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Kosovo Energy Regulatory Office

Rule on Regulated Generator Pricing
(Generation Pricing Rule)

D R A F T

2011

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CHAPTER 1 GENERAL PROVISIONS

Article 1 Introduction

1 This Rule was adopted by the Board of the Energy Regulatory Office ("the Regulator") at a public session held on [date], under the authority given to it under Article 8 of the Law on the Energy Regulator.

Article 2 Scope and Purposes

1 This Rule sets:

1.1 The basis for the determination of Maximum Allowed Revenues and Energy Costs that may be earned by Regulated Generators in any Relevant Year in order to allow them to recover the reasonable costs of operating, maintaining and investing in their generating and associated facilities for the purposes of supply to the Public Electricity Supplier ("PES") in accordance with the Law on the Energy Regulator; and

1.2 The process by which such Maximum Allowed Revenues and Energy Costs shall be reviewed and periodically re-determined.

Article 3 Definitions and Interpretations

1 The following terms are used in this Rule and have the following meanings:

1.1 "Actual Regulated Revenues" means the revenue recovered by a Regulated Generator through charges for the provision of energy and capacity to the PES and any other revenue items stipulated by the Regulator measured, measured on an accruals basis;

1.2 "Approved Investment Plan" has the meaning given to it in Schedule 2;

1.3 "Availability Target" means the target level of Availability Capacity for the year, adjusted for expected maintenance, forced outages and other causes of unavailability;

1.4 "Available Capacity" means the capacity of the Regulated Generator that is available for supply;

1.5 "Business Days" means all working days of the week as defined in Kosovo law;

1.6 "Capacity Charge" means the charge per unit of available capacity determined in accordance with Chapter 6;

1.7 "Economic Asset Lives" means the asset lives used to calculate allowed depreciation on the Regulatory Asset Base;

1.8 "Energy Charge" means the charge per unit supplied determined in accordance with Chapter 7;

1.9 "Energy Costs" means the allowed costs per unit supplied determined in accordance with Chapter 4;

1.10 "EURIBOR" means the European Banking Federation Interbank Offer Rate for Euro deposits for a period equal to 3 months which appears on the appropriate page of the

Reuters service at or about 11:00 a.m. Central European Time, or in the event that the Reuter's service, or any successor thereto, no longer provides such information, such other service as agreed by the Regulated Generator and the Regulator. For the avoidance of doubt it shall be an annual rate;

1.11 "Extraordinary Adjustment" has the meaning given to it in Schedule 6;

1.12 "Extraordinary Event" has the meaning given to it in Schedule 7;

1.13 "Extraordinary Review" has the meaning given to it in Article 7;

1.14 "Force Majeure Event" has the meaning given to it in Schedule 8;

1.15 "Generator Charges" means the Capacity Charges and Energy Charges applied by a Regulated Generator;

1.16 "Licence Fee" means the amount payable under the terms of Article 7 of the Schedule of Fees issued by the Regulator and amended from time to time;

1.17 "Lignite Supply Costs" means the costs of lignite supply to the Regulated Generator determined in accordance with Chapter 5;

1.18 "Market Rules" means the [to be defined when new market rules are in place];

1.19 "Materiality Threshold" has the meaning given to it in Schedule 6;

1.20 "Maximum Allowed Revenues" or "MAR" means the maximum amount that can be recovered in a Relevant Year by a Regulated Generator through its Energy Charge and its Capacity Charge, the revenues from which are regulated under the formulae in Schedule 1 of this Rule;

1.21 "Metered" means in relation to any electricity metered quantity, as measured by a meter installed for such a purpose under the Metering Code;

1.22 "MW" means megawatts;

1.23 "MWh" means megawatt hours;

1.24 "Net Present Value" means the method of discounting future cash flows;

1.25 "Proposal" has the meaning given to it in Schedule 4 paragraph 4;

1.26 "Provisional Decision" has the meaning given to it in Schedule 4 paragraph 6;

1.27 "Public Electricity Supplier" or "PES" means the holder of the Public Supply Licence;

1.28 "Periodic Review" means the review by the Regulator to determine Maximum Allowed Revenues of a Regulated Generator for the forthcoming Regulatory Period;

1.29 "Regular Adjustment" means the mechanical adjustment to Maximum Allowed Revenues undertaken towards the end of each Relevant Year;

1.30 "Regulated Generator" means a generator obligated under the Law on Electricity to supply the PES at a regulated price where insufficient wholesale competition exists and the PES requires the supply to meet its obligations;

1.31 “Regulator” means the Energy Regulatory Office;

1.32 “Regulatory Asset Base” has the meaning given to it in Schedule 2;

1.33 “Regulatory Period” has the meaning given to it in Article 5 paragraph 3;

1.34 “Relevant Year” means the period of 12 successive calendar months between Regular Adjustments;

1.35 “Statement of Generation Charging Principles” means a statement issued by the Regulator that the Regulated Generator’s Capacity Charges and Energy Charges must be in accordance with;

1.36 “Statement of Financial Impact” has the meaning given to it in Schedule 6;

1.37 “Transitional Period” has the meaning given to it in Schedule 9;

1.38 “Unit supplied” means a kilowatt hour;

1.39 “Units supplied” means the aggregate quantity of electricity units billed to the PES in respect of units supplied to it from a Regulated Generator;

1.40 “Weighted Average Cost of Capital” has the meaning given to it in Schedule 3; and

1.41 “X Factor” means the factor defined at Periodic Reviews and applied at Regular Adjustments to Maximum Allowed Revenues.

2 The other terms in this rule shall have the meanings specified in the Law on the Energy Regulator, in the Law on Electricity, or in the Law on Energy.

