

**Utilities
Regulatory
Authority**

Case Reference No: U-0018-14

**Commission Order establishing the Utilities (Restriction on Provision of Financial Support) Rules
2014**

The Commission has the duty to ensure that revenue collected from consumers for services provided by utilities are utilized prudently and in a way which does not prejudice the provision of safe, reliable and affordable regulated services and does promote the long term interests of consumers. The proper use of revenue by utilities plays a key role in tariff, investment into and condition of utility system and service received by consumers. Review of recent financial statements provided by the regulated utilities indicates that utilities are engaged in providing substantial financial assistance to third parties. It has therefore become necessary to address this issue so as to ensure that utility services are not jeopardized by inappropriate use of utility funds.

Powers and Functions of URA

Under the Utilities Regulatory Authority Act (**URA Act**) the Utilities Regulatory Authority (**URA**) is mandated to ensure the provision of safe, reliable and affordable regulated services including set maximum price charged to consumers and promote the long term interests of consumers including by ensuring that services are provided at least cost (Section 2 of the URA Act). Additionally, one of the primary functions of the URA is to investigate and act upon offences under the URA Act (Section 12(1)(e)).

In order for URA effectively to fulfil its functions, Section 13(1) of the URA Act empowers the URA to do all things that are necessary or convenient to be done for or in connection with the performance of its functions. URA's 'functions' include exercising the powers conferred by the URA Act. URA has the power (pursuant to Section 13(1A) of the URA Act) to require a utility to do those things expressly required by the provisions of the URA Act. This includes (and is not limited to) the following (Section 13(2) of the URA Act):

- (a) require a utility within a specified period, which is not less than 21 days to furnish the URA with specified information or documents, or information or documents of a specific kind, in the possession or control of the utility or any of its related entities relating to a regulated service or to corporate structure, accounts or finances of the utility; or
- (b) require a utility to confer with the URA as to the manner in which it carries on any specified activity in relation to a regulated service; or
- (c) do anything reasonably incidental to any of its powers.

Pursuant to Section 12(2) of the URA Act, the URA must exercise its functions in a way that considers the interests of, and impact on, consumers and utility businesses as well as Government policy.

Section 21(7) of the URA Act specifically prohibits a utility from engaging in any conduct that is misleading or deceptive, or is likely to mislead or deceive a consumer.

Concession contracts: Rights and obligations

The utilities are granted the right to provide water and electric service to consumers in Vanuatu. The rights are granted under a concession or management contract.

For the rights granted the utilities are authorized to collect revenues from the consumers for the services provided under tariff regime regulated by the URA.

In return for the revenues collected, the utility has the obligation to provide safe, reliable and affordable service to customers in their assigned service area.

Funds generated by Utilities

Revenue authorized by the URA in connection with the setting of prices and in turn collected by the utility provides for meeting all allowed operating expenses such as purchasing fuel, salaries and wages and other expenses prudently incurred. Revenue also allow for expenses to recover depreciation and a reasonable return on shareholder funds invested in the utility in connection with the provision of services.

A component of the utility annual profit may be disbursed to its owners in the form of dividends paid to its shareholders. The provisions for depreciation and amortization within the revenue collected are to be applied for replacement of assets as they exhaust their service lives, for system upgrades and for acquisition of new assets required to continue as an on-going business. Any shortfall in investment needs is made up by borrowing from the bank or a financial institution. Concessionaire owners may also inject further capital into the utility from left over profits less dividends in the form of retained earnings or provide fresh equity capital as needed. In their annual statutory accounts, utilities provide the statement of "Sources and Use of Funds" also called the Funds Flow statement.

Under the concession agreement the utility has obligation to maintain the system in good condition, make necessary investments to meet demand and make improvements to maintain an efficient utility system. Further, the utility must turn over the system to the Grantor (the Government) in good working order at the end of the concession.

Necessity of proper use of funds by Utilities

When the utility makes inadequate investments, the system is likely to deteriorate and eventually provide unsafe, unreliable and more expensive services to the consumers.

It is therefore critical that the utility make provision of adequate funds to make necessary investments in the utility system.

It is also important to understand that the utilities in Vanuatu are regulated electric or water utilities. Their activities should be restricted to the provision of utility services. Further they have an obligation to provide efficient, safe and reliable service at all times. The use of their funds, whether internally generated or

borrowed are to be strictly used for the utility purpose. A utility cannot spend on non-utility business without showing a compelling business necessity. Nor can the utility advance its utility funds to another entity- related or un-related. In other words, the regulated utility is not a financial institution, a bank or a lending institution. Thus any lending of funds, loan guarantees, assumptions or other purely financial transactions in way which puts at risk the provision of safe, reliable and affordable regulated services is a violation of the purpose and rights of the utilities under the concession agreements or management contract.

Findings

- Certain utilities are engaged in transactions such as advancing sizeable loans to its affiliates, non-utility businesses, and management employees.
- The Commission takes this issue seriously as such lending of funds is a high risk activity putting utility funds at risk which could seriously jeopardize the provision of essential utility services, whether in respect to extending services to new consumers, meeting customer growth, network expansion, etc.
- Not knowing under what circumstances the loans are advanced, no risks can be assessed as to the security of the return of those funds advanced to third parties.

