

EVENT REPORT

THE REFORM OF DISTRIBUTION COMPANIES (DISCOS) IN PAKISTAN'S ENERGY SECTOR

3RD SEPTEMBER, 2024



The energy crisis in Pakistan has had a profound impact on the nation's economy, particularly for those living in rural areas, as emphasized by **Dr. Nafisa Shah**. Energy shortages and unaffordable electricity have hindered economic growth, leading to business closures, job losses, and capital flight. Dr. Shah highlighted how the country has struggled under the weight of structural adjustments imposed by the IMF, including devaluations, high interest rates, and stagnating growth, which have pushed poverty levels to nearly 40%, according to the World Bank. She also pointed out the ballooning national debt, with interest payments consuming 70% of tax revenue, and discussed the burden of capacity payments amounting to 2.5 trillion PKR for unused energy. Despite having surplus energy capacity, both consumers and the government are unable to afford it.

Dr. Shah attributed the worsening situation to poor policy decisions and political infighting, which have exacerbated the twin crises of energy and economy. She noted that the failure of the parliament to effectively oversee government actions and hold it accountable has contributed to this crisis. Dr. Shah called for urgent reforms and stressed the importance of public participation, expert consultations, parliamentary debates, and cross-party engagement to address national issues. In particular, she advocated for simplifying complex energy policies to make them more accessible and for a shift towards renewable energy to tackle climate change. Dr. Shah concluded by raising the critical question of whether privatization is the only solution for electricity distribution reforms or if there are viable alternatives that could better address the country's energy challenges.

Hon. Speaker Mr. Ayaz Sadiq

praised the forum, highlighting its relevance amid concerns over electricity tariffs. He noted that Pakistan's parliament became "green" in 2015, the only one globally to do so. While mentioning the electricity prices, Mr. Sadiq called it a global issue, which is well managed by other countries. Mr. Sadiq discussed the challenges of attracting investment when

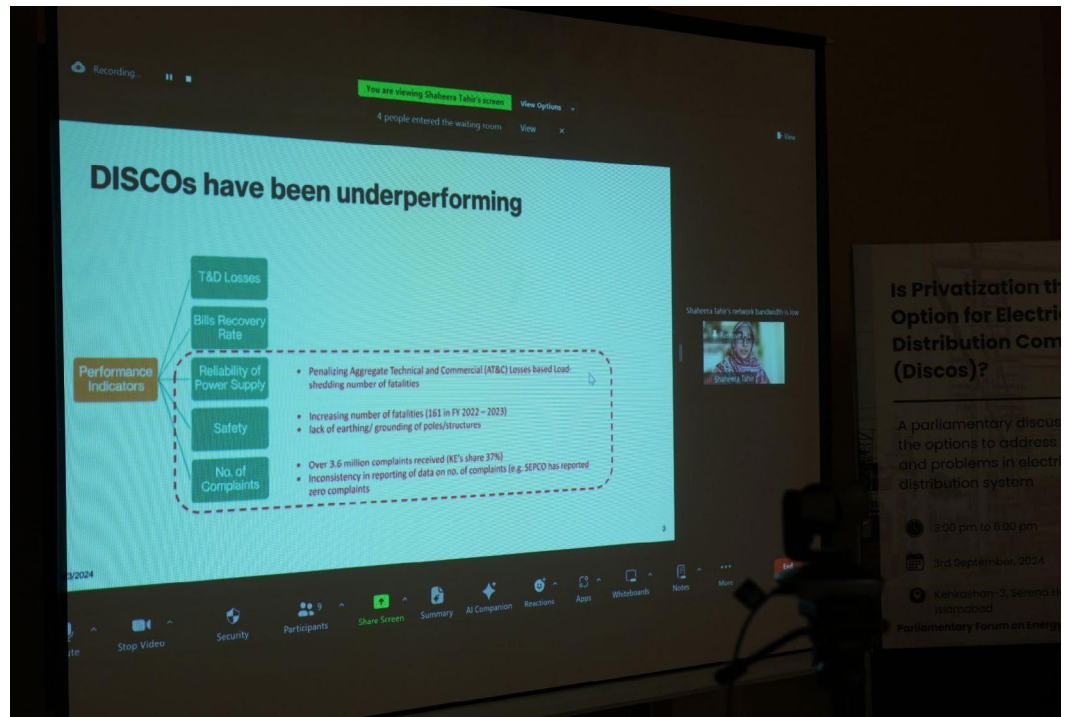


IPP contracts were signed and stressed that the government's role should be that of a regulator and, not a business operator. The lack of implementation and poor performance by NTDC led to delays in T&D infrastructure development while the delay in setting up a grid station in KP, despite available funds, was specifically mentioned. Sadiq also noted that well-performing DISCOs are bearing the burden of underperforming ones, and rooftop solar installations are reducing regular bill payments. Mr. Sadiq emphasized the role of specialized researchers supporting parliamentarians and the need for improved facilitation within the National Assembly. He also mentioned conducting interviews with 1,000 employees to ensure the right person for each role. Key follow-up points included addressing seasonal delta challenges, underutilization, and exploring consumer incentives. Mr. Sadiq called for an analysis of fuel costs, acknowledging that factors like the Ukraine-Russia conflict have driven up fuel prices, compounding existing issues.