CHAPTER 2 REGULATED GENERATOR CHARGES

Article 4 General Principles

1 Annual Generator Charges shall be set such that:

1.1 Within each Relevant Year the revenues that the Regulated Generator expects to earn from Capacity Charges are equal to Maximum Allowed Revenues (Chapter 3) approved by the Regulator;

1.2 Within each Relevant Year the revenues that the Regulated Generator expects to earn from Energy Charges are equal to the Energy Costs (Chapter 4) approved by the Regulator; and

1.3 Generator Charges are determined in accordance with a methodology developed by the Regulated Generator and approved by the Regulator. The methodology shall be in accordance with the Statement of Generation Charging Principles issued by the Regulator.

2 Maximum Allowed Revenues comprise the sum of:

2.1 Allowed fixed generator costs, including allowed fixed operating costs, allowed depreciation, and allowed return on capital and any fixed component of fuel supply costs.

3 Energy Costs comprise the sum of:

3.1 Allowed variable operating costs per unit of energy supplied;

3.2 Allowed variable lignite and other fuel supply costs per unit of energy supplied: and

3.3 The Licence Fee.

4 Maximum Allowed Revenues and Energy Costs shall be determined as follows:

4.1 Maximum Allowed Revenues and Energy Costs shall be set at Periodic Reviews (Article 5):

4.2 Before the end of each Relevant Year, a Regular Adjustment (Article 6) shall be applied which involves mechanical adjustments to Maximum Allowed Revenues and Energy Costs for changes in costs that are considered to be outside of the Regulated Generator’s control; and

4.3 Extraordinary Reviews (Article 7), which involve an adjustment to Maximum Allowed Revenues and/or Energy Costs for material changes in costs and/or revenues caused by an Extraordinary Event, shall be made as necessary.

5 Transitional provisions given in Schedule 9 shall apply until 31 March 2016.

Article 5 Periodic Reviews and Regulatory Periods

1 At Periodic Reviews Maximum Allowed Revenues and Energy Costs of the Regulated Generator for the following Regulatory Period shall be set.

2 A Periodic Review shall be held prior to each Regulatory Period.

3 Each Regulatory Period shall equal 5 years, except:

3.1 During the Transitional Period as given in Schedule 9; and

3.2 On the mutual agreement of the Regulated Generator and the Regulator, a Periodic Period may be shortened or extended.

4 The process for undertaking Periodic Reviews is given in Schedule 4.

Article 6 Regular Adjustments

1 At Regular Adjustments the permitted change in Maximum Allowed Revenues and Energy Costs shall be calculated.

2 A Regular Adjustment shall be held prior to each forthcoming Relevant Year.

3 The change in Maximum Allowed Revenues and Energy Costs at each Regular Adjustment shall be based on the following:

3.1 Under or over-recovery of Maximum Allowed Revenues in the current (soon to be competed) Relevant Year, due to differences between forecast and actual electricity supplied;

3.2 Adjustments to Energy Costs for changes in the costs of fuel supply and the forecast Licence Fee; and

3.3 Under or over-recovery of the allowed cost of Licence Fees, due to differences between forecast and actual costs.

4 The formulae for calculating Maximum Allowed Revenues and Energy Costs at Regular Adjustments are given in Schedule 1.

5 The process for making Regular Adjustments is given in Schedule 5.

Article 7 Extraordinary Reviews

1 Extraordinary Reviews shall be triggered by Extraordinary Events, as defined in Schedule 7.

2 At Extraordinary Reviews the impact of the Extraordinary Event on Maximum Allowed Revenues and/or Energy Costs for the remainder of the current Regulatory Period shall be calculated. If the impact is greater than the Materiality Threshold, then an Extraordinary Adjustment to Maximum Allowed Revenues and/or Energy Costs shall be made.

3 The calculation of the impact on Maximum Allowed Revenues and/or Energy Costs and the associated Extraordinary Adjustment shall not account for any factors that are not directly affected by the Extraordinary Event.

4 For the avoidance of doubt, the Regulator shall also take account of the on-going impacts of Extraordinary Events (that pass the Materiality Threshold) at future Periodic Reviews.

5 The process for undertaking Extraordinary Reviews is given in Schedule 6.

CHAPTER 3 MAXIMUM ALLOWED REVENUES

Article 8 General Principles

1 Maximum Allowed Revenues shall be set at such a level that enables the Regulated Generator to set Capacity Charges at a level that allows recovery of all reasonable non-energy costs of supply to the extent that the costs are justified and prudently asserted.

2 The reasonable non-energy costs of the Regulated Generator shall comprise:

2.1 Allowed generation costs, including allowed fixed operating costs (Article 9), allowed depreciation (Article 10), and allowed return on capital (Article 11). At Regular Adjustments allowed generation costs shall be adjusted for inflation less the X Factor;

2.2 The fixed component of Lignite Supply Costs (Article 12), where applicable.

3 In determining reasonable costs, the Regulator shall refer to, but is not bound by or limited to:

3.1 Past performance;

3.2 Projected performance;

3.3 Comparisons with similar utilities in Kosovo and elsewhere in Europe; and

3.4 Comparisons with the costs of similar activities in Kosovo and elsewhere in Europe.

4 Maximum Allowed Revenues shall exclude revenues from sources other than the supply of electricity to the PES.

5 Maximum Allowed Revenues shall be expressed in terms of Euros (€).

6 At Periodic Reviews the Regulator may adjust the profile of Maximum Allowed Revenues expected to be recovered over each Relevant Year to minimise step changes in Maximum Allowed Revenues.

7 At all times, the Net Present Value of the forecast Maximum Allowed Revenues to be recovered in this way shall equal the Net Present Value of the forecast allowed costs of the Regulated Generator to be recovered from Capacity Charges. The calculation of the Net Present Value shall use the Weighted Average Cost of Capital of the Regulated Generator, as determined by the Regulator, as the applicable discount rate.

