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DETERMINATION ON FIJI ELECTRICITY AUTHORITY CHARGING CUSTOMERS FOR CAPITAL COSTS

DATE: 20 JUNE 2011

1. INTRODUCTION

1.0 The Fiji Electricity Authority ("FEA") was established, incorporated and constituted under the provisions of the Electricity Act 1996 and began operating from 1 August, 1996.

1.1 The Fiji Electricity Authority was established as a statutory body in 1966.

1.2 In 1966, FEA was tasked to generate and distribute electricity to the people of Fiji at the lowest possible cost, with a view of the overall development of the country. Its core function is to generate, transmit, transform, distribute and sell energy either in bulk or to individual customers in any part of Fiji.

1.3 The General Extension Policy of FEA was first introduced in 1971 as per the provisions of the Electricity Act 1966, Section 15(1) - Duty of the Authority to supply energy. The submission made by FEA on its "Rural Extension Policy" comprises of only "Part 2", and has no clear mention of its origin.

1.4 The General Extension Policy has been reviewed from time to time and the last review was carried out in May 2009 which became effective from 21 May, 2009 and similarly for the Rural Extension Policy, the last review was carried out in July 2008 which became effective on 15th July 2008 and is currently in force.

1.5 This Determination analyses the current practices of FEA charging its customers the capital costs by way of its General Extension Policy and the Rural Extension Policy and incorporates the complaints and submissions received by the Fiji Commerce Commission ("Commission").

2. LEGAL FRAMEWORK

The Commerce Commission Decree 2010 is the legalisation under which the Fiji Commerce Commission is to function.

The Section 4 on Interpretation has the following relevant definitions:-

- 'authority' :

"authority", in relation to the State, means-

(a) a body corporate established for a purpose of the State by or under a law of the State; or

(b) an incorporated company in which the State, or a body corporate referred to in paragraph (a), has a controlling interest;

The Fiji Electricity Authority ("FEA") was established as a statutory body in 1966 under Section 3 of the Electricity Act, *vide* Ordinance No. 20 of 1966 and is thus considered an authority under the Commerce Commission Decree 2010.

- 'goods' :

"goods" include any article, product or thing which is the subject of trade and commerce and includes -

(a) ships, aircraft and other vehicles;

(b) animals, including fish;

(c) minerals, trees and crops, whether on, under or attached to land or not;

(d) gas and electricity; and

(e) any component part of goods.

Electricity is thus categorized as 'goods' under the Commerce Commission Decree 2010.

- 'regulated industry' :

"regulated industry" means-

(a) an industry engaged in the supply of electricity, water, sewerage, post, broadcasting, telecommunications, ports or civil aviation services; or

(b) any other industry that is declared under Section 5 to be a regulated industry.

FEA is thus a 'regulated industry' under the Commerce Commission Decree 2010.

Under Section 15 (3) the Commission has the following functions in relation to regulated industries-

(a) the provision of advice to the Minister about proposed access agreements;

(b) the maintenance of a register of access agreements;

(c) the facilitation of negotiations about access to infrastructure facilities or services under access regimes;

(d) the arbitration of disputes about access to infrastructure facilities or services under access regimes;

- (e) if, under a law relating to a regulated industry, the referring authority **delegates to the Commission the power to impose**, modify or revoke conditions in respect of licences granted under that law - the imposition, modification and revocation of those conditions in accordance with the relevant delegation;

The functions of the Commission are covered under Section 15 of the Commerce Commission Decree 2010, the relevant provisions are as follows:-

Section 15: Functions and powers

(1) The Commission has the following functions-

- (h) to receive and consider complaints concerning matters affecting or likely to affect the interests of consumers or persons negotiating or considering the acquisition of goods or services as consumers and, if the Commission is of the opinion that such action is warranted, to investigate the complaints and take such action on behalf of the consumers or persons negotiating including legal proceedings in respect thereof as seems proper to the Commission;
- (i) to investigate fraudulent or deceptive practices in relation to matters that affect or are likely to affect the interests of consumers or persons negotiating or considering the acquisition of goods or services as consumers and to take such action in respect of the practices as seems proper to the Commission;
- (l) to keep under review commercial activities carried on and to collect information regarding such activities and the persons by whom they are carried on with a view to becoming aware of, and ascertaining the circumstances relating to.

