Regulating Electricity, Promoting Our Energy

CONSULTATIVE DOCUMENT

Document Reference : 2024/004/CD-02

Revenue Requirement and Rate Base

for

Dominica Electricity Services LTD (DOMLEC)

SECOND ISSUE OF CONSULTATIVE DOCUMENT, WITH COMMENTS ON RESPONSES TO THE FIRST CONSULTATIVE DOCUMENT

DECEMBER 2024

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:

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Responses, clearly showing the *Document Reference* identification, may be sent by mail to the address 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 all 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 timetable for this consultation document are:

- **Document Title: DOMLEC's Revenue Requirement and Rate Base** - ***Comments on The First Response and Second Issue of Consultative Document***
- **Document Reference No.: 2024/004/CD-02**

EVENT	DATES
Publication of First Issue of Document	October 8th, 2024
Responses Closed – ***End of Phase 1 of Consultation***	November 30th, 2024
Comments on First Response and Publication of Second Issue of Document	December 18th, 2024
Responses close - ***End of Phase 2 of Consultation***	January 3rd , 2025
Statement of Results and Commission's Decision	January 6th to 15th, 2025

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Introduction and Background

DOMLEC informed the Commission of its need to initiate a tariff review in 2021 and the process of the tariff review commenced later that year.

The Commission is of the view that to ensure timely completion of its review of any application for a tariff review submitted by DOMLEC it would consider certain critical issues in separate proceedings leading up to the conclusion of the tariff review. These issues, which are critical inputs to the tariff determination, are:

- Depreciation Study *(Completed April 2024)*
- Weighted Average Cost of Capital - WACC *(Completed October 2024)*
- The Revenue Requirement and Rate Base
- Approval of 5-Year Investment Plan
- Review and Approval of the Cost of the Service Study
- Review and Approval of the Rate Proposal

The Commission will, when requested by DOMLEC, conduct its review of and make determinations on these issues prior to the final submission of the rate proposal.

The Depreciation Policy was addressed and completed in April 2024, as per the Commission's "*Decision Document Ref: 2024/001/D – Depreciation Policy for Dominica Electricity Services Ltd*". The Approval of the Weighted Average Cost of Capital (WACC) Study was completed in October 2024 as per the Commission's "*Decision Document Ref 2024/002/CD-02/D – Weighted Average Cost of Capital (WACC) for Dominica Electricity Services Ltd*".

The Revenue Requirement is the total amount of money a utility must collect from its customers to pay for the generation, supply and distribution of electricity under normal operations to include its return on investment. Similarly, the Rate Base is the value of the utility's property, plant and equipment that are considered used and useful by the Regulatory Agency on which the utility is required to earn a reasonable rate of return.

DOMLEC submitted its application on the Revenue Requirement and Rate Base for the Commission's consideration. Following comprehensive review by the Commission and collaboration discussions with DOMLEC, the Commission and DOMLEC set out their proposed determination on the Revenue Requirement and Rate Base for shareholders engagements.

The Commission's objective in this proceeding is to consider and decide on the proposed Revenue Requirement and Rate Base for DOMLEC. The Commission issued its first Consultative Document (CD) on October 8th, 2024, and held a hybrid public consultation to include virtual and in-person consultation on November 19th, 2024. Comments on the first response and publication on the second issue of the Consultative Document ended on November 30th, 2024.

This new document sets out the Commission's response to the stakeholders' feedback and comments received from the first round of consultation and the Commission's proposed Decision that flowed from this consideration. These proposed Decisions will replace those, if and where appropriate, that were indicated in the previous Consultative Document

The Commission's key objective in this proceeding is to consider and decide on:

The Forecast Revenue Requirement that is considered sustainable and reasonable for DOMLEC under normal operation and to be factored in the determination of the average tariff for the 3-year tariff period.

Policy and Legal Framework

Legal Framework

The Commission's duties and functions regarding tariff making are provided for pursuant to provisions in three principal instruments:

(i) the Act;
(ii) the Licence; and
(iii) the Commission's Determination as per its "*Tariff Regime for Dominica Electricity Services Ltd Document Ref: 2009/004/D"* (herein referred to as 'the Determination').

The Act provides at Section 18

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, except that the Commission shall have due regard to the public interest and overall Government policy, as embodied in legislation.

At Section 19

The Commission shall have sole and exclusive authority to regulate all electricity entities that are subject to this Act and shall have full powers to regulate all licencee with regard to all economic and technical aspects of regulation in accordance with this Act especially with regard to the determination of tariff or electricity charges.