8 The formulae for calculating Maximum Allowed Revenues are given in Schedule 1.

Article 9 Allowed Fixed Operating Costs

1 In submitting its estimates of fixed operating costs required to be recovered through Maximum Allowed Revenues for any forthcoming Regulatory Period, the Regulated Generator shall not seek to recover any proportion or element of the corporate costs of any parent entity or any affiliated entity that cannot reasonably be attributed to the Regulated Generator.

Article 10 Allowed Depreciation

1 Allowed depreciation costs shall be calculated on a straight-line basis as a function of Economic Asset Lives and the Regulatory Asset Base for different classes of assets, as described in Schedule 2.

Article 11 Allowed Return on Capital

1 Allowed return on capital costs shall be calculated as a function of the Weighted Average Cost of Capital and the Regulatory Asset Base, as described in Schedule 2.

2 Return on capital shall be calculated based on value of the Regulatory Asset Base at the middle of each Relevant Year (as an average of the opening and closing values of the Regulatory Asset Base).

3 The Regulated Generator shall not earn a return on assets financed using capital grants.

Article 12 Fixed Component of Lignite Supply Costs

1 The fixed component of Lignite Supply Costs shall be calculated in accordance with Chapter 5.

CHAPTER 4 ENERGY COSTS

Article 13 General Principles

1 Energy Costs shall be set at such a level that enables the Regulated Generator to set Energy Charges at a level that allows recovery of all reasonable energy costs of supply to the extent that the costs are justified and prudently asserted.

2 The reasonable energy costs of the Regulated Generator shall comprise:

2.1 Allowed generation costs, including allowed variable operating costs (Article 14). At Regular Adjustments allowed generation costs shall be adjusted for inflation less the X Factor;

2.2 The variable component of Lignite Supply Costs (Article 15),where applicable;

2.3 Other non-lignite fuel supply costs (Article 16); and

2.4 The Licence Fee (Article 17), which shall be fully passed-through at Regular Adjustments, assuming that the Licence Fee is expressed as at present in terms of Euros per unit supplied (€/kWh).

3 In determining reasonable costs, the Regulator shall refer to, but is not bound by or limited to:

3.1 Past performance;

3.2 Projected performance;

3.3 Comparisons with similar utilities in Kosovo and elsewhere in Europe; and

3.4 Comparisons with the costs of similar activities in Kosovo and elsewhere in Europe.

4 Energy Costs shall exclude revenues from sources other than the supply of electricity to the PES.

5 Energy Costs shall be expressed in terms of Euros per unit supplied (€/kWh).

6 The formulae for calculating Energy Costs are given in Schedule 1.

Article 14 Allowed Variable Operating Costs

1 In submitting its estimates of variable operating costs required to be recovered through Maximum Allowed Revenues for any forthcoming Regulatory Period, the Regulated Generator shall not seek to recover any proportion or element of the corporate costs of any parent entity or any affiliated entity that cannot reasonably be attributed to the Regulated Generator.

Article 15 Variable Component of Lignite Supply Costs

1 The variable component of Fuel Supply Costs shall be calculated in accordance with Chapter 5.

Article 16 Other fuel supply costs

1 Fuel supply requirements other than lignite shall be calculated on the basis of specific consumption per unit of energy supplied.

2 The cost of fuel supply other than lignite shall be determined with reference to:

2.1 The actual costs of fuel supplies other than lignite; and

2.2 National, regional and international fuel prices.

3 The costs of fuel supply other than lignite shall be adjusted for changes in fuel prices at each Regular Adjustment, as per the formulae given in Schedule 1.

Article 17 Pass-Through of Licence Fee

1 The Regulated Generator shall pass-through the Licence Fee. Maximum Allowed Revenues shall be adjusted for changes in the Licence Fee at each Regular Adjustment, as per the formulae given in Schedule 1.

CHAPTER 5 LIGNITE SUPPLY COSTS

Article 18 General Principles

1 Lignite Supply Costs allow recovery of the costs of lignite supply to the Regulated Generator.

2 Where a lignite supply agreement is in place, Lignite Supply Costs shall be determined in accordance with the applicable agreement and the split between fixed and variable costs shall be determined following the agreement.

3 Where no fuel supply agreement is in place, Lignite Supply Costs shall be calculated as if the lignite mining business is a stand-alone entity.

4 In this instance, the Lignite Supply Costs shall be determined in the same way as the allowed costs of a Regulated Generator (Chapter 3 and Chapter 4) and the costs shall be allocated between fixed and variable components in the same way.

CHAPTER 6 CAPACITY CHARGES

Article 19 General Principles

1 Capacity Charges shall be set from time to time such that:

1.1 The Capacity Charge recovers the Maximum Allowed Revenues of the Regulated Generator, provided that available generating capacity meets the Availability Target; and

1.2 Capacity Charges are in accordance with a methodology developed by the Regulated Generator and approved by the Regulator. The methodology shall be in accordance with the Statement of Generation Charging Principles issued by the Regulator.

2 Capacity Charges shall be expressed in Euros per unit of available capacity per [hour] (€/kW/[hour]).

3 The Regulator shall define the Availability Target used to calculate Capacity Charges in each year with reference to:

3.1 Past performance;

3.2 Projected performance; and

3.3 Comparisons with similar generators in Kosovo and elsewhere in Europe.

4 The Regulator shall define the procedures for testing of capacity availability as required.

Article 20 Capacity Charges Approval Process

1 The Regulated Generator shall submit to the Regulator its methodology for Capacity Charges and any subsequent amendments to this methodology at least [30 Business Days] prior to its proposed date of effectiveness.

