BEFORE
THE THAR COAL AND ENERGY BOARD

PETITION FOR DETERMINATION OF FINANCIAL CLOSE STAGE TARIFF

PURSUANT TO RULE 4(1) THAR COAL TARIFF DETERMINATION RULES, 2014
READ WITH THE PROVISIONS OF
THAR COAL AND ENERGY BOARD ACT, 2011

ON BEHALF OF

SINDH ENGRO COAL MINING COMPANY LIMITED

IN RELATION TO THE DETERMINATION OF THAR COAL AND ENERGY BOARD IN THE MATTER OF SINDH ENGRO COAL MINING COMPANY TARIFF DATED JUNE 5, 2015

DATED: 2ND OCTOBER, 2015

SINDH ENGRO COAL MINING COMPANY LIMITED

ADDRESS	:	4TH FLOOR, THE HARBOR FRONT BUILDING, BLOCK 4 CLIFTON, KARACHI 75600, PAKISTAN
UAN	:	+92 (21) 111 211 211
PHONE #	:	+92 (21) 3529 7501 – 10
FAX #	:	+92 (21) 3529 6018

Sindh Engro Coal Mining Company Limited

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1. DETAILS OF THE PETITIONER

NAME AND ADDRESS

SINDH ENGRO COAL MINING COMPANY LIMITED

ADDRESS : 4TH FLOOR, THE HARBOR FRONT BUILDING, BLOCK 4
CLIFTON, KARACHI 75600, PAKISTAN

UAN : +92 (21)111 211 211

PHONE # : +92 (21) 3529 7501 – 10

FAX # : +92 (21) 3529 6018

AUTHORIZED REPRESENTATIVE OF SINDH ENGRO COAL MINING -COMPANY LIMITED

- Shamsuddin A. Shaikh
  Chief Executive Officer

2. GROUND FOR REVISION IN TARIFF DETERMINATION FOR FINANCIAL CLOSE STAGE

2.1 Sindh Engro Coal Mining Company ("**SECMC**") is a joint venture between the Government of Sindh, Engro Corporation Limited (including its affiliates) and other private sector companies, established to construct, develop, own and operate a coal mine in District Tharparkar, Sindh, Pakistan.

2.2 SECMC, through its petition ("**Tariff Petition**") dated January 05, 2015, requested the Thar Coal and Energy Board ("**TCEB**") for determination of Reference Contract Stage Tariff for SECMC's Mine of 3.8 Mtpa up to 6.5 Mtpa at Block II Thar Coalfields, District Tharparkar, Sindh, Pakistan ("**Project**"). SECMC also submitted all relevant data/information required by the TCEB to arrive at an informed decision.

2.3 Thereafter, TCEB, pursuant to Rule 10(5) of the Thar Coal Tariff Determination Rules, 2014 ("**Rules**") issued its Determination in the Matter of Reference Contract Stage Tariff for SECMC's Mine of 3.8 Mtpa up to 6.5 Mtpa at Block II Thar Coalfields, District Tharparkar, Sindh, dated June 5, 2015 bearing reference No. TCEB/Registrar/2-1/2014 ("**Tariff Determination**").

2.4 Following the Tariff Determination, pursuant to Rule 10(8) of the Rules and on the grounds given below, SECMC filed a Motion for Leave for Review dated June 30, 2015 (the "**Motion for Leave for Review**"), before TCEB, to highlight certain key points stated in the Tariff Determination that could potentially affect the Project. The TCEB, through its determination addressed most of the points highlighted in the Motion for Leave for Review.

2.5 Following the determination on the above Motion for Leave for Review and based on the recent developments in the Project, , SECMC would like to file the present petition for Financial Close Stage tariff (the "**FC Stage Petition**"), before the TCEB, to identify certain developments in the Project that are likely to have an impact on the coal tariff and as such should be reflected / included in the Tariff Determination. The present FC Stage Petition is being filed pursuant to Rule 4(1) of the Rules read with the Thar Coal and Energy Board Act, 2011. SECMC, therefore, requests the TCEB to kindly reconsider the key points (discussed below).

2.6 The details regarding the adjustments / amendments sought in the Tariff Determination have been elaborated upon in Sections 3 to 7 below and consist of the following heads:

(i) Debt to Equity Ratio;

(ii) Foreign / Local Debt Mix & Sinosure Insurance;

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(iii) Changes in Advance Payment under the EPC Contract;

(iv) Controllable Costs; and

(v) Uncontrollable Costs – Security Costs.