At Section 20

(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 Act gives the **Commission full authority to act independently** in the performance of its duties under the Act – specifically having regard to public interest considerations and government policy, as embodied in legislation. In providing for its functions the ESA (Section 20) mandates the Commission to act in a manner which it considers best calculated to achieve several policy objectives and in this regard clauses *(a)*, *(b)*, *(d)*, *(e)* and *(g)* of *Section 20*, reproduced above, are instructive.

Furthermore, *Section 20. (1) (c)* of *the Act* provides a duty for the Commission to *"ensure the security and efficiency of the supply of electricity in Dominica, through the conduct of an efficient long term planning process with due regard for future potential generation sources such as geothermal and wind energy"*.

While the Determination sets out in detail the methodology and process for determining the tariff for DOMLEC.

Regulatory Policy Objectives

The Commission's regulatory policy is to establish a tariff which balances the interests of the consumers and investors alike where the investors have the opportunity to realize a fair return on investment while customers can expect an efficient, responsive and economic service in an environment where the rights of all stake holders are preserved. The Commission will not guarantee a rate of return to the investors but will seek to create a regulatory environment where the incentives are such that the company, through efficient operational practices and continual efficiency improvements, will have the opportunity to achieve the desired rate of return during any tariff period.

Tariff Principles

There are basically two models for a tariff structure which could apply in the Dominica situation.

1. *A tariff which includes all the costs including the costs of fuel, based on a projected cost of fuel over the tariff period or;*
2. *A two-part tariff comprising (i) a non-fuel base rate and (ii) a fuel charge, which fully recovers the cost of fuel (subject to efficiency factors) and no more.*

Both methods use the same techniques and parameters for estimating Revenue Requirements; the exception being that in the first case, fuel is included in the Revenue Requirements while it is not in the second case. The options for dealing with fuel costs are discussed separately. ***The Commission has accepted option No. 2 and will allow a 100% pass-through of fuel costs.***

The average tariff that will be in effect from time to time shall be consistent with the following:

RR= OC +FC +GO

Where:

RR = Revenue Requirement
OC = Operating Cost
FC = Financing Cost
GO = A provision to recover or return the cost of Obligations imposed by government which were not known or anticipated at the tariff review.

The "Average Rate" then becomes the Revenue Requirement ($) divided by the forecast sales (kWh).

Average Rate = Revenue Requirement ($) / Sales (kWh)

Revenue Requirements

The utility's Revenue Requirement is calculated as the sum of its estimated costs of providing service, where a fair return is included as one of those costs. These forecasted funding levels must be sufficient to get the required work done without adversely impacting quality of service, or compromising reliability, customer service or safety; any disallowance resulting in deferral of projects or work activities must be carefully considered and weighed against these criteria.

The Revenue Requirement consists of the sum of Operating Costs and Financing

Costs required for providing electricity services.

RR = Operating Costs + Financing Costs

Where:

RR = Revenue Requirement Operating Costs = Costs of labour, non-generation fuel, ***Depreciation****, income taxes, deferred costs*
Financing Costs = Cost of capital which includes cost of debt and equity.

The critical exercise is to determine the forecast of the Revenue Requirements based on a sustainable and defensible estimate of the expenses for the base year. One approach is where the base year is the year for which the most recent published annual reports and audited financial statements are available and from which the Test Year (the forecasted year), representing a forecasted statement of expenses and costs that are known and measurable is derived.

In any event, in all cases, the expenses that are ultimately approved for inclusion will be those that are determined by the Commission to be prudent.

The non-fuel Revenue Requirement is developed based on a combination of demonstrated historic costs and forecast costs. The Fuel Revenue Requirement is by definition a 100% pass-through of actual cost and will change monthly according to an agreed-to formula.

The Revenue Requirement for the Base Rate is then:

Base Rate RR = NFOC + FC + GO + RF

Where:

RR = Revenue Requirement
NFOC = Non-Fuel operating Costs (this includes non-generation fuel)
FC = Financing Costs
GO = Government Obligations, and
RF = Regulatory Fees

DOMLEC has carried out and completed its proposed determination on the Revenue Requirement and Rate Base as part of this Tariff Review application, which was initiated in 2021, and has filed its application and schedules for Revenue Requirement and Rate Base with the Commission.

The completed Revenue Requirement and Rate Base with their supporting schedules are now available to the public and relevant stakeholders for review and comment for this consultation with consultation questions to facilitate the process.

Filing Requirements

The Determination provides the "Application for Approval of Rate Base and Application of the Revenue Requirement with supporting shared dataset as contained in Schedule A to D, to be met by DOMLEC in submitting its proposals to be considered in the Cost-of-Service Study.

Following a comprehensive review, the Commission has determined that DOMLEC has satisfied the filing requirement as contained in the '*Application for Approval of Rate Base and Revenue Requirements'*.

