales volume -MMCF	384,983		384,983
BBTU	356,442		356,442
"A" Net Operating Revenues			
Gross sales net of general sales tax	104,247		104,247
Less: Gas development surcharge- existing	1,303		1,303
Net sales at current prescribed price	102,944		102,944
Meter rentals	552		552
Late payment surcharge	-	576	576
Amortization of deferred credit	298		298
Sale of gas condensate	197	307	504
Meter manufacturing profit	-	39	39
Gas transportation charges	18		18
Revenue from JJVL	2,942	-	2,942
Royalty income from JJVL	-	1,657	1,657
Other operating income	278	(119)	397
Total Operating Revenue "A "	107,229	2,460	109,926
"B" Less: Operating Expenses			
Cost of gas	102,448		102,448
UFG Adjustment	(451)	(2,256)	(2,707)
Transmission and distribution cost	5,407	(132)	5,275
Gas internally consumed	141	-	141
Depreciation	2,668	(11)	2,657
Other charges including (W.P.P.F)	2,636	(270)	2,366
Reclaimed items	(3)	(69)	(71)
Financial charges on short determination	484	(484)	-
Total Operating Expenses "B"	113,330		110,108
"C" Operating profit / (Loss) (A-B)	(6,101)	(3,222)	(182)
Return required on net operating fixed assets:			
Net operating fixed assets at beginning	31,290	(26)	31,264
Net operating fixed assets at ending	35,906	(22)	35,884
	67,196		67,148
Average net assets (I)	33,598		33,574
LPG air mix project asset at beginning	80	-	80
LPG air mix project asset at ending	80	-	80
	160		160
Average net LPG air mix project assets (II)	80		80
Meter manu. Plant at beginning	58	(58)	-
Meter manu. Plant asset at ending	51	(51)	-
	108		-
Average net meter manu. Plant (III)	54		-
Deferred credit at beginning	3,820	-	3,820
Deferred credit at ending	4,847	-	4,847
	8,666		8,666
Average net deferred credit (IV)	4,333	-	4,333
"D" Average (I-II-III-IV)	29,130	30	29,161
"E" 17% return required	4,952	5	4,957
"F" Shortfall in return required (C-E) (Gas Operation)	11,054	(5,914)	5,139
"G" Additional revenue requirement for Air-Mix LPG Project	35	-	35
Total Shortfall (F+G)	11,088	(5,914)	5,174
(Decrease) / Increase required in average prescribed price effective July 01, 2008 (Rs. / MMBTU)	31.11	(16.59)	14.52
Increase allowed in average prescribed price effective July 01, 2008 to the extent of shortfall of Rs. 1,289 million (Rs. /MMBTU)			3.62
Remaining shortfall to be adjusted in FY 2009-10			3,885

B. Prescribed Prices per REER for FY 2008-09

						W.E.F 01.07.2008	W.E.F 01.01.2009	
CATEGORY							Rs. per MMBTU	
(i)	Domestic Consumers							
	<i>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, universities, colleges, schools, private educational institutions, orphanages and other charitable institutions.</i>							
	First slab (upto 50 cubic metres per month).						78.38	82.30
	Second slab (over 50 upto 100 cubic metres per month)						82.07	86.17
	Third slab (over 100 upto 200 cubic metres per month)						149.40	156.87
	Fourth slab (over 200 upto 300 cubic metres per month)						313.10	332.12
	Fifth Slab (over 300 upto 400 cubic metres per month)						407.31	432.06
	Sixth Slab (over 400 upto 500 cubic meters per month)						529.50	561.67
	Seventh Slab (all over 500 cubic meters per month)						688.35	730.17
	<i>For hostels and residential colonies to whom gas is supplied through bulk meters.</i>							
	All off-takes at flat rate of						149.40	156.87
(ii)	Commercial Consumers							
	<i>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, places of entertainment like cinemas, clubs and theaters, private offices, clinics, maternity homes, etc.</i>							
	All off-takes at flat rate of						362.94	393.33
(iii)	Special Commercial Consumers (Roti Tandoors)							
	First slab (upto 50 cubic metres per month).						78.38	82.30
	Second slab (over 50 upto 100 cubic metres per month)						82.07	86.17
	Third slab (over 100 upto 200 cubic metres per month)						149.40	156.87
	Fourth slab (over 200 upto 300 cubic metres per month)						313.10	332.12
	Over 300 cubic metres per month						362.94	393.33
(iv)	Ice Factories							
	All off-takes at flat rate of						362.94	393.33

(v)	Industrial Consumers				
	<i>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.</i>				
	<i>All off-takes at flat rate of</i>			322.55	339.43
(vi)	Captive Power				
	<i>All off-takes at flat rate of</i>			322.55	339.43
(vii)	Compressed Natural Gas (CNG) Stations				
	<i>All off-takes at flat rate of</i>			373.45	406.00
viii)	Cement Factories				
	<i>All off-takes at flat rate of</i>			428.89	454.95
(ix)	Pakistan Steel				
	<i>All off-takes at flat rate of</i>			322.55	339.43
(x)	Fauji Fertilizer Bin Qasim Ltd.				
	(i) <i>For gas used as feed-stock for Fertilizer upto 60MMCFD</i>			36.77	102.01
	(ii) <i>Additional allocation (10 MMCFD) Provisional</i>			47.68	54.54
	(iii) <i>For gas used as fuel for generating steam and electricity and for usage in housing colonies for fertilizer factories.</i>			322.55	339.43
(xi)	Power Stations				
	<i>All off-takes at flat rate of</i>			322.55	349.56
(xii)	Independent Power Stations				
	<i>All off-takes at flat rate of</i>			251.55	273.48