1. The rationale and the urgency to reform/restructure DISCOs:

Ms. Shaheera Tahir, a researcher at Policy Research Institute for Equitable Development (PRIED), discussed the issue with DISCOs, why they are of concern and what action points are therefore required. She discussed the stats showing the underperformance of the respective DISCOs. She mentioned that transmission and distribution losses have translated into pkr 166 billion for FY 2022-23 and the breach of recovery targets by DISCOs has translated into financial loss of PKR 236 billion in the same year. And when DFIs extend their financing to cater to these challenges, they mandate structural challenges in the power sector and pass on the true cost of electricity to the end con-

sumers. She discussed the proposed solutions as the like of privatization done in KE, provincialization, management privatization, Dividing large DISCOs into small and some other alternatives. She further emphasized on some immediate steps to curb power theft, improve bill recoveries through introduction of Advanced metering infrastructure, and disconnecting non paying consumers with the use of smart meters. In addition to this, she proposed investments to strengthen the overall system and improve the distribution infrastructure.



2. Is Privatization the only or the most suitable option for reforming DISCOs:

Mr. Tahir Basharat Cheema, former head of Pakistan Electric Power Company (PEPCO), emphasizes that privatization is not the only or most suitable option for reforming DISCOs. Instead, he suggests that allowing financially strong parties with expert management teams to take over through long-term management concessions could be a better approach. This method would enable the assets to remain with Pakistani citizens. Cheema notes that the current privatization model, based on examples from South America and the Philippines, has not been successful. Cheema identified five externalities affecting DISCOs: unprofessional management, affordability concerns, uneven investment, human development index mapping, and flawed government policies. He then discussed different models for reform, including provincialization, long-term management concessions, public-private partnerships, and outright privatization.

Ultimately, Mr. Cheema concluded that long-term management concessions are the best possible option for reforming DISCOs, as this approach allows assets to remain with Pakistani citizens.

Session I : Addressing the question

A session moderated by Ms. Shezra Mansab discussed the reform of Distribution Companies (DISCOs) in Pakistan. The session highlighted the challenges faced by DISCOs, including transmission and distribution losses, unpaid bills, and inefficient supply. The following questions were posed by multi stakeholders attending the event namely, **Mr. Zaheer Bhumro, Ms. Mehtab Rashdi, Ms. Ahmed Kundi, and Mr. Basharat Hassan.** There were further addressed by Ms. Shaheera Tahir and Mr Tahir Cheema.

Questions

1. When did transmission and distribution losses start in the DISCOs? Were these losses present from the very beginning, or did they develop over time, and what were the reasons?
2. The speaker commented that nothing will change, and we'll continue with the same debate. Now that we've reached a point where we want to get rid of IPPs, should we keep them or not? Also, what should be done about the lack of recoveries by DISCOs, and why do we never address the root cause of these issues?
3. If we privatize DISCOs, won't they turn into monopolistic entities like K-Electric? How will we manage that?
4. K-Electric is inaccessible to the public, and it receives subsidies for losses. What are the receivables owed by industries, and are they still running? What is your view on community-based electricity systems?
5. Provincialization vs Privatization: If a province generates cheaper electricity but buys it at expensive rates from the central government, what is your understanding of this situation?

Q1. Transmission and Distribution Losses in DISCOs:

Transmission and distribution losses have been a persistent issue since the formation of DISCOs. These losses have their roots in inefficiencies in power generation and the affordability of electricity, as well as the varying levels of infrastructure investment by different DISCOs. Financial implications of these losses have been reflected in balance sheets over time, highlighting accumulated losses due to historical inefficiencies.

Q2. The Debate on IPPs and DISCOs:

Privatizations have controversies around it that national assets are sold at low price or given to relatives. And even after this, the previous privatization has become a business, and revenue based load shedding started and collectively punished those who did not pay bills ending frontier crimes in places like FATA. K Electric and other DISCOs also adopted these practices, although this is wrong but for the private sector this is a money making business, hence we learn that if the management is right and has no external interventions it'll work fine. So who will do it, bring the financial houses or the banks in and whoever out of them has financial debt and can bring financial investments and the best team.

Q3. Privatization Leading to Monopolies:

Privatization, if not managed properly, could lead to monopolistic entities that exploit consumers, as seen with some existing examples. To prevent this, a strong and independent regulatory framework is necessary. Regulating the sector effectively, with a focus on transparent management practices, can ensure fair competition and prevent the rise of monopolies in the electricity market.