Expert Advice

DOMLEC's Expert Advice:

In support of its request for the Determination of the WACC, DOMLEC relies on a study carried out by Mr. William Vinhage, of Vinhage and Associates as the main piece of expert evidence. Mr. Vinhage's report *"Determination on Return on Equity (ROE) Range for Dominica Electricity Service Ltd."*, dated June 2023, which was included with the submission, seeks to assist the utility to establish, using the methodology prescribed in the Determination, the ROE element of the WACC. The Commission has noted that Vinhage and Associates which is a Florida based company, has a client list which includes Grenada Electricity Services Ltd (GRENLEC) from the Caribbean region and WRB Enterprises of Florida. Mr. Vinhage has over 20 years' experience of consultancy services and professional experience in the following areas:

- Strategic Planning & Analysis
- Project/Program Process & Impact Evaluations and Financial Analysis
- Statistical and Econometric Analysis and Forecasting
- Development of Financial/Operational Measurement and Tracking Systems
- Financial Planning, Budgeting & Analysis
- Competitive Intelligence & Benchmarking
- Development of Utility Revenue Requirements, Cost of Service and Tariff Design
- Process Design, Coordination, Mapping & Analysis

He has also had utility experience with Progress Energy and Tampa Electric Company.

The Commission is of the view that Mr. William Vinhage has the competencies to carry out the expert work on behalf of DOMLEC The Commission has not received any adverse comments on the qualifications and/or expertise of Mr. Vinhage, and it therefore confirms its initial conclusion on his competencies.

The IRC's Expert Advice:

As part of regulatory proceedings, the Commission engaged the services of a regulatory consultant with the necessary competencies to provide expert assistance in this rate making exercise.

Mrs. Lamis Aljounaidi, Regulatory Consultant from Paris Infrastructure Advisory (PIA), is a recognized expert in energy economics, tariff setting and financing. She has sixteen years of experience in energy infrastructure development and economics focused on renewables and networks. The regulatory consultant supported over fifty (50) projects through different development and financing stages including regulation, WACC calculations, pricing and market design for investment incentives. She has experience working in Dominica, by providing support to the regulator through the development of a Geothermal Independent Power Producer (2018-2020) during which she evaluated DOMLEC and the Dominica Geothermal Development Company (DGDC) Limited Power Purchase Agreement, conducted Electricity Demand Forecasts, and reviewed the Project's Financial Model.

The Commission advised participants that the Regulatory Consultant has the professional competence and expertise to assist the IRC in conducting a comprehensive review and analysis of DOMLEC's Application of Revenue Requirement and Rate Base and shared datasets containing schedules of expenditure and costs.

Summary of DOMLEC's Proposal

DOMLEC's conclusions are presented below:

- The request to consider 2023 Test Year represented by 6 months actual and 6 months forecast expenditure and associated costs.
- The proposed Operating Expenses of $53,955,801.00.
- The proposed Rate Base of $163,667,387.66.
- The disallowance of $1,392,263 from the Regulated Assets Base as amount not considered used and useful in the rate-making proceedings.
- The proposed Revenue Requirement of $66,959,323.04.
- The proposed fuel charge of $ 46,467,998.00.

The Commission's Considerations

Respondents commented at the public consultation the need to consider ECCB Inflation Rate as comparison to determine the Inflation Rate to be applied annually to DOMLEC's Revenue Requirement.

Respondents questioned the cost savings that could be realized in fuel costs, if DOMLEC had invested in the 4.5MW Solar Plant over the past years.

Some respondents commented that, given the introduction of full pass through of fuel costs to customers, whether some performance targets could be established to incentivize DOMLEC to improve efficiency and minimize costs. The Commission alluded that some key performance indicators will be implemented in the 3-year tariff period. These indicators will allow DOMLEC to improve the efficiency level and reduce operating and maintenance costs.

The Commission noted the comments from stakeholders and has taken them into account appropriately in its deliberations that followed as per each of the consultation questions raised for each proposed decision by the Commission.

The Commission also accepted other concerns expressed by the respondents during stakeholder engagements.

The Commission's Proposed Decisions, Consultation Questions and Respondents' Comments and Responses

PROPOSED DECISION 1

The Commission shall accept the application of Revenue Requirement and Rate Base submitted by DOMLEC to be used to set rates for the 3-year Tariff.

Consultation Question No 1:
Do respondents agree that it is not only in order but also prudent for the Commission to accept for its consideration the Application of the Revenue Requirement and Rate Base submitted by DOMLEC?

Respondents' Comments and Responses:

The backdrop of this question arises from the regulatory framework that mandates the Commission to review and approve a tariff for DOMLEC. It raises concerns whether stakeholders are of the view that the Commission acted contrary to the established methodology and followed due process; and established best practices to determine a reasonable Revenue Requirement for DOMLEC. A fair and reasonable Revenue Requirement will enable the company to operate effectively and efficiently under normal conditions.

