CONSULTATIVE DOCUMENT

Document Reference: 2011/002/CD-03

DRAFT

TRANSMISSION, DISTRIBUTION AND SUPPLY LICENCE

For

DOMINICA ELECTRICITY SERVICES LTD

STATEMENT OF RESULTS AND PRELIMINARY DECISIONS

April 2013

Independent Regulatory Commission
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CONSULTATION PROCESS

Persons who wish to participate in this consultation and to express opinions on this Document are invited to submit comments in writing to the IRC. Reponses/Comments should be sent to:

Executive Director
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P.O. Box 1687
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Responses, clearly showing the Document Reference identification, may be sent by mail or fax to the address or fax number above or by e mail to: admin@ircdominica.org.

Confidential information provided with responses should be submitted as a separate document and clearly identified as such.

In order to stimulate debate, the IRC will place any responses received on its website at www.ircdominica.org immediately following the last date for receipt of responses. Comments on the responses will also be entertained by the IRC which should, likewise, be submitted by the date indicated.

The references and proposed time table for this consultation are:

Document Ref No: 2011/002/CD-03
Document Title: Transmission Distribution and Supply Licence for DOMLEC – Statement of Results

Event	**Proposed Date**
Publication of Document	April 19, 2013
Responses close	April 30, 2013
Decision by Commission	September 13, 2013

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DRAFT TRANSMISSION DISTRIBUTION AND SUPPLY LICENCE FOR DOMINICA ELECTRICITY SERVICES LTD

Introduction and Background

Pursuant to its duties under the Electricity Supply Act 10 of 2006 (ESA), which establishes a regime of separate licensing for each of the business sectors of public electricity supply undertakings – generation, transmission distribution and supply, the Commission issued Consultative Document Ref No: 2011/002/CD-02 as the second consultation in its deliberations regarding the issuance of a new Transmission, Distribution and Supply Licence for DOMLEC.

The consultation is being conducted in accordance with the timetable set out below at Table 1.

This procedure establishes the process as summarized at Table 1.

Table 1
Time table for managing negotiations with DOMLEC for renewal or issuance of new Licences

<table>
<tr><th>Months before end of Term</th><th>Target objective (1)</th><th>Target objective (2)</th></tr>
<tr><td>42</td><td colspan="2">Licencee to advise the Commission, in writing, as to its intention to renegotiate the licence or surrender it. This will be acknowledged by the Commission within seven (7) working days of receipt.</td></tr>
<tr><td>39</td><td>If Licencee demonstrates its intention to renegotiate the Licence, the Commission to respond to the Licencee providing broad frame work and draft of proposed new Licence and setting out a proposed time table for meeting the objective contained herein.</td><td>If Licencee demonstrates its intention to surrender the licence, the Commission to respond to the Licencee proposing the broad framework and procedure for managing the Investor's disengagement from the business of the Licencee</td></tr>
<tr><td>39 - 36</td><td>Preliminary negotiation of new licence terms.</td><td rowspan="3">New investors identified and new Licence negotiated concomitantly with sale/disposal of the asset by the investor</td></tr>
<tr><td>36 - 33</td><td>Public consultation on proposed new Licence</td></tr>
<tr><td>33 – 30</td><td>Final round of negotiations</td></tr>
</table>

27	Commission issues new Licence	
24	If the Commission and the Licensee fail to reach agreement on a new Licence or if the Investor fails to identify a purchaser satisfactory to the Commission, the Commission will recommend to the Minister that the Government embarks on the process of "acquisition" of the assets of the investor at the Fair Market Value* - payment of which will be effected on the expiration date of the Term or such other date as the parties may mutually agree. New Licence to become effective on the date of acquisition of the asset.	

The Commission issued the second consultative document Consultative Document Ref No: 2011/002/CD-02 on January 14, 2013 and held four public meetings at which members of the public were invited provide inputs to the discussion. The following public meetings were held

- Roseau January 28, 2013
- Portsmouth January 29, 2013
- Marigot February 19, 2013
- Grand Bay February 26, 2013

Additionally, the Commission received some comments posted to its web site and also formal written comments from the Government of Dominica's "Deal Team" which is negotiating certain geothermal arrangements on behalf of the Government.