2 No methodology or amendments to a methodology shall be effective until approved by the Regulator.

3 The Regulated Generator shall have the right to determine the Capacity Charges subject to the requirements of Article 19 above and the approval of the Regulator.

4 Parties shall have the rights to refer any dispute over the Capacity Charges applicable to them to the Regulator, as provided for in relevant legislation.

CHAPTER 7 ENERGY CHARGES

Article 21 General Principles

1 Energy Charges shall be set from time to time such that:

1.1 The Energy Charge recovers the Energy Costs of the Regulated Generator; and

1.2 Energy Charges are in accordance with a methodology developed by the Regulated Generator and approved by the Regulator. The methodology shall be in accordance with the Statement of Generation Charging Principles issued by the Regulator.

2 Energy Charges shall be expressed in Euros per unit of energy supplied (€/kWh).

Article 22 Energy Charges Approval Process

1 The Regulated Generator shall submit to the Regulator its methodology for Energy Charges and any subsequent amendments to this methodology at least [30 Business Days] prior to its proposed date of effectiveness.

2 No methodology or amendments to a methodology shall be effective until approved by the Regulator.

3 The Regulated Generator shall have the right to determine the Energy Charges subject to the requirements of Article 21 above and the approval of the Regulator.

4 Parties shall have the rights to refer any dispute over the Energy Charges applicable to them to the Regulator, as provided for in relevant legislation.

SCHEDULE 1 MAXIMUM ALLOWED REVENUES AND ENERGY COSTS CALCULATION

1 This schedule sets out the formulae for calculating Maximum Allowed Revenues and Energy Costs of the Regulated Generator. This schedule is intended to complement the principles set out in the main body of the Rules.

2 Maximum Allowed Revenues *(MAR_t)* shall be calculated using the following formula:

$$MAR_t = NENR_t + KREV_t$$

Where

MAR_t	*is Maximum Allowed Revenues in Relevant Year t*
$NENR_t$	*is allowed non-energy revenues in Relevant Year t, which are set at Periodic Reviews such that, the Net Present Value (over the Regulatory Period and taking account of the X Factor) is expected to equal the Net Present Value of forecast allowed non-energy costs*
$KREV_t$	*is the revenue correction factor in Relevant Year t, which is forecast as zero at Periodic Reviews*

2.1 Allowed non-energy revenues ($NENR_t$) shall be calculated at Regular Adjustments using the following formula:

$$NENR_t = NENR_{t-1} * (1 + CPI_{t-1} - X_t)$$

Where

$NENR_t$	*is allowed non-energy revenues in Relevant Year t*
$NENR_{t-1}$	*is allowed non-energy revenues in Relevant Year t-1 except for Relevant Year 1, when a value determined by the Regulator at the most recent Periodic Review shall be used*
CPI_{t-1}	*is the actual value of inflation in Relevant Year t-1, measured using the Harmonised Indices of Consumer Prices (HICPs) – All Items, for the Eurozone, published by Eurostat*
X_t	*is the X Factor in Relevant Year t, which is set at Periodic Reviews*

2.2 The revenue adjustment factor ($KREV_t$) shall be calculated at Regular Adjustments using the following formula:

$$KREV_t = (MAR_{t-1} - ARR_{t-1}) * (1 + I_t)$$

Where

ARR_{t-1}	*is the Actual Regulated Revenues in Relevant Year t-1*
MAR_{t-1}	*is Maximum Allowed Revenues in Relevant Year t-1*

I_t *is the interest rate for the Relevant Year t calculated based on EURIBOR plus 1%*

3 Energy Costs (ENCt) shall be calculated using the following formula:

$$ENC_t = LIGV_t + FUEL_t + VOM_t + LICC_t$$

Where

ENC_t *is the allowed Energy cost in Relevant Year t (in €/kWh)*

$LIGV_t$ *is the allowed variable component of Lignite Supply Costs in Relevant Year t (in €/kWh where the unit is the units supplied by the Regulated Generator)*

$FUEL_t$ *is allowed other non-lignite fuel supply costs in Relevant Year t (in €/kWh where the unit is the units supplied by the Regulated Generator)*

VOM_t *is allowed variable operating costs in Relevant Year t (in €/kWh)*

$LICC_t$ *is the Licence Fee in Relevant Year t (in €/kWh)*

3.1 The variable component of Lignite Supply Costs ($LIGV_t$) shall be calculated at Regular Adjustments using the following formula:

$$LIGV_t = LIGV_{t-1} * (1 + CPI_{t-1} - Y_t)$$

Where

$LIGV_t$ *is the allowed variable component of Lignite Supply Costs in Relevant Year t*

$LIGV_{t-1}$ *is the allowed variable component of Lignite Supply Costs in Relevant Year t-1 except for Relevant Year 1, when a value determined by the Regulator at the most recent Periodic Review shall be used*

CPI_{t-1} *is the actual value of inflation in Relevant Year t-1, measured using the Harmonised Indices of Consumer Prices (HICPs) – All Items, for the Eurozone, published by Eurostat*

Y_t *is the expected annual efficiency improvement in the variable costs of the lignite mining business, as determined by the Regulator at the most recent Periodic Review (expressed in %)*