FEA under the Electricity Act has power to borrow money in order to fund its capital requirements

Section 16. Power to borrow

(1) The Authority may, from time to time, with the approval of the Minister responsible for finance, borrow money by the issue of debentures or debenture stock or in whatsoever manner and subject to such terms, security, guarantee, mortgage, pledge or charge as may be so approved, for all or any of the following purposes:—

- (a) the provision of working capital;
- (b) for performing the functions of the Authority under this Act;
- (c) the acquisition of undertakings;
- (d) any other expenditure properly chargeable to capital account; and
- (e) any other purpose whatsoever which the Minister responsible for finance may specify.

(2) Subject to the conditions of any approval of the Minister responsible for finance, the Authority may make rules, not inconsistent with the provisions of this Act, to provide for the issue of debentures or debenture stock, or in connection with any other purpose mentioned in subsection (1) or which may be specified by the Minister

responsible for finance from time to time, and, in particular, for regulating the issue, transfer, redemption or other dealing with debentures or debenture stock.

(Amended by Legal Notice No. 112 of 1970.)

3. THE PROCESS

- 3.1 On 2 November, 2010, the Commission received a formal complaint from Wavi Island Resort on the issue of FEA charging high amount for supply of Electricity to Wavi Island in Savusavu. The complaint was to pay additional costs after being asked to pay a lower amount earlier. These charges were levied under FEA's general Extension Policy (confirmed by a letter from FEA dated 14 December, 2010). The Commission had commenced investigations on the issue as per the Commerce Commission Decree 2010.
- 3.2 On 1 March, 2011, the Commission received another complaint on the same issue. Fiji National University lodged a formal complaint to the Commission that FEA is asking Fiji National University to fund part of Capital Infrastructure to expand the grid.
- 3.3 The Commission sought FEA's response on the issue. The response from FEA was not to the Commission's satisfaction and this compelled the Commission to start a full investigation on the issues related to FEA's General Extensions Policy.
- 3.4 On 4th March, 2011 the Commission wrote to FEA seeking clarifications on the following issues:
 - 3.4.1 Current Grid (Extension) Policy and if the Grid Policy has been changed in last five (5) years , then all such Grid Policies that were in existence in the last 5 years.
 - 3.4.2 Detailed Breakdown of capital investments made in the last 5 years, including the contribution made by customers for each of the capital projects.
 - 3.4.3 Justification for asking customers to pay their Capital Cost and at the same time requiring them to pay market tariff rates.
 - 3.4.4 Justification for exercising ownership rights on an investment made by the consumers.
 - 3.4.5 Justification to deny the customers a return on the portion of the capital that the consumers have funded.
- 3.5 The Commission received the response from FEA to its letter dated 4 March, 2011 on 14 March. FEA provided responses to 3.4.1 and 3.4.2 above, and indicated that for items 3.4.3 to 3.4.5 it will need to formally presented/submitted in a face to face meeting between FEA CEO and Commerce Commission.
- 3.6 The Commission noting the request from FEA met the FEA team on 21 March, 2011. During the meeting FEA made a presentation to the Commission and also clarified issues surrounding the General Extensions Policy and FEA business in general.
- 3.7 On 4 March, 2011, the Commission also made a press statement on the issue and called for public submissions. The deadline for the public submission was set for 18 March, 2011.

- 3.8 After the deadline for public submissions had elapsed, the Commission summarized the major issues to form part of this determination. The Commission received a total of ten (10) submissions from business community, general consumers and non-trading organisations.
- 3.9 The Commission received further information and data from FEA on 28 March, 2011.
- 3.10 Noting the submissions received from the members of the public and FEA, the Commission then carried out its independent analysis to make this determination.
- 3.11 On 13th April 2011, the Commission made the draft determination.
- 3.12 On 27th April 2011, the Commission received a letter from the Mr Hasmukh Patel the CEO of FEA requesting to make submissions on the Rural Extension Policy. On 4th May 2011 the Commission requested FEA to make submissions on the Rural Extension Policy and any other policy which FEA has concerning capital cost.
- 3.13 On 10 May 2011 the Commission received the response from FEA regarding the Rural Extension Policy.
- 3.14 Noting the submissions received from the members of the public and FEA, the Commission then did its independent analysis in order to make the determination

4. Commission's Analysis of FEA's General Extensions Policy

In exercise of its powers under Section 15(1) of the Electricity Ordinance introduced the Consumer Extensions and Increased Maximum Demand Policy. Under this policy General Extension is defined as any overhead extension to the authority's existing distribution system which is not –