The Commission wishes to thank all those who have participated in the process and to recognize the valuable inputs that have been provided.

This document discusses the comments received and sets out the Commission's preliminary decisions in regard to the issues raised. The Commission wishes to assure all stake holders that all inputs and suggestions have been carefully reviewed. However it should be bourne in mind that many of the points raised will have been repetitive and where this is so the Commission has, in this document, chosen to group similar comments and represented these as a single comment.

In the next section the issues raised in the Consultation are discussed and in the section following the Commission sets out its preliminary decisions.

For completeness, the Draft Transmission Distribution and Supply Licence which was attached to the Consultation Document is attached for ease of reference.

Consultation Questions

The Commission raised three specific issues in the consultation; one with regard to the proposed Term of the Licence and the other regarding the Commencement Date.

Scope of the Licence

In the consultation leading to its Decision ***Regulatory Policy and Procedure – Licensing Procedures Document Reference: 2009/001/D,*** the Commission made no references to the possibility of a third party developer providing retail supply of electricity (using any available technology) where the circumstances are that it is uneconomic for DOMLEC to provide the supply or for any other reason DOMLEC is unwilling to do so. This matter was not raised as an issue during those proceedings and since then the Commission has reflected on the matter and has formed the view that under these circumstances third party supply should be allowed. The Draft Licence therefore makes this provision under Condition 2 where at Clause 3 it provides as follows:

> Notwithstanding the provisions of Clause 2 of this Condition 2, the *Commission* will allow and issue licences for third party supply to any *Development Areas* where it is demonstrated that for technical, commercial or other reasons the Licensee is unable or unwilling to extend the electricity supply system to those area.

It would be the intention Commission intention to amend its licensing procedure to reflect the principle which guides this provision. Clear and specific rules/guidelines to govern these arrangements would have to be prepared in order to ensure that this facility does not compromise the exclusive of DOMLEC's Licence.

Consultation Question No 1

The Commission would be interested to hear the views of stakeholders on the principle of allowing third parties to supply un-served areas under specific conditions. Do respondents have any specific recommendations on the circumstances that would allow third party supply to development areas and whether, e.g. the solutions should be prescribed by the Commission or approved by DOMLEC on a case by case basis,

Responses

Although no specific responses were received to the Question, a number of respondents inquired and sought clarifications as to how the arrangement would work and whether, for example, DOMLEC would be the licence issuing party. The Commission affirmed that pursuant to the Act, developers would require licences issued by the Commission and that these would include provisions for construction to be at standards consistent with those to which DOMLEC is held.

Term and Renewal of Licence

The current licence ends on December 31, 2015. The Commission's motivation for initiating the licensing discussions for the issuance of a new licence, as early as 42 months in advance, is to preserve the environment for continuity such that the investor has a fair degree of certainty in making investment decisions, particularly as the end of the term of the licence approaches.

As the Licensee that is required to invest in the electricity delivery infrastructure on an ongoing basis to ensure that the transmission and distribution systems are robust and have the capacity to deliver electricity from the generating plant to the end user with acceptable reliability and quality, the licensee really requires a longer term certainty of the licensing environment. For this reason the licence cannot reasonably be tied to the economic life of the investment as is the case of generating licences. In considering the question of what is a reasonable term the Commission feels that the utility company as a corporate entity should not be confused with the investors in that entity. The fact is that while the investors and perhaps the controlling interest in the company may change from time to time, the utility will always exists, however organised, with the express purpose of supplying electricity to the country. In this sense the utility company is unlike any other business which can open and close depending on the business climate. The important issue here is that the licence is granted to the utility company, in this case DOMLEC and not individually to the investors in DOMLEC. The perception of risk is the factor that will largely influence the investor's attitude to DOMLEC, and in many instances this perception will drive expectation of return or willingness to invest. Clearly, the longer the term of the licence (all other things being equal) is the lesser the risk or the greater the certainty of recovering investment over the life of the licence. In any dispensation, however, where a licence has a finite term, the problem of the willingness of the investor to make new investments will always arise as the term comes to an end. The Commission has considered these greatly and in weighing the competing requirements, it has formed the view that the initial term should be related to the typical period for the recovery of Transmission and distribution infrastructure assets, if those investments were made on the first day of the licence. However, instead of waiting three and half years before the end of the term to start the process of renegotiating the licence, the Commission has attempted to provide a regime of periodic assessment of the licensee's performance during the life of the licence and where the performance is deemed to be acceptable the licence term is extended for a specified period. If this arrangement works as intended, the term of the licence should roll at specified intervals, presuming the licensee (investors) have met its commitments.