The Revenue Requirement is the key component to derive the average tariff. DOMLEC is capital intensive in nature with major investments in generation, transmission and distribution assets among others. To provide reliable and efficient services, the onus is on DOMLEC to align Operating Expenses to Gross Plant in Service as far as possible.

The Commission's informed participants of its Regulatory Objective: "to *set a tariff which balances the interests of the consumers and investors alike where the investors have the opportunity to realize a fair return on investment while customers can expect an efficient, responsive and economical service in an environment where the rights of all stakeholders are preserved. The Commission will not guarantee a rate of return to the investors but will seek to create a regulatory environment where the incentives are such that the company through efficient operational practices and continual efficiency improvements will have the opportunity to achieve the desired rate of return during any tariff period."*

The *Tariff Decision Document* outlines the two (2) approaches to determine the Revenue Requirement. This statement is re-affirmed for emphasis:

> *There are basically two models for a tariff structure which could apply in the Dominica situation.*
>
> *1. A tariff which includes all the costs including the costs of fuel, based on a projected cost of fuel over the tariff period;*
>
> *or*
>
> *2. A two-part tariff comprising (i) a non-fuel base rate and (ii) a fuel charge, which fully recovers the cost of fuel (subject to efficiency factors) and no more.*

The Commission advised that *Option 2* has been accepted as the model for the tariff structure and will allow 100% pass through of fuel costs. This allows the Commission to factor in DOMLEC's proposed Revenue Requirement, the most recent data comprising 6 months actual and 6 months forecasted data. This included accounting data as per DOMLEC's shared datasets of actual values from January to June 2023 and forecasted data from July to December 2023.

The Commission explained that the purpose of determining the Rate Base is to develop an appropriate level of utility investments on which a reasonable Rate of Return can be earned.
The Rate Base items are the utility's investments in fixed assets that are considered ***used and useful during a tariff period***.

The *Tariff Regime Decision Document* outlines the Rate Base items to be considered in the computation: "*Fixed Capital Costs other methodology to determine the Rate Base. The Rate Base items include, Fixed Capital Costs, otherwise known as Electric Plant-in-Service, refer to assets in generation, transmission, distribution, shared services, information technology, capitalized software and corporate center; Adjustments, Working Capital and Deductions for Reserves."*

The Determination sets the method for reviewing fixed capital costs. This statement is repeated for emphasis

> *"The methodology for reviewing Fixed Capital Cost consists of determining the historic spending pattern and then adding any specific plant budget items for the Test Period. Some utilities use a project-by-project review of the actual capital work that needs to be performed. Capital expenditures are directly related to the forecasted plant in service levels if capital projects and blanket work orders are on schedule and on target."*

Stakeholders were informed that a comprehensive review and analysis of DOMLEC's shared datasets was conducted. These allowed the Commission to validate the accuracy of the values used in the computation of DOMLEC's proposed Revenue Requirement and Rate Base. Amounts were reconciled against schedules and associated worksheets. Adjustments were made to include productivity targets for operation, maintenance and administration expenses. An audit of DOMLEC's property, plants and equipment was also executed to determine the existence of a sample of Generation, Transmission, Distribution and Engineering assets among others fixed assets.

These statements dictate that the Commission is not in violation of its established rules and practices as mandated in the '*Tariff Regime for DOMLEC, Decision Document Ref 2009/004/D'*.

DOMLEC states that *"the Revenue Requirement culminates all the detailed work conducted from the Depreciation Study to the Weighted Average Cost of Capital Study and adds to the Operating, Maintenance and Administrative Expenses and Rate Base values.*

The Rate Base consists of net plants in service, which is the historical investments made in the plants minus all the accumulated depreciation made from the day they went into service to the end of the year. 'Construction Work in Progress', these are projects that are in the process of being undertaken but not yet in service. 'Working Capital Amounts' are basically cash and other working capital amounts on hand, to address both financial and operating needs. It consists primarily of cash, the net difference between accounts receivable and accounts payable and inventory, the principle amounts of working capital.

There are credits to the Rate Base, which are basically sources of cash that are available to the company at zero or very low costs. These include customers' deposits, capital grants and then deferment in income taxes."

Deferred Cost Estimate

Deferred Costs are costs that have been incurred by the utility but have not yet been recovered from ratepayers. These cost deferrals occur, as in determining Revenue Requirements, the estimates used could vary from actual costs. The utility can record these costs in a deferral account and once regulatory approval is obtained, these costs can be recovered from ratepayers through an adjustment in future rates. This treatment of deferred costs allows for rate stability and predictability. It is advisable that these costs be recovered as close as possible to the time they are incurred, that is usually within two to three years.