Q4. K-Electric's Monopoly and Community-Based Systems:

The issue of monopolistic practices by utilities like K-Electric has raised concerns, especially with regards to subsidies and outstanding receivables. While there was an initial move towards decentralized, community-based electricity systems, the geographical and seasonal variations in Pakistan necessitate an integrated electricity grid. The current system is considered more effective in managing these challenges, despite the issues with monopolistic practices and high receivables.

Q5. Provincialization vs Privatization:

The challenge of managing DISCOs is significant at the federal level, and it is believed that provincial governments would struggle even more due to the complexities of the electricity sector. The misconception that certain provinces can generate cheap electricity is outdated, as generation costs have risen significantly, especially with the growing role of IPPs. It is suggested that provinces should not bear the responsibility for managing DISCOs, as doing so could exacerbate existing challenges, particularly in terms of financial sustainability and capacity building.

3. Provincialization of DISCOs: Are there lessons to be learnt from India

A presentation by Ms. Rimsha Rehan, a researcher at PRIED, highlighted the potential benefits and challenges of shifting the management of electricity distribution companies (DISCOs) in Pakistan from federal to provincial control. The rationale for provincialization includes addressing the inefficiencies, high losses, and power theft associated with federal management. Provincial governments, being closer to the consumers and having control over local enforcement tools like the police, are argued to be better positioned to manage DISCOs effectively. This shift could lead to improved bill recovery, higher efficiency, and potentially lower tariffs, providing an electoral incentive for provincial governments.

However, the presentation also highlights significant challenges, such as the financial liabilities and losses that provincial governments might inherit, the risk of increased financial burden, and the necessity of infrastructure development and regulatory frameworks at the provincial level. The presentation draws lessons from India's electricity market, where various ownership models of DISCOMs have been implemented including PPP, Franchise models, suggesting that competitive tariffs and strong regulatory oversight (provincial regulatory bodies) are essential for the success of provincialization. Ultimately, the transition should be managed carefully in a phased manner, ensuring a win-win scenario for all stakeholders involved.

4. Public Private Partnership – The so called Turkish model for electricity distribution:

Another session by Mr. Manzoor Ahmed Alizai discussed the IMF's directives for Pakistan, which include privatizing state-owned enterprises and improving fiscal stability and efficiency. He cautioned that Pakistan must consider its domestic dynamics and interlinked issues, noting that blindly adopting the Turkish model might not be effective.

He emphasized the need for a careful approach in transition considerations to ensure reforms align with Pakistan's specific needs and avoid ill-conceived transitions.

Manzoor explained the key differences between the concessionary regime, which had exclusive service rights and no separation of distribution and sales services, and the non-concessionary regime, which allowed for consumer choice and focused on grid investments and maintenance by distribution companies. He pointed out the higher rate of change in end-user tariffs compared to wholesale tariffs, with a 45.1% increase in end-user tariffs over four years versus a 23.3% increase in wholesale tariffs. He suggested assessing the market readiness for implementing any model.

Session II : The search for answers

The Q&A session, moderated by **Ms. Sharmila Farooqi**, addressed key issues related to the energy sector, specifically focusing on the potential for provincializing Distribution Companies (DISCOs), adapting successful models from other countries, and incorporating technology and consistent reforms. The questions were mainly addressed by Mr. Alizai and Ms. Rehan.

Questions

1. Do you think there is a DISCO that can be provincialized, and does the province have the capacity to manage it?
2. Can Pakistan adapt the Turkish model for distribution system reforms, considering regular upgrades and reforms?
3. Have we considered the role of technology in improving DISCO performance, and how are we addressing structural and systematic issues?
4. Considering the need for preventive measures and sustainability, how much time should be given to provinces for pilot projects to understand their respective situations?

Q1. Provincializing DISCOs: Provincializing DISCOs depends on various factors, including geographical aspects, administrative capabilities, and the type of consumer base. DISCOs with better administrative systems, such as IESCO and LESCO, would be more suitable for provincialization due to their better infrastructure. However, DISCOs like QESCO and PESCO, which suffer from higher losses, would face more challenges in implementing such a model. These DISCOs require significant improvement before they can be considered for provincial management.

Q2. Adapting the Turkish Model: Pakistan can learn from Turkey's approach, which involved consistent reforms over time, unlike the delayed and fragmented reforms in Pakistan. Turkey's shift to a non-concessionary model, supported by sovereign guarantees for investor security, has proven successful. For Pakistan, a similar model could work, but it is essential for provinces to have autonomy to choose and implement models suited to their unique needs and circumstances.