It is against this background that the Commission has proposed that the initial term of the licence be 20 years subject to the following:

a. At any time after the fifth anniversary but prior to the sixth anniversary of the Commencement Date, and thereafter at every consecutive five (5) year interval, the Licensee may serve notice on the *Commission* requesting an extension of this Licence for a further period of five years. The Licensee must demonstrate to the satisfaction of the *Commission* that it has met or is meeting its obligations under the Licence and provide economic and technical justification in support of its request.

b. Provided that the Licensee demonstrates, to the satisfaction of the *Commission*, that it has made the previously submitted levels of investment and that it is not otherwise in breach of this Licence, then this Licence will be extended for a further five years subject to the same conditions or any modified conditions.

Consultation Question No 2
The Commission would be interested to hear views on and reactions to

a. the Commission's proposals for (i) an initial term of 20 years based on the premise that, the best practice is that investments in transmission and distribution infrastructure are assigned an economic life of 20 years and (ii) that DOMLEC's performance be reviewed every five years and that the license term be extended by five years where it is assessed that the company has met its commitments under the Licence.
b. DOMLEC's request for an initial term of 25 years

The Commission would also be interested in hearing alternate views with reasons.

Responses
Subsequent to the first round of negotiations DOMLEC proffered a view that a 25 year term initially would be ideal as the company would be better positioned to access long term financing at a reasonable cost which in the long run would redound to the benefit of consumers. The company also made the comment that the commissions position that transmission and distribution assets are normally depreciated over 20 years is incorrect. The company welcomed the proposal of the renewal mechanism every five years, but averred that this did not negate the necessity for a 25 year initial term.

The many views expressed reflected those of the "Deal Team" which were sceptical of the suggested "roll over" arrangement. The Deal Team suggested that the principle for establishing the licence term should be consistent with arrangements provided in other licences of a similar nature; i.e. for a finite time.

Regarding the actual term the views expressed were quite ambivalent as to a preferred period, the concern being more strongly voiced on insisting that a rigorous review mechanism had to be put in place to ensure that DOMLEC complies with the licence conditions and investment commitments.

Commencement Date

The current licence expires on December 31, 2015. It is proposed that the new licence would commence on January 1, 2016. It has been proposed that, assuming the current proceedings are completed within the expected time frame that the commencement date of the new Licence could be advanced to January 1, 2014; provided that the term is extended by the two years "lost". The Commission would not be unsympathetic to this proposal but it has the view that because of certain legacy considerations, the Government of Dominica should explicitly provide its opinion on this proposal.

Consultation Question No 3

Nevertheless, the Commission would be interested to hear views on and reactions to the proposal to define the commencement date as January 1, 2014 with the proviso that the term of the Licence be extended by two (2) years.

Responses

The overall consensus is reflected at the discussions at the Roseau meeting where it was felt that the commencement date is (2014 or 2016) is a non issue and really is a matter of what is practical. Both DOMLEC and the Commission's representatives were not seized with any preference except that the attractiveness and practicality of having the new licensing and therefore regulatory regime in place earlier rather than later had some merit.

The Deal Team has suggested that the current licence should run its full term to December 2015. This, it has opined, would allow, in the context of the geothermal development, for any "unforeseen matters related to the proposed PPA and interconnection to the national grid to be fully addressed before any actual license comes into force".