DOMLEC informed stakeholders that in the execution of the work undertaken, a 2023 Test-Year was considered and accepted by the Commission. DOMLEC's Operation, Maintenance and Administration Expenditure and Rate Base items include 6 months actuals from January to June 2023 and 6 months projected values from July to December 2023. DOMLEC's shared datasets were reviewed by the IRC's regulatory consultant and its team. Collaborative discussions were held between DOMLEC and the IRC to clarify certain line items. Adjustments were made to Operation, Maintenance and Administration Expenses and agreed upon. *Table 1.0 below refers.*

Table 1.0 below presents the summary of DOMLEC's Proposed Revenue Requirement and Rate Base:

Computation of DOMLEC's Rate Base		
Rate Filing for 2023 Test Year		
Description	**EC$**	**EC$**
Plant In Service/Fixed Capital		396,581,624.00
Reserve for Accumulated Depreciation		(219,719,153.84)
Net Plant in Service		176,862,470.16
Construction Work in Progress 51.7% Complete		7,835,278.50
Working Capital Allowance:		
Inventory	14,970,172.00	
Working Capital	4,705,138.00	19,675,310.00
Other Rate Base Items		
Customers Deposit	(3,730,478.00)	
Deferred Revenue	(15,773,704.00)	
Deferred Income Tax Liability	(21,201,589.00)	(40,705,771.00)
Rate Base		**163,667,287.00**

PROPOSED DECISION 2

DOMLEC's operating expenses of $53,955,801.00 based on the 2023 Test Year shall be factored in the determination of the Revenue Requirement for the 3-year Tariff.

Consultation Question No 2:

Do respondents consider as fair and reasonable the operating expenses of $53,955,801.00 proposed by DOMLEC as shown in the appendices to be factored in the determination of the Revenue Requirement for this Tariff Rate Review?
If not, please provide reasons?

Respondents' Comments and Responses:

The Commission informed stakeholders of the composition of Operating Costs of power companies represented by Operation, Maintenance and Administrative (OMA) Expenses incurred during the normal course of business activities. The Operating Costs include the cost of labour, fuel, depreciation, income taxes and certain deferred costs.

The *Tariff Regime Decision Document* dictates that *"Historical adjustments" are made to remove cyclical and unusual expenses incurred during that recorded period. These are normalized adjustments to the utility's historical data for costs incurred for non-recurring, unusual, or one-time expenditures for ratemaking purposes to reflect what should be the utility's normal and reasonable costs of doing business. An example of one-time expenditures to be removed would be costs of one-off specific studies that will not be continued or replicated in the future. The forecast then must account for "future adjustments" to incorporate anticipated cyclical and unusual activities and expenses that the utility plans in the forecasted period. Non-fuel operating costs are all prudently incurred costs which are not directly associated with investment in capital plant including OMA expenses."*

Typically, the utility's OMA expenses will remain relatively constant yearly, reflecting mainly the impact of inflation in current terms. Expenses associated with extraordinary events, such as the impact of natural disasters, are usually readily identifiable and should not be included in the forecasted costs.

The Tariff Decision Document outlines the elements of operating, maintenance and administrative costs. These are re-affirmed for emphasis:

- *"The typical elements* Operation, Maintenance and Administrative *(OMA) Expenses are:*

    - *Employee salaries, wages and benefits*
    - *Travel*
    - *Communication*
    - *Information technology*
    - *Office expenses*
    - *Public relations*
    - *Legal and professional*
    - *Equipment and line repair/maintenance*
    - *Insurance*
    - *Bank and credit card charges*
    - *Security*
    - *Commercial costs – meter reading, billing, etc.*
    - Other expenses "

There are other expenses, including depreciation, taxes and deferred costs.

The Commission noted the method of income tax to be charged to be utilities as set out in the Determination – *"If income taxes are charged to the utility, there are two ways to treat income taxes as an expense:*

i) reflect only income taxes payable during the period under review;

or

ii) reflect income taxes related to the period under review regardless of when they are paid.

The latter is the most prevalent approach among utilities. Tax expense is the composite of projected taxable income streams, book expenses, special tax deductions, and tax credits. It is calculated as stipulated under tax law, but it may be subject to different treatment for regulatory purposes as determined by the Commission.

DOMLEC informed stakeholders that the Operating Cost of $38,053,468.00 was derived from the 2023 Test-Year. Based on discussions, the Commission implemented an adjustment to be deducted from the Operating Costs. The adjustments are geared toward improving productivity in the system. This is represented by 1% productivity targets applied to total amounts for Operation, Maintenance and Administration Expenses.