C. Prescribed Prices Determined by the Authority for FY 2008-09

		W.E.F 01.07.2008	W.E.F 01.01.2009
		Rs. per MMBTU	
CATEGORY			
(i)	<u>Domestic Consumers</u>		
	<i>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, universities, colleges, schools, private educational institutions, orphanages and other charitable institutions.</i>		
	<i>First slab (upto 50 cubic metres per month).</i>	78.38	82.30
	<i>Second slab (over 50 upto 100 cubic metres per month)</i>	82.07	86.17
	<i>Third slab (over 100 upto 200 cubic metres per month)</i>	149.40	156.87
	<i>Fourth slab (over 200 upto 300 cubic metres per month)</i>	313.10	332.12
	<i>Fifth Slab (over 300 upto 400 cubic metres per month)</i>	407.31	432.06
	<i>Sixth Slab (over 400 upto 500 cubic meters per month)</i>	529.50	561.67
	<i>Seventh Slab (all over 500 cubic meters per month)</i>	688.35	730.17
	<i>For hostels and residential colonies to whom gas is supplied through bulk meters.</i>		
	<i>All off-takes at flat rate of</i>	149.40	156.87
(ii)	<u>Commercial Consumers</u>		
	<i>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, places of entertainment like cinemas, clubs and theaters, private offices, clinics, maternity homes, etc.</i>		
	<i>All off-takes at flat rate of</i>	370.80	393.33
(iii)	<u>Special Commercial Consumers (Roti Tandoors)</u>		
	<i>First slab (upto 50 cubic metres per month).</i>	78.38	82.30
	<i>Second slab (over 50 upto 100 cubic metres per month)</i>	82.07	86.17
	<i>Third slab (over 100 upto 200 cubic metres per month)</i>	149.40	156.87
	<i>Fourth slab (over 200 upto 300 cubic metres per month)</i>	313.10	332.12
	<i>Over 300 cubic metres per month</i>	370.80	393.33
(iv)	<u>Ice Factories</u>		
	<i>All off-takes at flat rate of</i>	370.80	393.33

(v)	<u>Industrial Consumers</u>				
	<i>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.</i>				
	<i>All off-takes at flat rate of</i>			329.54	339.43
(vi)	<u>Captive Power</u>				
	<i>All off-takes at flat rate of</i>			329.54	339.43
(vii)	<u>Compressed Natural Gas (CNG) Stations</u>				
	<i>All off-takes at flat rate of</i>			388.32	427.15
(viii)	<u>Cement Factories</u>				
	<i>All off-takes at flat rate of</i>			428.89	454.95
(ix)	<u>Pakistan Steel</u>				
	<i>All off-takes at flat rate of</i>			329.54	339.43
(x)	<u>Fauji Fertilizer Bin Qasim Ltd.</u>				
	(i) <i>For gas used as feed-stock for Fertilizer upto 60MMCFD</i>			36.77	102.01
	(ii) <i>Additional allocation (10 MMCFD) Provisional</i>			47.68	54.54
	(iii) <i>For gas used as fuel for generating steam and electricity and for usage in housing colonies for fertilizer factories.</i>			329.54	339.43
(xi)	<u>Power Stations</u>				
	<i>All off-takes at flat rate of</i>			329.54	349.56
(xii)	<u>Independent Power Stations</u>				
	<i>All off-takes at flat rate of</i>			251.55	295.03

D. HR Benchmark Cost Determined by the Authority

Description	Base year FY 2007-08	Rs. in Million	
		FY 2008-09	
		The Petition	Determined by OGRA
Total HR cost incl. IAS-19 & TA's Cost	3,480	4,150	
Less:			
IAS-19		171	
TAs Cost	427	475	
HR cost (actual / projected by the licensee)	3,053	3,504	
BASIS OF BENCHMARK			
No. of consumers (actual / projected by the licensee)	2,072,086	2,155,000	2,155,000
Sale Volume (MMCF) (")	377,265	384,983	384,983
T & D network (km) (")	35,193	37,575	37,575
Consumer Price Index (CPI) (")	12.00%	20.77%	20.77%
Per unit cost factor (Sale volume base) (Rs.) (Base Year)	8.09	7.68	8.09
Per unit cost factor (T & D Network) (Rs.) (Base Year)	86.75	90.33	86.75
Per unit cost factor (consumer base) (Rs.) (Base Year)	1,473	1,450	1,473
Based on number of consumers (50% weightage)	1,832	1,874	1,905
Based on sale volume (20% weightage)	611	591	623
Based on T & D network (20% weightage)	611	679	652
CPI adjustment @ 50% of previous year's benchmark HR cost	-	332	332
Benchmark HR Cost	3,053	3,476	3,512
Add: IAS -19 Provision and TAs cost	427	646	646
Total benchmark H.R. Cost	3,480	4,122	4,158
Saving/ (Excess)		(14)	4
H.R. Cost allowed		4,136	4,154