

Determining the Length of the Regulatory Control Period

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This document is a summary of the Length of the Regulatory Control Period consultative paper which is published for the information of all stakeholders, as part of the second Price Review for T&TEC.

Summary
Document

DETERMINING THE LENGTH OF THE PRICE CONTROL PERIOD

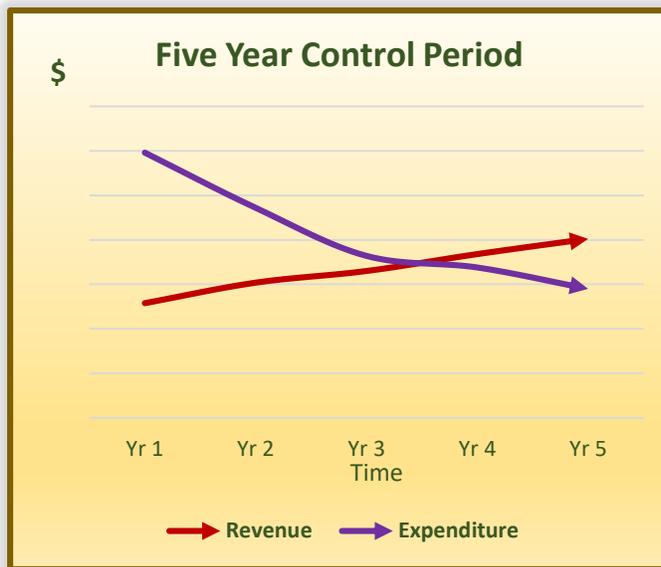
The price control period is the specified time over which the utility is expected to execute what has been set out in its business plan that was submitted to the regulator, over the relevant review period. The utility will be allowed to recover sufficient revenue over this period, such that it provides quality service to its customers and has the ability to charge rates that the regulator has determined is suitable, to meet its efficient costs.

A regulator must weigh the advantages of a longer-term price control over a shorter period when setting the length of this period, giving consideration to the particular utility sector and the local context. Ofgem, the gas and electricity transmission and distribution regulator in Great Britain, has moved to a longer price control period of 8 years, having previously utilized 5-years.

The table below captures some of the pros and cons of a longer period of price control.

ADVANTAGES	DISADVANTAGES
Promote value for money over the longer term	Risks of windfall profits / losses for the utility
Greater incentives to improve performance	Longer wait time before cost savings can be passed to customers
Lower administrative costs	Greater scope for prices to become out of line with costs
Lower regulatory risk	Possibility of price hikes / falls following price reviews
Encourages innovation and promote dynamic efficiency	Risks of reopening the price control
Greater stability for investment planning	Reduced adaptability of the regime

RIC'S EXPERIENCE WITH A FIVE-YEAR PRICE CONTROL



The RIC utilized a five-year control period for its first price review for T&TEC. The RIC's position then was that the five-year control period provided adequate opportunity for the service provider to earn profit by reducing expenditure through efficiency improvements. In essence, it represented the RIC's commitment to the service provider that it could keep any gains that it made for five years.

Overall the RIC considers that its forecasts over the first control period were reasonable and there was no cause to reopen the price controls that were in effect. T&TEC's financial performance improved over the period of the first price control and the length of the price control period posed no risks in this regard.

IS A SHORTER OR LONGER CONTROL PERIOD SUITABLE IN THE LOCAL CONTEXT

The RIC's own experience in regulating state-owned and controlled entities has demonstrated that such firms make little attempt to anticipate customer needs and to deliver value for money through innovative cost cutting efforts. Thus, the RIC is not inclined to believe that the benefits, in terms of innovation and value for money, resulting from longer term controls will materialize.

The RIC is also concerned that longer term controls also pose many of their own risks. For example, if outputs are not achieved and appropriate safeguards are not built into the regime

then recourse could be delayed for a longer period. Also, implementation of controls that are greater than five years will also require major changes to the legislative and regulatory framework, thereby increasing the complexity of the regulatory regime.

CONCLUSION

The RIC is constrained by its Act to a period of five years or shorter. Based on its consideration of the pros and cons of longer vs shorter price controls and its own legislation, the RIC considers that a five-year price control period strikes an appropriate balance between risks and the ability to undertake costs savings. The RIC therefore is inclined to continue the use of a five-year price control.

The RIC seeks comments on the appropriate length of the next regulatory period.

All persons wishing to comment on the need for annual price adjustments are invited to review the main document and submit their comments using any of the options provided.