- (1) An extension which the authority in its absolute discretion has decided is in the interest of future electricity development or necessary for the efficiency of Authority's operations;
- (2) A rural extension

The salient features of the said policy are as follows:-

1. The General extensions will be constructed, owned and maintained by the authority.
2. The type of extension is determined after taking into account the anticipated load for a minimum period of 5 years without reinforcement.
3. The cost of general extension is defined as the estimated cost of an overhead extension from the Authority's nearest main supply point and shall include an additional mainline connection fee if FEA has provided an extension in the interest of future electricity development.

The table on page 6 of this determination summarizes the analysis of changes in FEA policy on General Extensions within an established supply area:-

POLICY	SALIENT FEATURES	REMARKS
24 September 1971	Person, Company or Body corporate seeking extension to pay:- 1. A non-refundable capital contribution of 75% of the cost of the extension. OR 2. An interest free advance of one hundred percent (100%) of the cost of extension.	1. No economic justification 2. No consultative process involved
1 January 1986	(First Revision)	Lost by FEA
28 January 1994	(Second Revision)	Lost by FEA
6 April 1995 (Third Revision)	1. An industrial or commercial consumer provides an irrevocable Deed of Guarantee, at no cost to the Authority, for one hundred percent (100%) of the cost of the extension. OR 2. An interest free refundable contribution of one hundred percent (100%) of the cost of extension. OR 3. A non-refundable capital contribution of 75% of the cost of the extension.	1. No economic justification for new policy 2. No economic justification for change from previous policy 3. No consultative process involved
15 March 2007 (Fourth Revision)	An industrial or commercial consumer provides :- 1. An irrevocable Deed of Guarantee, at no cost to the Authority, for one hundred percent (100%) of the cost of the extension <u>PLUS</u> a non-refundable cash contribution of thirty percent (30%) of the cost of the extension. OR 2. An interest free refundable contribution of one hundred percent (100%) of the cost of extension. OR 3. A non-refundable capital contribution of 75% of the cost of the extension.	1. No economic justification for new policy 2. No economic justification for change from previous policy 3. No consultative process involved
25 February 2008 (Fifth Revision)	An industrial or commercial consumer provides :- 1. An irrevocable Deed of Guarantee, at no cost to the Authority, for one hundred percent (100%) of the cost of the extension <u>PLUS</u> a non-refundable cash contribution of thirty percent (30%) of the cost of the extension. OR 2. An interest free refundable contribution of one hundred percent (100%) of the cost of extension. OR 3. A non-refundable capital contribution of 75% of the cost of the extension.	1. No economic justification for new policy 2. No economic justification for change from previous policy. 3. No consultative process involved
21 May 2009 (Sixth Revision)	1. An industrial or commercial consumer provides a non-refundable capital contribution of 75% of the cost of the extension for extensions costing up to \$ 1,000,000 OR the total costs of the extension less \$ 250,000 for projects costing over \$1, 000,000. I.e. FEA is contribution 25% of the cost of extension.	1. No economic justification for new policy 2. No economic justification for change from previous policy. 3. No consultative process involved

The Commission has further noted that:-

1. As per the FEA policy and absolute power, customers have no choice but to pay the cost of extensions.
2. While the customers pay for the grid and capital costs, FEA has the full ownership right over the capital infrastructure and thus any future returns accrue to FEA only;
3. While customers pay for the capital costs, they are also required to pay the full tariff rate as stipulated for all customers;
4. While customers are required to pay for the full capital costs, any additional customer that joins the grid do not have to pay any costs towards the already incurred capital costs. Furthermore, FEA enjoys any additional income arising out of these additional customers;
5. In case of FEA paying for 25% capital costs, in its books, FEA treats this as a fully funded investment and enjoys depreciation benefits on 100% on the cost of extension.
6. As per Fiji Revenue and Customs Authority (FRCA) the depreciation rate for transformers is 6% i.e. upon following the straight line depreciation, it will take 16.67 years to fully depreciate.
7. Under Section 16 of the Electricity Act, FEA has power to borrow money by issue of debentures or debenture stock, but FEA instead relies forcing its policy on consumers to fund such extensions.
8. FEA in November, 2010 was given a major increase in its tariff rates. The increase in tariff rate was what FEA had asked for. FEA's argument was that the existing tariff rates were placing them in a loss situation and the tariff sought will not only allow them to make profit, but will also allow them to invest in capital projects as well as renewable energy projects. Based on this, FEA's request for tariff increase up to 12 % was granted. For FEA to, then, get customers to pay for capital costs, over and above the market based tariff rates, is unethical and against basic accounting principles.
9. The rates of return on capital for utilities around the globe are no more than 10%. With the new tariff rates, FEA's rate of return on Capital is significantly higher than this international bench mark.
10. FEA, has so far, developed and passed a Grid Extension Policy which has no economic basis. Given the FEA is a monopoly provider of electricity in Fiji, such policy should not only have an economic basis, must also undergo consultation with the general public, in particular the key stakeholders. However, FEA has been able to levy these charges unilaterally because it has absolute power. FEA has abused its power and the Board has allowed FEA to abuse this power.