Other issues raised during the Consultation

A number of other issues were raised common concerns on the following:

- The timing for tariff reviews
- Wheeling
- Encouraging the development of renewable energy

The timing for tariff reviews

Both the Deal Team and at least one other member of the public raised the question of the conditions to trigger the first tariff review under the new Licence. The Deal Team raised two issues (a) against the background that the last consideration of DOMLEC's tariff was in 2007 and that such a review can only be triggered by a request from DOMLEC (as per the ESA, it suggested "*that some mechanism be included in the license that would allow the IRC to carry out a review if it receives a request from an authorised source and deems such a request as a valid one*" and (b) a recommendation that "*in view of the "basket of Energies" that are likely to come on stream in the coming years, a tariff re-structuring exercise is undertaken in early course*".

A member of the public raised the question that the draft Licence did not appear to have a provision that would cause the first tariff review to be initiated.

Wheeling

Although there were some implicit references to the concept of wheeling, the Deal Team expressed this as an opinion that arrangements should be provided in the Licence to allow wheeling of energy on the utility's grid citing the opportunities that would be available to potential investors to at least examine "*the viability of generation of energy at suitable locations and utilization at others where the investors themselves may need it*".

Encouraging the development of renewable energy

The question of renewable energy was first mooted by one participant at the Roseau meeting who queried whether the entire exercise was being conducted in the context of an Energy Policy issued by the government. Another, at the Portsmouth meeting was very concerned about the environmental concerns and hydro development.

The Deal Team raised the issue of renewable energy by suggesting that a maximum allowable limit for renewable energy generation should be established (after having due regard for system stability and other operating conditions. This it suggested would serve as an incentive for further investment in the sector (renewable). On another related issue it was suggested that the Commission should change its policy from "net billing" to "net metering". The Deal Team commented that "*We do feel very strongly about this matter as the Utility seems to be the only beneficiary to any grid-tied renewable energy initiatives established so far. Also, net metering would allow small scale and medium sized renewable energy initiatives to become relatively more viable to would be investors in the sector*".

Preliminary Decisions

After having considered all the views and comments received, the Commission's preliminary decisions and the reasons there for are set out below

Apart from the issues raised below and which were specific consultation questions, the Commission, in the absence of any substantive adverse comments intends to adopt the

Licence in its entirety as set out in the Draft that was attached to the consultation document.

With regard to the specific issues raised the Commission will reflect the following considerations in the final Licence:

Scope of the Licence

The Commission received no substantive comments or responses to the provisions of Clause 2 of Condition 2, where the *Commission* proposes to "*allow and issue licences for third party supply to any Development Areas where it is demonstrated that for technical, commercial or other reasons the Licensee is unable or unwilling to extend the electricity supply system to those area".*

The Commission has therefore determined that the provision as set out at Clause 2 of Condition 2 in the draft Licence to *allow and issue licences for third party supply to any Development Areas* is to be adopted.

In order to make the Clause 2 of Condition 2 of the Licence consistent with its Rules, the Commission will issue a Notice of Proposed Rule Making (NPRM) to amend its Decision ***Regulatory Policy and Procedure – Licensing Procedures Document Reference: 2009/001/D*** appropriately. As a procedural action, the Commission shall refer to the consultation under this proceeding as being relevant to the Proceeding on the NPRM.

Term

The Commission has taken careful note of the views emanating from the consultation which can be summarised as follows:

- There is certain ambivalence to 25 years or 20 years. If the longer term licence is granted then the conditions imposed on DOMLEC should be "strict" particularly in terms of implementing investment plans
- There was an expressed unease at the concept of the 5 year review and rolling five year extensions.
- There was a distinct and clear preference for a fixed term.

In considering these issues the Commission is mindful of its reasoning to fix the initial term as the shorter period. It also considers the concept of the five year review and rolling five year extension as a rather elegant means of securing the performance of the licencee with an assurance of continuity if the performance meets the required standards. The Commission though is minded to have regard to the very clearly expressed discomfort of respondents to the concept of 5 year review with 5 year extensions and has determined that it will abandon further consideration of this option.

