

## **Respondent No. 1 - Draft Regulations on Tariff Setting Methodology**

### **Section 4:**

Establishes a concept of a “social tariff” which is “defined and financed in accordance with the Policy established by the Minister”. How does the Minister intend to finance this? Such financing should not impact the network licensee’s ability to meet its service standards, make necessary capital investments and earn a reasonable rate of return.

### **Section 7:**

The retail tariff includes “(c) the demand or fixed charge”. What is intended by this fixed or demand charge? Here the demand charge should include a fixed component for those rate payers that self-generate electricity but at the same time maintain a connection to the grid.

### **Section 8:**

The Commission is limited in calculating the Non-Fuel Revenue Requirement to costs that are “prudently incurred”. This is an open-ended limitation; how is prudent defined and established?

### **Section 9:**

The concept of “efficient conversion” of fuel into electricity is introduced by the regulations to the fuel pass through mechanism. The efficiency adjustments to the fuel rate which are defined in Schedule 3, Section 1.4 and comprise a “system heat rate target” and “system losses rate target” which are both “determined by the regulator”. However, the regulations neither define how targets are set nor what the proposed targets levels should be. As written, this appears arbitrary and will serve as a deterrent to investment. The efficiency targets must be clearly defined, the process for setting targets clearly established along with the consultation and review period with the network licensee.

### **Section 17:**

The levels for service standards are based on “(a) industry-best practice internationally”. However, this does not account for the economic, technical and other operating factors specific to small island states. Service standards in Sweden are not directly comparable to Grenada. The language should be modified to take this into account, as it is in Section 2.5 of Part B of Schedule 1 where it states, “customary practices of electricity utility operation recognizing the specific peculiarities of operating in Grenada”.

### **Section 28:**

This section allows for a tariff calculated according to a different methodology than contained in the regulation schedules. However, the circumstances in which this tariff would apply are general and ill-defined and are based only on a lack of “information available”. The circumstances must be defined more precisely, in particular what specific missing information would prevent compliance and trigger the contemplated “interim tariff”.

Section 29 (3):

This sub-regulation is very unclear regarding the obligation of the Commission to follow the recommendation of consultants and their studies as well as the circumstances and consequences if the Commission does not. The sub-regulation should be clarified in this respect precisely defining the circumstances in which the Commission would not follow the recommendations of consultants and studies prepared in conjunction with sub-regulation 29 (1).

Schedule 1, Part A, 1.5:

It is unclear whether contributions to the Universal Service Fund are to be added to the base rate under taxes and licence fees. This should be clarified and added to the building blocks.

Schedule 1, Part B, 2.3:

The Commission is limited in calculating the NFRR to costs that are “prudently incurred”. This is an open-ended limitation and can be interpreted arbitrarily. The concept of prudence must be clearly defined and established.

Schedule 1, Part B, 2.4 (f):

The average Country Risk Premium (country default spread x relative equity market volatility for that market) for a comparable Caribbean country peer group is 6.5% . The allowed Rate of Return on Equity should accurately reflect the required risk-adjusted equity return for an investor. The fixed adder should be increased to 6.5%. Additionally, the allowed Rate of Return on Equity includes the Long Term Bond Rate of the Government’s “most recent long-term bond issued by the RGSM”. However, Grenada has previously been in selective default and there has not been a recent issue of a “long term” bond. Only short term bonds of 2-years maturity or less have been issued recently. Yields have fluctuated on Grenada’s outstanding medium-term bonds from 15 to +30%. Short-term bond rates are not an appropriate substitute for Long-Term Bond rates as they will understate the risk of investment. In the absence of a Long-Term benchmark bond offering by Grenada, the average Long-Term bond rate of a comparable peer country group should be used as a substitute.

Schedule 2, Part B, Section 2.1:

The section describes the service standards and initial targets for the calculated Q-Factor which are very aggressive and do not account for any investment initial investment required to reach those targets. GRENLEC has never achieved 6.9% system losses and moving from 85% to 95% collections may create some social frictions to achieve given the required aggressive collection methods. These initial targets should be reviewed and agreed with the Network Licensee during the initial Tariff review, otherwise it will negatively impact the bankability of the Network Licensee.