4. Commission's Analysis of FEA's Rural Extension Policy

Rural Area is generally defined as an area pertaining to the area outside the larger and moderate-sized cities and surrounding population concentrations. Generally characterized by farms, ranches, small towns, and unpopulated regions.

Definition of "Rural Extension" as per FEA Policy

A rural extension is defined as any extension of the Authority's distribution network which is totally or partly funded by the Government, Fiji Electricity Authority, a group of people or by an individual and is **not**:

- (a) A General Extension: or
- (b) An extension which the Authority in its absolute discretion has decided is in the interest of future electricity development or necessary for the efficiency of the Authority's operations.

The Rural Extension Policy was introduced pursuant to Electricity Act for Electrification of Rural Areas which as per FEA did not yield the required rate of return. The main objective of this policy was to help low income people in the rural areas.

As per the submissions by FEA, the following changes and/or developments have taken place with regard to the Rural Extension Policy:

- In 1995 FEA invested in Rural Electrification extension projects that gave an internal rate of return of 8%. For projects that was not commercially viable, FEA invested an appropriate amount so that a rate of 8 % is secured.
- In December 2002, there was a change in method of assessing rural expansion capital projects. To ensure commercial viability, FEA invested in those projects that yield a minimum rate of return 15% before tax.
- On 13 June 2008 the Department of Energy directed FEA that the rate of return required for RE projects be reduced from 10% post tax to 2.5% post tax. This would reduce the burden of capital expenditure costs on the consumers.
- On 17 June 2008 FEA complying with the directive proposed that the 'return be reduced to 2.5% post tax'.
- However, in July 2008 FEA indicated to 'Makereta' of Department of Energy that the new rate is 4% pre tax.
- Thus for those RE projects where the Rate of Return is equal to or is in excess of 4% were to be executed by FEA at no costs to the customers. However if the Rate of Return is less, then the customers have to contribute financially to come to rate of return at 4%.
- Additionally customers are subjected to Operations and Maintenance (O&M) charge of \$ 600/km

6. DETERMINATION

Based on the submissions received from various stakeholders and its own independent analysis, the Commission makes its Determination, applicable to both urban and rural areas, to be effective from 20 June, 2011 as follows:-

1. For households no capital costs ('Fee') is to be charged.
2. For loads other than households having monthly loads up to 5 KW units, no Fee is to be charged.
3. For monthly loads between 5 KW to 10KW units; 50% of the cost of extension may be charged as an interest free deposit which is to be fully refunded after 8 years of continuous usage.
4. For monthly loads above 10 KW, 100% of the cost of extension may be charged as an interest free deposit which is to be fully refunded after 8 years of continuous usage.

5. No Capital costs or Operations and Maintenance Charge is to be levied on customers seeking extension of grid in uneconomical geographical areas or rural areas.
 - a. However, FEA can borrow money under the options available in Section 16 of the Electricity Act or
 - b. Make a case to Government for support for capital infrastructure in the rural areas where such extension may provide low returns. This again is purely a transaction between Government and FEA and must not involve the community/firm/households/consumers in any way.
6. FEA, when undertaking valuation of capital costs for rural expansion, must get its costing vetted by an independent valuer to be appointed by either the Fiji Commerce Commission or Department of Energy.

Commissioners:

		
Dr Mahendra Reddy	Leba Mataitini	Sepeti Tagilala
Chairman	Commissioner	Commissioner
20/06/2011	20/06/2011	20/06/2011

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