Any discussion about the term for licences of the type under consideration, invariably conjures concerns about long term relationships with investors particularly if these investor happens to be foreign. The Commission is strongly of the view that, if the national and public interest is to be best served, utility companies such as DOMLEC require investors that have the capacity to raise capital and thus make the necessary investments in the company. It is in this context that the Commission thought it would be useful to repeat earlier comments on this question - In considering the question of what is a reasonable term the Commission feels that the utility company as a corporate entity should not be confused with the investors in that entity. The fact is that while the investors and perhaps the controlling interest in the company may change from time to time, the utility will always exists, however organised, with the express purpose of supplying electricity to the country. In this sense the utility company is unlike any other business which can open and close depending on the business climate. The important issue here is that the licence is granted to the utility company, in this case DOMLEC and not individually to the investors in DOMLEC. The perception of risk is the factor that will largely influence the investor's attitude to DOMLEC, and in many instances this perception will drive expectation of return or willingness to invest. Clearly, the longer the term of the licence (all other things being equal) is the lesser the risk or the greater the certainty of recovering investment over the life of the licence. In any dispensation, however, where a licence has a finite term, the problem of the willingness of the investor to make new investments will always arise as the term comes to an end.

The question of the period, 20 or 25 years, requires further thought as the pros and cons of each are equally compelling although he Commission is not persuaded by DOMLEC's argument that long term financing of Transmission and Distribution assets will be more attractive with the longer term. It is the Commissions' view that the most attractive financing that could be available would be through one of the multilateral lending agencies and these are not known to extend 25 year financial terms support for transmission and distribution infrastructure. The Commission is also of the view that regardless of the decision on the commencement date (to be discussed later), the actual number of years over which the company will have operating certainty includes the period up to the expiry of the current licence; that is to say that, for example, if the new licence is signed in December 2013 the company will enjoy the certainty to negotiate financing with effect from that date thus effectively reflecting certainty for 22 year period in the case of a 20 year term or 27 years in the case of 25 year term. It appears to the Commission that in these circumstances, a 20 year Term would be quite appropriate. In order to address the issue of certainty over continuity that will arise towards the end of the Term the Commission proposes that the licence conditions will provide for the process of renewal to commence 42 Months before the end of the term and conducted along the lines of the current proceeding.

The Commission has therefore determined that the Term of the Licence be fixed for 20 years with a provision for negotiations regarding renewal to commence 42 months and end 24 months before the expiration of the Term.

Commencement Date

As far as the Transmission Distribution and Supply Licence is concerned, the responses have not been sufficient to sway the Commission's thinking towards one option or another. The Deal Team's recommendation that the current licence should run its full term to December 2015 so as to allow, in the context of the geothermal development, for any "unforeseen matters related to the proposed PPA and interconnection to the national grid to be fully addressed before any actual license comes into force should be measured against the advantages of an earlier start; for example, the possibility of an earlier rather than later tariff review, the prospect of making early determinations on the investment programme as well as the ability of bringing a more rigid and formalised regulatory oversight regime into effect earlier rather than later. This would strengthen the Commission's position in terms of securing efficiency gains on behalf of consumers.

However, while the Commission would be minded to opt for the earlier (January 2014) commencement date, the fact is that the current licence cannot be terminated on an order of the Commission as these are Licence provisions that are enshrined in the ESA. For this to happen, the process as set out in the Act, would have to be conducted

The Commission has therefore determined that the Commencement Date of the new Licence shall be January 1, 2016.

The Commission would, however, be minded to change the Commencement Date to January 1, 2014 if the Company formally, requests this amendment to the current Licence and the due process followed.

Consideration of other issues raised during the Consultation

A number of other issues were raised common concerns on the following:

- The timing for tariff reviews
- Wheeling
- Encouraging the development of renewable energy

The timing for tariff reviews

The Commission has taken note of the comments regarding the need to undertaken a tariff review as soon as practicable after the Commencement Date. After having considered the matter the Commission agrees that this is a rather serious omission as there is no provision (either in the Act or in the Draft Licence) available to the Commission to trigger the initial tariff review. The Commission is of the view and agrees with respondents that DOMLEC's tariffs should be revisited as soon as practicable after the Commencement Date.