The proposed Operating Costs were adjusted as follows:

Table 2.0- DOMLEC's Proposed Operating Expenses

Total Operating Expense for 2023 Test Year	**$EC**
Purchased Power Expense	61,083.00
Other Operation Maintenance & Administration	38,053,468.00
Less 1% IRC Productivity Adjustment	(473,444.00)
	37,580,024.00
Depreciation Expense	13,249,972.56
Income Taxes	3,064,107.00
Total Operating Expense	**53,955,186.56**

The Commission informed stakeholders that Operation, Maintenance and Administrative (OMA) Expenses form an integral component of the utility's Revenue Requirement. The increase in inflation has been driven by the rising costs in the supply chain. The pressure of increase in cost of goods reflects a dramatic change in business operation and consumers lifestyles since the early stage of the COVID Pandemic. To date, the prices of commodities are increasing at an alarming rate.

The Commission noted that inflation rates of 4.45% published by the Central Statistical Office of Dominica should be applied annually to DOMLEC's Operating Maintenance and Administrative Expenses for the 3-Year tariff period.

PROPOSED DECISION 3

Fuel Charge of $46,467,998.00 shall be considered a separate line item as full – pass through costs to customers for fuel used in the generation of energy.

Consultation Question No 3:
Do respondents consider as fair and reasonable the value for inclusion of DOMLEC's proposed fuel charge of $46,467,998.00 as full pass-through costs to customers used in the generation of energy?

Respondents' Comments and Responses:

The basis of the question relates to the implementation of the established *'Rules and Procedures'* stipulated in the *Tariff Regime Decision Document* for calculating fuel costs.

The document connotes "*The Commission sets, as its regulatory policy a full pass through to customer s of the cost of fuel having regards to and taking into account the cost of fuel utilized by DOMLEC, IPP costs, fuel efficiencies and prescribed system performances.*"

The Commission informed shareholders that *for this tariff exercise the **fuel surcharge** will be replaced by a **fuel charge** (adopting a complete pass-through mechanism) shown as a line item without putting fuel costs in the Base Revenue Requirement as part of the energy charge.*

DOMLEC mentioned that if fuel costs were factored in the Base Rate that the proposed Revenue Requirement would have been EC$113,429,455. This is why fuel costs are technically administered as a pass-through. Fuel cost is very sensitive to the price of diesel on the world market. That number can vary significantly yearly based on the movement in the oil market.

Some respondents held that if DOMLEC had pursued the development of the 4.5MW Solar-PV in the past, customers would have benefited from a reduction in the fuel charge by at least 30%.

The Commission informed that fuel charge reduction by at least 30% is not factual. Further the Government of Dominica's priority in terms of renewable energy is the geothermal project; and this is already on the way. It is a more formidable form of energy compared to solar and wind and can consistently meet the base load nationally. At some time in the future other forms of renewal will be part of the energy mix.

A respondent commented that DOMLEC should have aimed to opt for the hedging arrangement for the purchase of fuel. Hedging is a contract to buy the quantity of diesel at the stated price over the contractual period. DOMLEC could stand to benefit from a lower price of fuel at different intervals providing an increase in prices overtime. This arrangement would enable customers to realize a reduction in fuel surcharge.

PROPOSED DECISION 4

Construction Work-In-Progress of $7,835,279.00 and Inventory Balances of $14,412,432.00 shall be factored in the determination of the Rate Base.

Consultation Question No. 4

***Do respondents consider as fair and reasonable the values for inclusion of the historic costs of Utility's Plant (net of adjustments) of $396,581,624, Construction Work-In-Progress (CWIP) of $7,835,279.00 and Inventory balances of $14,412,432.00 as provided by DOMLEC be factored in the determination of Rate Base?* If not, please provide a reason.**

PROPOSED DECISION 5

The sum of $1,392,263.00 shall be allowed in the determination of the Regulated Assets Base as an amount not considered used and useful for this ratemaking exercise.

Consultation Question No. 5

Do respondents consider as reasonable that $1,392,263.00 be disallowed from the Regulatory Asset base as amounts not considered used and useful for this rate making exercise?
If not, please provide reasons.

Respondents' Comments and Responses:

The rationale for Consultation Questions 4 and 5 (above) and 6 (below) are based on the applicable *'Rules and Procedures'* as set out in the *Tariff Regime Decision Document* to determine the Revenue Requirement and average tariff.

Table 3.0 shows the list of assets to be disallowed from the Rate Base

Land at Tarrou	$	1,383,229.00
Land at Melville Hall	$	9,034.00
	$	**1,392,263.00**

The Commission alluded that only assets that are considered used and useful for the 3-Year tariff period should be recognized as part of the Regulated Assets Base. Stakeholders were informed that DOMLEC land at Tarrou is expected to be used for the development of 4.5 MW Solar Plant. Since the construction of the 10MW Geothermal Plant, the Solar PV project has been placed on hold. Accordingly, the land at Tarrou of $1,392,637 and Melville of $9,034 are not considered used and useful for the 3-Year tariff.