Q3. Role of Technology in DISCOs: Technology, particularly smart metering, is an important factor in improving DISCO performance. The introduction of modern technologies should accompany privatization or reforms like the CTBCM. NEPRA has already issued directives considering technological advancements. Therefore, the technological aspect should be integrated into any reforms or privatization initiatives to improve operational efficiency.

Q4. Time for Provincial Pilot Projects: There is no fixed time period for pilot projects; instead, continuous monitoring and evaluation are essential. A regulator, whether central or provincial, should oversee the implementation of reforms with regular assessments, such as quarterly evaluations, to ensure progress. A phased strategy should be adopted, with selected provinces serving as test cases to evaluate the effectiveness of the chosen model.

Additional Insights: Incorporating capacity-building exercises is critical before provincializing any sector. Without sufficient preparation, the lack of infrastructure and technology readiness could result in poor outcomes, as seen with environmental management under provincial jurisdiction after the 18th Amendment. Proper training and capacity building are essential to ensure the successful implementation of advanced technologies in provincialized sectors.

Session III : Critical analysis

The Q&A session, moderated by **Mr. Daniyal Chaudhry**, brought together a panel of current and former technical experts and policy-makers to address critical issues surrounding Pakistan's energy sector and have their opinion on market liberalization and Privatization. The key speakers of the session included **Mr. Tauseef Farooqi, Imtiaz Baloch, Gul Hassan, Osama Mela, Mr.Irfan Yusuf, and Mr. Asad Alam Niazi.**



Questions

1. What are your views on the role of NEPRA and its oversight in the energy sector, especially concerning privatization and public safety?
2. How can the government improve the privatization process for DISCOs, and what should be the key considerations for a seamless transition?
3. What is your opinion on the proposed idea of wheeling for DISCOs and its viability in Pakistan's energy sector?
4. How can DISCOs enhance their collection efficiency and better manage power purchase costs?
5. What are your thoughts on provincialization versus privatization, and how can we manage the division of assets like major dams between provinces?
6. Do you think privatization should be extended to all DISCOs, or are there alternative approaches such as listing them on the stock exchange or introducing automation?
7. How do you see the role of good governance, climate resilience, and long-term planning in addressing the challenges of the power sector?

Q1. NEPRA and Regulatory Oversight: Concerns were raised about the negligence of NEPRA, specifically regarding safety incidents, and the need for stronger regulatory authority. It was emphasized that privatized entities must be held accountable and that regulatory oversight should drive quicker decision-making.

Q2. Privatization Process: There was agreement on the importance of consistent, transparent policies for privatization. A smooth, transparent transition was considered key, with privatization needing to be done systematically and consistently.



Q.3. Wheeling for DISCOs: Skepticism was expressed about the viability of wheeling as a solution for DISCOs, suggesting that it may not be suitable for Pakistan’s energy context.

Q.4. Collection Efficiency: Focus was placed on improving retail operations and collection efficiency. The suggestion was made to shift towards competition and liberalization in the sector, alongside a stronger emphasis on collection strategies.

Q.5. Provincialization vs. Privatization: There were concerns about the feasibility of provincialization, particularly with regard to managing assets like major dams. The idea of listing DISCOs on the stock exchange to attract private investment was suggested as an alternative.

Q.6. Privatization and Automation: The importance of a phased approach to privatization was stressed, with a focus on ending political influence. Automation and a well-functioning system operator were identified as key to directing investments correctly, with privatization seen as a last resort.

Q.7. Long-term Planning and Climate Resilience: The need for long-term planning and climate resilience was emphasized, along with the importance of learning from international models. It was noted that governance reforms, particularly in the context of climate financing, are essential for addressing power sector challenges.

The discussions highlighted the critical need for a strategic approach to addressing Pakistan’s energy crisis. Dr. Amjad Ali Khan emphasized the importance of solution-based discussions, cautioning against the flawed history of privatization and advocating for a combined model of provincialization and public-private partnerships. His call for strong regulatory frameworks and consistent, sustainable implementation reflects the need for thoughtful, long-term solutions.



Hon. Mr. Naveed Qamar concluded the session by emphasizing the need to move beyond blame games in parliamentary debates and focus on actionable solutions. He highlighted that while privatization is necessary across all three sectors, the key lies in integrating technology with effective management. He proposed that provinces could better manage the DISCOs, with an emphasis on prioritizing loss-making entities. Drawing from the successful deregulation of the telecommunications sector, he recommended adopting a prepaid electricity model to improve recoveries. Furthermore, he stressed that ownership is secondary to management, which must be empowered with autonomy and robust support. By adopting a citizen-first approach, fostering industrial growth, and increasing demand, concerns about electricity costs could be alleviated. He concluded by stressing the importance of strengthening the role of regulators, promoting competition, and ensuring comprehensive management reforms to end the status quo and drive progress in Pakistan’s energy sector.