3.2 The non-lignite fuel costs (FUELt) shall be calculated at Regular Adjustments using the following formula:

$$FUEL_t = \sum FUEL_{j,t}$$

$$FUEL_{j,t} = FUPR_{j,t} * FUCO_j$$

$$FUPR_{j,t} = FUPR_{j,t-1} * (1 + FPI_{j,t})$$

Where

$FUEL_t$ *is allowed other non-lignite fuel supply costs in Relevant Year t*

$FUEL_{j,t}$	*is allowed fuel supply costs for fuel j in Relevant Year t*
$FUPR_{j,t}$	*is allowed fuel supply price for fuel j in Relevant Year t*
$FUCO_j$	*is specific fuel consumption of fuel j, as determined by the Regulator at the most recent Periodic Review (expressed in unit of fuel per unit supplied by the Regulated Generator)*
$FUPR_{j,t-1}$	*is allowed fuel supply price for fuel j in Relevant Year t-1 except for Relevant Year 1, when a value determined by ERO at the most recent Periodic Review shall be used (expressed in €/unit of fuel)*
$FPI_{j,t}$	*is the annual change in a fuel price index for fuel j, as specified by the Regulator at the most recent Periodic Review (expressed in %)*

3.3 The variable operating costs (VOM_t) shall be calculated at Regular Adjustments using the following formula:

$$VOM_t = VOM_{t-1} * (1 + CPI_{t-1} - Z_t)$$

Where

VOM_t	*is allowed variable operating costs in Relevant Year t*
VOM_{t-1}	*is allowed variable operating costs in Relevant Year t -1 except for Relevant Year 1, when a value determined by ERO at the most recent Periodic Review shall be used*
CPI_{t-1}	*is the actual value of inflation in Relevant Year t-1, measured using the Harmonised Indices of Consumer Prices (HICPs) – All Items, for the Eurozone, published by Eurostat*
Z_t	*is the expected annual efficiency improvement in the variable operating costs of the Regulated Generator, as determined by ERO at the most recent Periodic Review*

3.4 Licence Fee ($LICC_t$) shall be calculated at Regular Adjustments using the following formula:

$$LICC_t = LICCf_t + (LICCa_{t-1} - LICCf_{t-1}) * (1 + I_t)$$

Where

$LICC_t$	*is the Licence Fee in Relevant Year t*
$LICCf_t$	*is the forecast Licence Fee in Relevant Year t*
$LICCa_{t-1}$	*is the actual Licence Fee in Relevant Year t-1*
$LICCf_{t-1}$	*is the forecast Licence Fee in Relevant Year t-1*
I_t	*is the interest rate for the Relevant Year t calculated based on EURIBOR plus 1%*

SCHEDULE 2 REGULATORY ASSET BASE

1 This schedule describes the determination of the Regulatory Asset Base for the purpose of calculating allowed depreciation (Article 10) and allowed return on capital (Article 11).

2 The Regulatory Asset Base shall be a regulatory value of the Regulated Generator's used and useful fixed assets. It shall distinguish between different classes of assets.

3 The Regulatory Asset Base shall be updated at each Periodic Review as follows:

3.1 Allowed depreciation costs during the current Regulatory Period shall be subtracted from the Regulatory Asset Base, calculated on a straight-line basis using Economic Asset Lives;

3.2 Asset disposals during the current Regulatory Period shall be subtracted from the Regulatory Asset Base based on their regulatory value. Any difference between the disposal value and regulatory value of an asset, shall be deducted from Maximum Allowed Revenues in the forthcoming Regulatory Period;

3.3 Approved capital expenditure during the current Regulatory Period shall be added to the Regulatory Asset Base as from the date when the asset is brought into service and at the cost approved in the Approved Investment Plan. Interest during construction shall be capitalised. For the avoidance of doubt, the Regulator shall not make any retroactive reduction in future revenues to account for differences between the actual cost of investments and the approved cost. However the Regulator shall consider actual costs at future Periodic Reviews as a means of forecasting the cost of future investments;

3.4 If a capital project in the Approved Investment Plan is not brought into service in the current Regulatory Period, its approved cost shall not be added to the Regulatory Asset Base at the next Periodic Review and any revenues earned from the project in the current Regulatory Period shall be deducted from revenues in the following Regulatory Period;

3.5 Where any maintenance cost is or has previously been included in allowed operating costs it shall not be capitalised, nor shall it be included in the Regulatory Asset Base; and

3.6 The Regulatory Asset Base shall be adjusted to take into account inflation over the previous Regulatory Period, using the Harmonised Indices of Consumer Prices - All Items for the Eurozone area as published by Eurostat as the relevant measure.

4 Economic Asset Lives for different asset classes shall be used to calculate depreciation on the Regulatory Asset Base. Economic Asset Lives shall be determined at Periodic Reviews such that they reflect the technical lives of assets, except where there is demonstrable reason why the technical life of an asset shall vary from the useful economic life of an asset.

5 Approved capital expenditure shall be determined at Periodic Reviews based on the Approved Investment Plan for the forthcoming Regulatory Period. The Approved Investment Plan shall:

5.1 Comprise the capital projects reasonably required to provide supplies;

5.2 Identify each capital project ranked in priority order;

5.3 Show the benefit to Regulated Customers that each capital project is reasonably expected to deliver;

5.4 Have regard to any other relevant investment or development plans for the Regulated Generator that have been approved by the Regulator (and any differences between these plans shall be identified by the Regulated Generator and explained); and

5.5 Be developed using discounted cash flow techniques.

6 The Approved Investment Plan shall be implemented as follows:

6.1 The Regulated Generator shall use all reasonable endeavours to ensure the implementation of the Approved Investment Plan in line with its approved timetable;

6.2 If the Regulated Generator shall be or is unable to, for reasons beyond its control, undertake a capital investment in accordance with the timetable given in the Approved Investment Plan, it shall notify the Regulator. The Regulated Generator shall also detail the reasons for the delay and the revised timetable;

6.3 The Regulated Generator may at any time apply to the Regulator to substitute a capital project in its Approved Investment Plan for an alternative capital project; so long the alternative project can be shown to be expected to result in the same or greater net benefits to customers (taking account of the expected outcomes and lifetime costs). If the Regulator approves the substitution, the alternative project shall be added to the Regulatory Asset Base at the next Periodic Review. For the avoidance of doubt, Maximum Allowed Revenues in the current Regulatory Period shall not be adjusted; and

6.4 If the Regulated Generator substitutes a capital project in its Approved Investment Plan for an alternative project without the prior approval of the Regulator, the Regulator shall consider whether to approve the substitution at the next Periodic Review but is not bound to do so.