PROPOSED DECISION 6

The Rate base of $163,667,289.00 as per 2023 Test Year shall be applied in the determination of the Revenue Requirement for the 3- year tariff period.

Consultation Question No. 6

Do respondents agree to the methodology or approach used by DOMLEC that determines the proposed rate base of $163,667,289.00 as denoted in Table 2.0 above? If not, please provide reasons?

Respondents' Comments and Responses:

The Commission informed stakeholders that the Gross Plant in Service was adjusted to reflect the Regulated Asset Base. The Gross Plant in Service/ Property Plant and Equipment are used in the determination of DOMLEC's Rate Base.

DOMLEC held that a "key component in the determination of the rate base is derived from all the accounts balance under Gross Plant in Service. An average of the actual opening balances and the projected closing balance for 2023 and other adjustments were used to compute the Rate Base".

DOMLEC's projected Rate Base was determined as follows:

Table 4 – DOMLEC's Proposed Rate Base

Rate Base	EC$
Plant in Service/Fixed Capital	396,581,624.00
Reserve for Accumulated Depreciation	(219,719,153.84)
Net Plant in Service	176,862,470.16
Construction Work in Progress	7,835,278.50
Working Capital Allowance	19,675,309.89
Other Rate Base Items	(40,705,770.00)
Rate Base	**163,667,288.55**

Construction Work in Progress was projected over the 2023 Test-Year. The Working Capital amount was based on a 45-day payable assumption. DOMLEC added that inventory balances were high and were adjusted to reflect the impact of slow-moving items. After Hurricane Maria, many items were brought in and resulted in excessive supplies. These adjustments resulted in a reduction in the Rate Base from $171 million to $163.7 million.

The Commission reaffirmed that an audit of DOMLEC's Gross Plant in Service was conducted to ascertain the existence of use and useful Fixed Assets/ Regulated Asset Base. A follow-up partial audit for Transmission and Distribution Assets was also conducted during which the Commission was able to substantiate the existence of the Sample Network Assets. These assets were reconciled against DOMLEC's Geographic Information System (GIS). The audit reports were shared with DOMLEC. Moreover, a comprehensive review and analysis of DOMLEC's shared dataset was concluded.

The commission is of the view that DOMLEC's Rate Base for the 2023 Test-Year of $163,667,289.00 is reasonable.

PROPOSED DECISION 7

The Revenue Requirement of $66,959,323.04 shall be used to determine the average tariff for the 3-year tariff

Consultative Question No. 7

Do respondents consider the proposed Revenue Requirement of $66,959,323.04 determined by DOMLEC and illustrated in Table 3.0 above as reasonable and acceptable value that would enable DOMLEC to provide efficient and reliable services and at the same time achieve a fair return on investment? If not, provide reasons.

Respondents Comments and Responses:

The Regulatory Policy establishes the tariff framework as mandated in the *Tariff Regime for DOMLEC Decision Document Ref. 2009/04/D*. The statement is reaffirmed for emphasis:

> ***Revenue Requirements***
>
> *The Utility's Revenue Requirement is calculated as the sum of its estimated costs of providing service, where a fair return is included as one of those costs. These forecasted funding levels have to be sufficient to get the required work done without adversely impacting quality of service, or compromising reliability, customer service or safety: any disallowance resulting in deferral of projects or work activities must be carefully considered and weighed against these criteria.*
>
> **The Revenue Requirement consists of the sum of Operating Costs and Financing Costs required for providing electricity service.**
>
> ***RR = Operating Costs + Financing Costs***
>
> *Where:*
>
> *RR = Revenue requirement*
> *Operating Costs = Costs of labour, non-generation fuel,* ***depreciation****, income taxes, deferred costs*
> *Financing Costs = Cost of capital which includes cost of debt and equity*

The Commission explained that the Revenue Requirement is the total amount of money DOMLEC needs to collect from customers to meet normal operations, and also to achieve a reasonable return on investment. The Revenue Requirement will, therefore, be based on a test year which will consider all efficient non-fuel operating costs (including non-generation fuel costs), depreciation expenses, taxes and a fair return on investment

DOMLEC explained that the proposed Revenue Requirement of $66,959,323.04 was computed based on the 2023 Test-Year approved by the Commission. The adjustments made to Operating Expenditure as proposed by the Commission were factored in the Revenue Requirement.