2.7 In addition to the above, the following documents, required to be submitted along with this FC Stage Petition, are also enclosed in the Annexures hereto:

Latest Form A of SECMC certified by the Securities and Exchange Commission of Pakistan (**SECP**)	**Annexure A**
Latest Form 3 of SECMC certified by the SECP	**Annexure B**
Executed copy of the Coal Supply Agreement	**Annexure C**
Executed copy of the Power Purchase Agreement	**Annexure D**
Shareholders Agreement executed between the shareholders of SECMC	**Annexure E**
Document indicating a binding commitment of injection of the required equity	**Annexure F**
Financing and Security Documents executed in respect of the Project	**Annexure G**

2.8 We request that SECMC be allowed to submit additional evidence and further submissions in relation to this FC Stage Petition, if the same are required by the TCEB.

2.9 Further, we would be pleased to provide any further information, clarification or explanation that may be required by the TCEB during the evaluation process.

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3. Debt to Equity Ratio

(Reference paragraph (vi) of General Conditions – on page 34 – of the Tariff Determination)

TCEB has fixed the Debt to Equity Ratio in the Tariff Determination at 80:20 with the provision that SECMC will be allowed a Debt to Equity ratio of 75:25 only if financing requirements necessitate injection of capital beyond USD 700 Million (i.e. the cover provided by the Sovereign Guarantee). The Tariff Determination further states that any capital injection in excess of 25% will be treated as commercial debt to the project at the prevailing rates but not exceeding KIBOR plus 3%.

In our discussions with the TCEB we were informed that the Debt to Equity Ratio stated in the Tariff Determination shall be finalized at the time of financial close of the Project based on the actual terms agreed with the lenders. It is therefore submitted that the SECMC has finalized debt financing arrangements with a consortium of local and foreign lenders at a Debt to Equity Ratio of 75:25. The lenders have already given a concession by withdrawing their earlier requirement for a Debt to Equity Ratio of 70:30; therefore the Debt to Equity Ratio of 75:25 finalized by SECMC for the Project is a major achievement for the Project since the lenders were reluctant to allow the same due to *inter alia* the following reasons:

- Mining is being undertaken in Pakistan for the first time. While the Project is backed by a Sovereign Guarantee, the Project is nevertheless categorized as a '*high risk*' Project. Further, considering the fact that a project of this magnitude is being undertaken for the first time in Pakistan, the lenders want to structure this as a bankable project finance transaction and categorize the Sovereign Guarantee as only a secondary comfort (considering other projects where there was a Sovereign Guarantee and which have still been impacted).

- With a Debt to Equity ratio of 80:20 there would be no room left for seeking additional financing for any cost overruns in respect of the development of Phase – I (3.8 MPTA mining capacity). Arranging working capital loans during Phase – I of 3.8 MTPA will be difficult as banks generally do not allow a total leverage of 4:1, which the Project will achieve if the capital structure is set at 80:20, The lenders generally keep a cushion in case a project needs working capital at a later stage. Therefore, the lenders have permitted a Debt to Equity Ratio of 75:25.

In view of the foregoing, it is requested that the TCEB reconsiders the Debt to Equity ratio allowed in the Tariff Determination and revises the same to 75:25, which is in line with the Debt to Equity ratio agreed with both foreign currency and local currency lenders of the Project.

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4. FOREIGN / LOCAL DEBT MIX & SINOSURE INSURANCE

(Reference paragraph (v) – General Conditions – Page 34 – of the tariff Determination)

A. FOREIGN / LOCAL DEBT MIX:

The tariff determination is based on a 100% Local Debt with a provision for introduction of foreign debt. Under the current financing arrangement, SECMC will be taking approximately USD 200 million of foreign debt and the balance will be financed through local debt for the Project. The interest rate for the foreign debt has been negotiated at LIBOR + 3.3%, which is below the interest rate applicable to local lending (i.e. KIBOR + 1.75%) and would thus have a positive impact on the Coal Tariff even after accounting for the Sinosure premium of 6.42%.

It is important to note that Government of Pakistan has recently concluded a 10 year bond at 8.25% which implies LIBOR spread of 6.25% as 10 year LIBOR benchmark rate on the date of issuance was 2%. Against this we have successfully negotiated a spread of only 3.3% for the same GoP risk and that too for a tenor of 14 years. Even if Sinosure's premium of 6.42% is added on a per annum basis, the spread is only 4.58% per annum as against 6.25% of the GoP Bonds.

In this regard the Tariff Determination also states that any impact of foreign lending on the Coal Tariff will be incorporated in the Coal Tariff at the time of financial close.

The reasons SECMC has opted for a mix of foreign and local lending for the Project include the following:

- Being an early harvest project under the China Pakistan Economic Corridor, SECMC is able to obtain a rate of LIBOR + 3.3%. This rate is lower than the local financing rate of KIBOR + 1.75% that has been approved and thereby will provide a direct benefit to the consumer.