The Commission has therefore determined that a new Condition 34 – "Initial Tariff Review" will be included in the Licence to the effect that DOMLEC shall within

Three (3) Months of the Commencement Date submit an application to the Commission for a tariff review in the format set out in the Commission's Decision *Tariff Regime for Dominica Electricity Services Ltd - Document Ref 2009/004/D.*

Wheeling

The Commission notes the comments regarding wheeling where it is suggested that the licence should at least provide the opportunity for potential investors to the Dominican economy to be able to consider the option of wheeling of energy in investment decision making. Wheeling is an arrangement where a generator may connect at one point on the public electricity grid and connect the load at a another point using the grid purely as the means for transporting the energy and for which there would be charge by the owner/operator of the grid for use of the system.

In providing for its functions the ESA (S20) mandates the Commission to act in a manner which it considers best calculated to achieve a number of policy objectives and in this regard clauses (a), (b), (d), (e) and (g) of Section 20 reproduced below are instructive.

(1) The Commission shall, without limiting the generality of this section, have a duty to perform and exercise its functions and powers under this Act in the manner which it considers best calculated to:

> *(a) encourage the expansion of electricity supply in Dominica where this is economic and cost effective and in the public interest;*
> *(b) encourage the operation and development of a safe, efficient and economic electricity sector in Dominica;*
> *(d) facilitate the promotion of sustainable and fair competition in the electricity sector where it is efficient to do so;*
> *(e) protect the interests of all classes of consumers of electricity as to the terms and conditions and price of supply;*
> *(g) ensure that the financial viability of efficient regulated electricity undertakings is not undermined;*

The Commission regards wheeling to be just another mechanism for competition in the transmission distribution system and believes that it must be guided by Section 20 of the ESA. None the less, the Commission also believes that the long term construct of the Licence is such that the Commission must provide for the possibility of a changing environment and to this end should at least be testing the market for the viability of competition. Wheeling and or provisions for the use of the system by third parties is perhaps the most commonly adopted approach for these interventions. The Commission believes that it has a duty pursuant to Section 20 to continually seek to create an environment that facilitates competition. A case in point is the Commission's position on self generators where these are not discouraged because in themselves these generators compete with DOMLEC.

Having considered this situation the commission is minded to include a provision in the Licence which will not discourage wheeling/or third party use of the system.
The Commission has therefore determined that Condition 6 of the Draft Licence shall be amended to include a provision to the effect that DOMLEC shall be obliged to provide access to self generators for wheeling energy (use of system) for off take at another point on the system when such arrangements are determined by the Commission (after due process) to satisfy the provisions of Section 20 of the Act and at such charges as the Commission shall determine.

Encouraging the development of renewable energy
While these issues were not specific to the licence itself, the concern about the development of renewable energy is very relevant to the electricity supply environment in which the licence will have application.

The issue of the development of renewable and introduction of these technologies into the electricity supply environment pose challenges for regulators in many jurisdictions. Many regulators have as a primary mandate a duty to secure electricity to consumers at the least cost. It is for this reason that the regulator not only reviews and fixes tariffs but in doing so concerns itself with the workings of the entire operation – from system modelling and forecasting, to investment planning, to generation technology choices and transmission, distribution and supply operations. In most cases the renewable energy solutions do not represent the least cost option and where these technologies are introduced care has to be taken to understand the effect on tariffs. For example the Commission's decision to apply net billing for renewables connected to the network is conditioned by the fact that his modality is the most cost effective for consumers. Net metering on the other hand is the most advantageous to the investor. So while the suggestions that have been made regarding limits for renewable energy capacity and a change to net metering from net billing, the Commission must to be guided by Section 20 of the ESA.

The issues raised therefore on this subject are best addressed as Government policy the promulgation of which would provide the Commission to act pursuant to Section 18 of the ESA –

> *The Commission shall be independent in the performance of its functions and duties under this Act and shall not be subject to the direction and control of the Government or of any person, corporation or authority, <u>except that the Commission shall have due regard to the public interest and overall Government policy, as embodied in legislation</u>.*

The Commission has therefore determined that it can take no action on the issues raised regarding renewable energy but will await the appropriate policy guidance pursuant to Section 18 of the ESA

Attachment 1 – Draft Transmission, Distribution and Supply Licence