7 For the purposes of determining the allowed Lignite Supply Costs, the Regulator shall, where no lignite supply agreement exists, determine a Regulatory Asset Base for the lignite mining business in the same way as described above, with the following exceptions:

7.1 The Regulator shall consult with the licensed operator of the lignite mining business on their proposed investment plan, but shall not have powers to require the submission of any such plan or to approve it;

7.2 Based on these consultations, the Regulator shall prepare their own estimates of projected investment requirements of the lignite mining business for the purpose of determining Lignite Supply Costs; and

7.3 The Regulator shall use such information on additions and disposals as is available to it, from the published financial accounts of the licensed operator of the lignite mining business and from consultation with the licensed operator in determining what additions and disposals have been made for the purposes of updating the Regulatory Asset Base at each Periodic Review.

SCHEDULE 3 WEIGHTED AVERAGE COST OF CAPITAL

1 The Weighted Average Cost of Capital shall be calculated on a pre-tax basis according to the following formulae:

$$WACC = (1 - gi) * (rEi) / (1 - t) + gi * (rDi)$$

Where

WACC	*is the Weighted Average Cost of Capital*
gi	*gearing (debt:equity ratio) for firm i*
rEi	*real cost of equity (expressed as a %) for firm i*
rDi	*real cost debt (expressed as a %) for firm i*
t	*Kosovo corporate income tax rate*

2 The gearing (g) shall be a value determined by the Regulator between 0 and 1, and shall represent the share of debt in total financing. The value shall be determined based on a consideration of the actual financing mix of the Regulated Generator, the financing mix that might be expected for similar commercial businesses and the financing mix of similar utilities internationally.

3 The cost of equity (rEi) shall be a value calculated by the Regulator using the Capital Asset Pricing Model (CAPM) with the following general formula:

$$rEi = rf + \beta i * ERPm$$

rf	*risk-free rate*
ERPm	*equity risk premium applicable to the market as a whole*
βi	*covariance between the returns on the individual equity asset and those of the market as a whole (the equity beta)*

3.1 The risk-free rate (rf) shall represent the cost of sovereign debt in Kosovo, in real terms, and shall be determined by the Regulator using evidence on the cost of sovereign debt for Kosovo and/or, where this is unavailable or insufficient, the cost of sovereign debt for countries considered to have a similar credit status to Kosovo.

3.2 The equity risk premium (ERPm) shall be determined by the Regulator using evidence on the equity risk premium internationally.

3.3 The beta (βi) shall be determined by the Regulator using evidence on the beta applicable to similar utilities internationally.

4 The cost of debt (rDi) shall be the average interest rate of existing long-term loans (exceeding one year) to the Regulated Generator, expressed in real terms and weighted according to the value in Euros of each loan.

4.1 The Regulated Generator shall be required to procure loans through a competitive process, or to demonstrate to the satisfaction of the Regulator that the interest rate of those loans not procured through a competitive process is equal to or less than the prevailing market interest rate at the time the loan agreement was signed.

4.2 Where the Regulator considers that the interest rate of a loan not procured commercially exceeds the prevailing market interest rate, that loan shall be excluded from the calculation of the cost of debt.

4.3 Where the Regulator considers there are insufficient existing loans to provide a reasonable estimate of the actual cost of future debt financing to the Regulated Generator, the Regulator may make an adjustment to the actual cost of debt calculated as above. This adjustment shall be made based on:

(i) An assessment of the prevailing market interest rate for loans to businesses of similar size, risk and credit status as the Regulated Generator.

(ii) An assessment of the expected interest rate applied to any future concessional loans to the Regulated Generator.

(iii) An assessment of the expected mix of commercial (non-concessional) and concessional loans in the debt of the Regulated Generator over the coming Regulatory Period.

5 For the purposes of determining the allowed Lignite Supply Costs, the Regulator shall, where no lignite supply agreement exists, determine a Weighted Average Cost of Capital for the lignite mining business in the same way as described above, with the following exceptions:

5.1 The Regulator shall consult with the licensed operator of the lignite mining business on their costs of financing;

5.2 As the Regulator has no powers to require the licensed operator to procure loans through a competitive process, the Regulator shall determine an estimated cost of debt for the licensed operator using the same principles as described in 4.3 of this schedule; and

5.3 In doing so, the Regulator shall take due account of any evidence on actual financing costs presented to it by the licensed operator.

SCHEDULE 4 PERIODIC REVIEW PROCESS

1 The Regulator shall, in order to promote transparency, publish all submissions, comments, and other documentation received from the Regulated Generator or other interested parties in relation to the Periodic Review on its official website within [5 working days] of its receipt and the Regulator shall disclose all material information submitted to it by the Regulated Generator, excluding any information that the Regulator acknowledges as being commercially confidential.

2 The Regulator shall initiate the Periodic Review no later than [six months] prior to start of the forthcoming Regulatory Period. Different timing shall apply during the Transitional Period as given in Schedule 9.