- Given the fact that SECMC's contractor is Chinese and the contracted payments are to be made in USD, foreign lending limits SECMC's exposure to foreign exchange risk. Furthermore, the foreign debt will be utilized to cover offshore payment requirements under the EPC contract thereby ensuring saving of foreign exchange leaving the country. The issue was also raised by the Ministry of Finance while signing Sovereign Guarantee, that they will be mindful of the fact that

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the project should be at least partly covering its foreign exchange component through back to back foreign currency loan.

After several discussions with foreign lenders, a consortium of lenders from China has agreed to fund the Project. Detailed term sheets, including pricing, security and guarantee requirements have been agreed with such foreign lenders. Almost agreed draft of foreign currency loan is also attached for your consideration.

B. SINOSURE INSURANCE:

Since lending by Chinese commercial banks requires Sinosure Insurance coverage, SECMC has had to obtain the same for the Project. In this regard Sinosure has issued a letter of intent and the premium that it has agreed to charge is 6.42% of the total amount of foreign financing (principal + interest).

In view of the foregoing, it is requested that the TCEB reviews the Tariff Determination and allows the Project to have a foreign / local debt mix with a USD 200 million foreign debt and the balance to be local debt and accordingly adjusts the Coal Tariff. It is further requested that the TCEB allows the cost of Sinosure Insurance as part of the Project Costs in the Coal Tariff.

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5. CHANGES IN ADVANCE PAYMENT UNDER THE EPC CONTRACT

(Reference General Conditions of the Tariff Determination)

One of the requirements of Sinosure Insurance is that SECMC makes a payment of at least 15% of the Agreement Price to its Contractor under the Engineering, Procurement and Construction (**EPC**) Contract for the Project. As a consequence of this requirement, SECMC will be making an advance payment of USD 69 million to the EPC Contractor instead of the previous amount of USD 48 million. However, as per the new arrangement with the EPC Contractor, SECMC will adjust this additional amount of USD 21 million against the scheduled payments under the EPC Contract and would make scheduled payments after the amortization of the additional amount plus a financing cost of 0.3%. As such, there would be minimal impact on the project cost as a result of this change.

In view of the foregoing, it is requested that the TCEB allows the additional advance payment to be made to the EPC contractor under the Sinosure requirements and accordingly adjust the coal tariff based on the foregoing.

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6. CONTROLLABLE COSTS

(Reference General Conditions of the Tariff Determination)

In the Tariff Petition submitted by SECMC to the TCEB, the costs were divided into two categories, i.e. controllable costs and uncontrollable costs. The Tariff Determination in some clauses seeks to cap the Non-EPC costs, excluding costs in respect of land acquisition and village relocation. However, if the Non-EPC cost is capped at an aggregate level rather than at individual levels, SECMC may pursue efficiencies in one controllable cost and use them to cover another controllable cost that may be suffering an overrun. Since this is a first of its kind Project being implemented in Pakistan, there may be potential cost overruns. Therefore, having an aggregate cap of the Non-EPC costs would allow SECMC to manage its cash flows without affecting the Project or the Coal Purchaser.

In view of the foregoing, it is kindly requested that the TCEB allows an overall aggregate cap on such controllable Non-EPC costs.

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7. UNCONTROLLABLE COSTS – SECURITY COSTS

(Reference General Conditions of the Tariff Determination)

The Tariff Determination mentions 'security costs' under the Operating Expenses head, which is a part of the Non-EPC Costs. It may be noted that it is very difficult to lock down the security costs for a Project of this scale and nature. As such, due to the difficulty in locking down security costs at this stage of the Project, SECMC proposes that the security costs for the Project, both during the construction and the operations phases, should be categorized as 'Uncontrollable Costs' under the Tariff Determination.

In view of the foregoing, it is kindly requested that the TCEB categorizes and allows security costs of the Project, both during the construction and the operations phases, as 'Uncontrollable Costs'.

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In view of the foregoing, the TCEB is kindly requested to look into the above matters and make appropriate amendments in the Tariff Determination so that the Project can proceed further. It would be appropriate to reflect the same in the Tariff Determination as also provided for in the Rules.

SECMC is grateful to the TCEB for supporting the Project throughout since its inception and would be available to discuss the above matters at its convenience.

FOR AND ON BEHALF OF
SINDH ENGRO COAL MINING COMPANY LIMITED

Ashan

Sindh Engro Coal Mining Company Limited

SHAMSUDDIN A. SHAIKH
CHIEF EXECUTIVE OFFICER