

THE IMPORTANCE OF TIMELY PRICE REVIEWS

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This document is a summary of the factors that affect the timeliness of price reviews and the advantages of conducting such reviews when they are due.

Summary
Document

PURPOSE OF THIS DOCUMENT

This paper will discuss the factors that impact the timeliness with which price reviews occur in Trinidad and Tobago, the implications of these delays for various stakeholders and the merits of conducting price reviews when they are due.

The Role of Price Reviews

Price reviews ensure that the service provider is able to earn revenues to cover the efficient costs of the daily operation and has sufficient funds to invest in new network infrastructure and replace aging assets. Price reviews also ensure that customers get appropriate price signals about the costs that the utility incurs to provide them with service. This should guide customers towards more efficient use and adopt conservative usage patterns.

A price review involves several broad stages. The first step involves establishing the service standards that the utility is expected to meet during the control period. The second step involves assessing costs to derive a revenue requirement for delivery of the desired level of service. The final step involves determining tariffs to meet the revenue requirement and the mechanism for controlling changes in the tariffs over the regulatory period.

ADVANTAGES OF CONDUCTING TIMELY PRICE REVIEWS

Stability in the Utility Industry

Timely price reviews are important to providing some level of stability for utility rates and to avoid rate shocks. A regulated utility may incur significant costs that may be uncertain and some are outside its control. In fulfilling its mandate to ensure the service provider recovers sufficient return to finance investments, the regulator will consider increases in costs when setting rates for the subsequent period. The RIC is also expected to set a rate that is fair and reasonable to the customer however, increases in efficient costs should be reflected in rates. The more time that elapses before a price review is conducted, the larger the potential increase in rates. The cumulative effect of a delayed price review on rates may be onerous to administer over a relatively short period of time.

Passing on Savings to Customers

Incentive regulation, which is utilized by the RIC, allows the utility to retain the efficiency gains that it makes for the duration of the regulatory control period and to utilize any gains as it sees fit. At the time of next price review these efficiency gains can be passed to customers in the form of lower prices/rates.

Adjustments of Standards of Service

During a price review, historical and forecast capital and operating costs are crucial factors to consider when considering the expected quality of service. The regulator is responsible for monitoring the performance of the utility and identifies areas of service improvements. It is important for price reviews to be on time so that utilities have sufficient funds to maintain levels of performance. Also, an overdue price review may undermine the regulator's efforts in setting standards, as additional revenue may be needed to fund improvements in quality of service.

Reduced Burden on the Government

The government of Trinidad and Tobago uses a combination of targeted and untargeted subsidies as a social policy measure in terms of making utility service more affordable to low-income citizens. Also, government subventions are used to assist utilities with covering its operational expenses. On time price reviews will ensure that utilities recover its costs from rates and will need to rely less on government support. Also, the establishment of new rates including lifeline tariffs, will help address affordability for low-income customers, which lessens the burden of government financing same. Government revenues can then be redirected into other sectors of the economy that may bring about increased growth and development.

Resource Conservation and Intergenerational Equity

Cost-reflective utility prices send signals to customers to use the utility service efficiently. As time elapses without adjusting prices to reflect changes in costs, prices may not send the kind of signals to consumers that may encourage efficient consumption. The more consumers pay attention to their consumption of utility services and make adjustments towards more prudent use, the less resources are required to deliver the service, which drives efficiency as well.

In the absence of on time reviews, it can be argued that the utility may defer needed investment or sustain losses, which in the case of state-owned and run utilities, is funded by either direct subventions or often government-backed debt. It can be argued that this violates the benefiter pays principle (concept of intergenerational equity). Hence, future customers may end up paying, at least in part, for services consumed by current customers for which those benefitting do not pay.

Maintains a Robust Regulator

From an external standpoint, price reviews are important for the regulator to fulfil its mandate and for the public to recognize this. Internally, when staff get involved in the work of a price review, significant knowledge transfer and learning-by-doing takes place.

THE LOCAL EXPERIENCE AND STRATEGIES ON THE WAY FORWARD

The timeliness of price reviews in Trinidad and Tobago has been affected by a number of factors, which are discussed further below.

Legislative Issue

In 2011, the RIC was well underway to complete its second review of rates for T&TEC when the process halted as a result of a question regarding the ability of the RIC to proceed with a rate review in the absence of subsidiary legislation. This issue has now been resolved and the price review is proceeding.

Availability of Data

The lack of timely data and poor quality data undermines the regulator's ability to make prudent decisions regarding the revenue requirement of the utility and tariff structure. The RIC recognized certain deficiencies in the preparation of information by the electric utility for regulatory decision making and recommended that a department be set up dedicated for this purpose, which was implemented several years ago. This has improved the timeliness with which information is received from the service provider and both regulator and utility continue to work towards improving the quality and reliability of data that is required for regulatory purposes.

The Availability of Resources

The price review exercise is time consuming and requires a certain level of expertise to be appropriately undertaken. Regulatory staff need to be properly trained and competent to carry out the exercise. Similarly, the utility must possess staff that is equipped to respond to data requests and analysis as prescribed by the regulator.

CONCLUSION

Various stakeholders are affected by the timeliness of a rate review exercise including the utility, its customers, the Government and the regulator.

The utility benefits when a rate review is conducted on time because they will be able to recover costs as incurred.

The customer will experience improvements in utility services at fair and reasonable rates.

The Government will be able to reduce its expenditure on subventions and subsidies.

The overall population may benefit from redirected government expenditure.

Staff development and public perception of the regulator will be enhanced when it conducts timely price reviews.

Responding to the Document

All persons wishing to comment on the main document are invited to submit their comments by March 30, 2018 by post, fax or e-mail to:

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