Table 5. 0: Computation of DOMLEC's Revenue Requirements

COMPUTATION OF DOMLEC Proposed Revenue Requirement		
	Rate Filing for 2023 Test-Year	
Description		
Operating Costs:		**EC$**
Purchased Power Expense		61,083.03
Operating Expenses		37,580,024.08
Depreciation Expense		13,249,972.56
Income Taxes		3,064,721.81
Total Operating Expense		53,955,801.48
Finance Cost:		
Rate Base	163,667,289	
After-Tax Rate of Return	7.95%	
Pre-Tax Rate of Return	9.82%	
Financing Costs		13,003,521.56
Revenue Requirement		**66,959,323.04.00**

The Commission held that the applicable 'Rules and Procedures' as set out in the Tariff Regime Decision Document were utilized in the determination of the Revenue Requirement and Rate Base and that DOMLEC' s proposed Revenue Requirement of $66,959,323.04 is fair and reasonable under normal operating conditions.

Consultation Question No. 8

Do respondents agree that an inflation rate of 4.45% for 2023 as published by the Central Statistical Office in Dominica be used to forecast DOMLEC's Operation, Maintenance and Administrative expenses for the 3-year tariff period?

Respondents' Comments and Responses:

The background of this question is based on the rising cost of commodities and whether the proposed Revenue Requirement of $66,959,323.04 is sustainable to meet the Cost of Operation

The Commission notes that the regulatory environment prescribes that the utility should be encouraged to improve and maintain efficiency in critical areas to provide reliable service for its customers. An inflation rate should be included to determine the annual Revenue Requirement to cover the costs operation that will enable DOMLEC to operate effectively.

In the document, the Commission proposed an inflation rate of 4.45% for 2023 to be applied annually to DOMLEC's proposed Revenue Requirement. The inflation rate is based on the data published by the Central Statistical Office in the Commonwealth of Dominica. The Commission noted that the method to select inflation is stipulated in the *Tariff Regime Document*. This statement is stated for reference: -

The Tariff Determination connotes that: - *"Typically, the utility's OMA expenses will remain relatively constant from year to year reflecting primarily the impact of inflation in current terms.*

The rates for electric power shall consist of the following components to include among others:

A Non-Fuel Base Rate which is adjusted annually by the Inflation rate in Dominica as fixed by the Statistical Bureau of the Government of Dominica"

Some respondents were of the view that the Commission should review the inflation rate published by the Eastern Caribbean Central Bank (ECCB) for comparison. A respondent stated that the average inflation rate for 2023 was 3.8%. Respondents also proposed that the Commission should use the ECCB inflation rate if it is lower than that published by Central Statistical Division Office in Dominica.

Other stakeholders noted that the global trend shows that the inflation rates are declining.

The Commission noted the concerns expressed by stakeholders and reviewed the inflation rate as published on the ECCB's Website. The ECCB inflation rate for 2023 is 4%; however, the Commission's Regulatory Framework as set out in the Determination dictates that the Commission shall use the inflation rate *as published by Central Statistical Office in Dominica.*

Consultation Question No. 9

Do respondents have any other (related) comments or recommendations?

Respondents Comments and Responses:

Respondents did not provide any additional comments or recommendations.

Conclusion

The Commission is in general agreement with and will consider as part of the Regulated Asset Base the following asset categories:

- Buildings and Construction.
- Plant and machinery – Hydro and Thermal.
- Network.
- Tools and Equipment.
- Vehicles.
- Office Furniture.
- Office Equipment (Appliances).
- Software (Intangible Assets) Concluding Comments.

Reference is made to *Schedule 1, page 27 & 28*, of the Commission's *Rules of Practice and Procedures 2008; Decision Document Ref: 2008/004/D*:

"The views and analysis set out by the Commission in the said Consultative Document shall be for discussion purposes only and are not final. The purpose of the consultative document is to invite comments and evidence to be supplied, which may assist the Commission in the formulation, and, if need be, revision of its views. The Consultative document may include a series of questions the Commission is seeking comments on. If the Commission considers it appropriate, respondents may wish to address other aspects of the document for which the Commission has not prepared any specific question. If respondents may only wish to answer some of the questions posed – failure to provide answers to all questions will in no way reduce the considerations given to the response.

Following careful consideration of the responses and, if necessary, undertaking additional analysis and evidence gathering, the Commission shall publish a further document in which it provides comments on the responses. On major and/or complex issues, this may be another Consultative document with a view to inviting comments on matters not fully explored in the first Consultative document. Once the Commission has gathered all responses on all relevant aspects of the issue and has completed its analysis, it shall publish a decision/statement or policy position paper with the basis for its judgement….."

Therefore, in compliance with its core corporate values of professionalism, predictability, integrity, responsiveness, teamwork and transparency, the Commission is always guided by the principle to garner the widest possible range of views on the matter under consideration.

The Commission will explain the basis for its decisions and factors influencing its position in any given matter through its published documents.

~~ END OF DOCUMENT ~~