3 The Regulator shall initiate the Periodic Review by notification to the Regulated Generator of:

3.1 The years for which actual, estimated forecast data is required;

3.2 The format in which the data is required to be submitted;

3.3 The timetable for submission of the Regulated Generator's Proposal for its Maximum Allowed Revenue for the forthcoming Regulatory Period; and

3.4 The timetable for the overall review process.

4 The Regulated Generator's Proposal shall contain the following information and address the following matters (without limitation):

4.1 Actual Regulated Revenues earned during the current Regulatory Period (using a reasonable estimate for the remaining months where necessary);

4.2 Actual costs of providing supply during the current Regulatory Period, in line with the definition of costs that was used for calculating Maximum Allowed Revenues and Energy Costs;

4.3 Actual Lignite Supply Costs during the current Regulatory Period;

4.4 The annual report and audited financial statements for each financial year that ended in the current Regulatory Period;

4.5 Actual available capacity and units supplied during the current Regulatory Period;

4.6 Forecast available capacity and units supplied for the forthcoming Regulatory Period;

4.7 Forecast Maximum Allowed Revenues and Energy Costs, reporting each of the allowed cost components separately, for the forthcoming Regulatory Period;

4.8 Forecast Lignite Supply Costs for the forthcoming Regulatory Period; and

4.9 Any other additional material that the Regulator reasonably considers should be included in the Regulated Generator's proposal, so long as the Regulator has notified the Regulated Generator a reasonable time prior to the deadline for the Regulated Generator's proposal.

5 The Regulated Generator shall, to the fullest extent possible, apply the methodology set out in this Rule in preparing its Proposal. It shall disclose any areas where it has not applied the methodology, the reason for not applying it, the reasons supporting the alternative approach, and provide an estimate of the impact of using the alternative approach.

6 Upon receiving the Regulated Generator's Proposal, the Regulator shall determine its accuracy, relevance and reasonableness by applying the methodology set out in this Rule, including determining whether the proposed Maximum Allowed Revenues and Energy Costs reflect the reasonable costs of supply.

7 The Regulator shall prepare a Provisional Decision on the Regulated Generator's Proposal no later than [50 Business Days] before the start of the forthcoming Regulatory Period, after consulting with the Regulated Generator as necessary. The Provisional Decision shall set out the Regulator's proposals on the Maximum Allowed Revenues and Energy Costs to be recovered by the Regulated Generator during the Regulatory Period and the justification for these. The Regulator, in preparing its Provisional Decision, may amend, remove or replace any part of the Regulated Generator's Proposal as it considers appropriate provided that it shall identify such amendments, removals or replacements and provide justification for these.

8 At the same time as it notifies the Regulated Generator of its Provisional Decision, the Regulator shall launch a public consultation on its Provisional Decision, in accordance with the Law on the Energy Regulator.

9 Following completion of the public consultation and no later than [20 Business Days] before the start of the forthcoming Regulatory Period, the Regulator shall make its Final Decision on Maximum Allowed Revenues and Energy Costs for the forthcoming Regulatory Period. Its decision shall be consistent with this Rule.

10 Maximum Allowed Revenues and Energy Costs as provided in the Regulator's Final Decision shall apply from the start date of the forthcoming Regulatory Period.

11 The Regulated Generator may dispute or appeal any decision by the Regulator in accordance with applicable legislation.

SCHEDULE 5 REGULAR ADJUSTMENT PROCESS

1 The Regulated Generator shall submit the proposed new Maximum Allowed Revenues and Energy Costs for the forthcoming Relevant Year to the Regulator at least [20 Business Days] before the start of the forthcoming Relevant Year. The Regulated Generator shall also include in its submission all relevant documents and evidence including the values relating to all the components of the Regular Adjustment formulae given in Chapter 7 and any other items notified by the Regulator.

2 The Regulator may reasonably require the Regulated Generator to further explain its method of calculating the proposed Maximum Allowed Revenues and Energy Costs, and if so required, the Regulated Generator shall promptly provide to the Regulator any further information or explanations sought.

3 The Regulator shall advise the Regulated Generator at least [5 Business Days] before the start of the forthcoming Relevant Year whether or not it approves the Regulated Generator's calculation of the proposed Maximum Allowed Revenues and Energy Costs.

4 If the Regulator approves the proposed Maximum Allowed Revenues and Energy Costs, they shall become the Maximum Allowed Revenues and Energy Costs for the forthcoming Relevant Year.

5 If the Regulator does not approve the proposed Maximum Allowed Revenues and Energy Costs, it shall provide reasons and evidence why, in accordance with this Rule. The Maximum Allowed Revenues and Energy Costs shall not be adjusted until the Regulator approves a proposal or provides its own calculation of Maximum Allowed Revenues and Energy Costs.

6 Any difference in revenues that arises from incorrect calculations, misreporting of Actual Regulated Revenue and Energy Costs, or disputes relating to Regular Adjustment shall be recovered in subsequent Relevant Years.

7 If the Regulator does not advise the Regulated Generator within the required period, approval is assumed and the proposed Maximum Allowed Revenues and Energy Costs shall become effective on the first day of the following Relevant Year.

8 The Regulated Generator may dispute or appeal any decision by the Regulator in accordance with applicable legislation.

SCHEDULE 6 EXTRAORDINARY REVIEW PROCESS

1 If an Extraordinary Event has occurred, the Regulated Generator may request an Extraordinary Review.

2 An Extraordinary Review cannot be launched undertaken within [six months] of a Periodic Review or the completion of a previous Extraordinary Review.

3 An Extraordinary Review may relate to more than one Extraordinary Event, in which case this schedule addresses the cumulative financial effect of those events.

4 Within [20 Business Days] of the Regulated Generator requesting an Extraordinary Review, it shall submit to the Regulator a Statement of Financial Impact that includes the following matters:

4.1 A description of the Extraordinary Event that is the reason for requesting the Extraordinary Review;

4.2 A summary of the impact of the Extraordinary Event on the Regulated Generator's business;

4.3 An estimate of the change in the Regulated Generator's costs in each year from the date that the Extraordinary Event occurred (or began) to the end of the current Regulatory Period;

4.4 An estimate of the change in forecast revenues resulting from the Extraordinary Event, in each year from the date that the Extraordinary Event occurred (or began) to the end of the current Regulatory Period;

4.5 A calculation of the financial impact on the Regulated Generator of the Extraordinary Event in each year, calculated as the sum of the change in the Regulated Generator's costs and revenues above. Revenues shall be treated as positive numbers and costs treated as negative numbers; and

4.6 A calculation of whether the financial impact is expected to be greater than the Materiality Threshold multiplied by the revenues received by the Regulated Generator (in the year before the Extraordinary Event) multiplied by the number of years between the date of the Extraordinary Event and the end of the Regulatory Period. The Materiality Threshold shall be a fixed percentage determined at Periodic Reviews; and

5 If the Regulated Generator determines that the financial impact is greater than the Materiality Threshold, it shall include in its Statement of Financial Impact a proposed Extraordinary Adjustment to Maximum Allowed Revenues and/or Energy Costs. The proposed Extraordinary Adjustment shall meet the following conditions:

5.1 The Extraordinary Adjustment shall change Maximum Allowed Revenues and/or Energy Costs in such a manner that the Net Present Value of the forecast change is equal (but opposite sign) to the Net Present Value of the financial impact of the Extraordinary Event, using the Weighted Average Cost of Capital as the discount rate;

5.2 The timing and structure of the Extraordinary Adjustment shall, where possible, reduce the tariff shock to customers (for example by smoothing the effect of the Extraordinary Adjustment over a number of years).

6 The Regulator may also launch an Extraordinary Review without the request of the Regulated Generator. If so, the Regulator shall notify the Regulated Generator and include a description of the Extraordinary Event and a summary its expected impact. The Regulated Generator shall then prepare a Statement of Financial Impact as per the process described above.

7 The Regulator may reasonably require the Regulated Generator to further explain its method of calculating the Statement of Financial Impact and Extraordinary Adjustment, and if so required, the Regulated Generator shall promptly provide to the Regulator any further information or explanations sought.

8 The Regulator shall advise the Regulated Generator within [20 Business Days] of receiving the Statement of Financial Impact whether or not it approves the Regulated Generator's proposed Extraordinary Adjustment. The Regulator shall approve the proposal if it:

8.1 Meets the conditions provided above;

8.2 Is calculated correctly; and

8.3 Takes into account all material information reasonably available at the time.

9 If the Regulator approves the proposed Extraordinary Adjustment, the new Maximum Allowed Revenues and/or Energy Costsshall become effective immediately.

10 If the Regulator does not approve the proposed Extraordinary Adjustment, it shall provide reasons and evidence why, in accordance with this Rule. Maximum Allowed Revenues and/or Energy Costs shall not be adjusted until the Regulator approves a proposal.

11 If the Regulator does not advise the Regulated Generator within the required period (above), approval is assumed and the proposed Extraordinary Adjustment shall become effective immediately.

12 The Regulated Generator may dispute or appeal any decision by the Regulator in accordance with applicable legislation.

SCHEDULE 7 EXTRAORDINARY EVENTS

1 An Extraordinary Event shall be the occurrence of any one of the following:

1.1 Any change in the tax rate, including royalties, applicable to the Regulated Generator that is greater than 3% and shall not be fully recovered through Regular Adjustments;

1.2 Any force majeure events as defined in Schedule 8;

1.3 Any other event, which meets all of the following conditions:

(i) Was not reasonably foreseeable;

(ii) Was not reasonably under the control of the Regulated Generator;

(iii) The Regulated Generator was not required or reasonably expected to provide against;

(iv) Shall not be fully recovered through Regular Adjustments; and

(v) Shall significantly change the revenues and/or costs of the Regulated Generator over any 12 month period, such that it seems reasonable that the Materiality Threshold (described in Schedule 6) may be breached.

2 The occurrence of an Extraordinary Event is sufficient to trigger an Extraordinary Review, however as described in Schedule 6, the event must still breach the Materiality Threshold before Maximum Allowed Revenues shall be adjusted.

SCHEDULE 8 FORCE MAJEURE EVENTS

1 A force majeure event shall be an exceptional event or circumstance which is all of the following:

1.1 Is beyond the Regulated Generator's control;

1.2 The Regulated Generator could not reasonably have provided against;

1.3 Having arisen the Regulated Generator could not reasonably have avoided or overcome; and

1.4 Is not substantially attributable to the Regulated Generator.

2 A force majeure event may include, but is not limited to, exceptional events or circumstances of the kind listed below, so long as the conditions above are satisfied:

2.1 War, hostilities (whether war be declared or not), invasion, act of foreign enemies;

2.2 Rebellion, terrorism, sabotage by persons other than the Regulated Generator's employees, contractors or subcontractors, revolution, insurrection, military or usurped power, or civil war;

2.3 Riot, commotion, disorder, strike or lockout by persons other than the party's employees, contractors or subcontractors;

2.4 Munitions of war, explosive materials, ionising radiation or contamination by radio-activity, except as may be attributable to the party's use of such munitions, explosives, radiation or radio-activity; and

2.5 Natural catastrophes such as earthquake, tsunami, typhoon or volcanic activity.

SCHEDULE 9 TRANSITIONAL PROVISIONS

1 The Transitional Period is from 1 April 2012 until 31 March 2016.

2 The first Regulatory Period shall be [4 years].

3 The Regulator shall define the opening Regulatory Asset Base (as at 1 April 2012) prior to the start of the first Regulatory Period.