Therefore the Commission must take an immediate action to address and monitor this practice of the regulated utilities advancing financial assistance (loans or otherwise), directly or indirectly, to third parties. The Commission must ensure scrutiny, place certain restrictions and require regular disclosure to ensure that utility services are not jeopardized by inappropriate and reckless use of utility funds.

Commission Order

The URA Commission hereby establishes the following Utilities (Restriction on Provision of Financial Support) Rules 2014 (**Rules**):

1. **Applicability:** The Rules apply to a utility (other than a State owned entity) granted a concession or management contract under the Electricity Supply Act or Water Supply Act (**Concessionaire**).
2. **Restricted Financial Support:**
 - 2.1 **'Restricted Financial Support'** means, directly or indirectly, documented or undocumented:
 - (a) loan or other financial assistance provided by a Concessionaire to a person exceeding the value 100,000 vuv in one or more transaction;
 - (b) guarantee, collateral, pledge given/assumed by a Concessionaire with regard to a loan or financial obligation of a person other than the said Concessionaire;
 - (c) encumbrance on behalf of a person on the assets forming part of the concession other than in respect of the regulated service(s), or
 - (d) use of concession assets or facilities forming part of the concession (including vehicles, office buildings, IT services, etc.) for any business or activities other than in respect of the regulated service(s), by the Concessionaire or any other person.

It is clarified that Restricted Financial Support does not include distribution by the Concessionaire of proceeds from its net income generated from regulated service(s). Advance payment for goods and services sought by the Concessionaire in the ordinary course of business in respect of the regulated service(s) are not regulated by the Rules.

- 2.2 A Concessionaire shall not provide a Restricted Financial Support to any person.
- 2.3 In exceptional circumstances the Concessionaire may approach the URA and request for its approval in order to be able to provide a Restricted Financial Support to a person. The URA may grant the approval subject to such terms and conditions it considers appropriate.
- 2.4 Provision of Restricted Financial Support by the Concessionaire, subject to Rules 2.2 and 2.3, shall be consistent with applicable laws of Vanuatu and applicable financial and accounting standards.

3. **Financial support given prior to coming into effect of the Rules:**

- 3.1 If a Concessionaire has provided financial support to or on behalf of another person (including those listed under Rule 2.1) prior to the coming into effect of the Rules and there is an outstanding balance or encumbrance, the Concessionaire shall inform the URA in writing and submit all documents executed in relation thereto immediately, but no later than 45 (forty five) days of the Rules coming into effect.
- 3.2 Upon review of the financial support referred to in Rule 3.1, and amounting to a Restricted Financial Support, the URA may order to accelerate the repayment, cancel the guarantees or obligations assumed by the Concessionaire. URA shall give due regard to the impact of such action on the Concessionaire's overall financial position in determining the necessary action.
- 3.3 The Concessionaire shall seek URA approval prior to any change in the terms or conditions of the Restricted Financial Support advanced including transferring, granting waiver or relief, etc.

4. **Reporting Requirement:**

- 4.1 Without limiting Rules 2 and 3.3, the Concessionaire shall inform the URA in writing about the execution of or change in financial support, including if a financial support is paid-off, satisfied, transferred, waived, etc., within 30 (thirty) days of such execution or change. The notice shall be supported by documentation entered into by the Concessionaire reflecting such execution or change.
- 4.2 The URA may ask for additional information or documents or clarifications for reviewing the information provided under these Rules. The Concessionaire shall provide the requested information within the timeline prescribed by the URA (which shall be in accordance with the URA Act).

5. **Effective Date:** The Rules come into effect immediately.

6. **Notice of Grievance:**

- 6.1 If a utility is aggrieved by this Order, it may request the Commission to reconsider the decision on issues aggrieved upon (**Notice of Grievance**). A Notice of Grievance must be submitted within 30 (thirty) days of the Order and be addressed to the Commission.

6.2 The Notice of Grievance shall contain:

- The issue or issues being contested
- A detailed description of any facts or matters supporting the grievance
- Copies of any documents supporting the grievance
- A detailed description of any alleged error of law

6.3 The Notice of Grievance may be:

delivered in person at the: Office of the Utilities Regulatory Authority VNPF Compound Corner Pierre Lamy & Andre Ballande Street Port Vila, Vanuatu	mailed to: Case U-0018-14 Utilities Regulatory Authority P.M.B 9093 Port Vila Vanuatu	addressed to: Hasso Bhatia, PhD Chief Executive Officer Utilities Regulatory Authority
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6.4 If the Commission receives a timely Notice of Grievance, it shall conduct a review in accordance with the Section 27 of the URA Act. If upon review the Commission determines that the grievance is justified, then it shall revoke or amend the Order on the matter complained of.

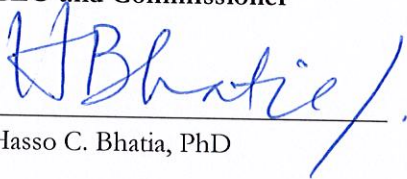
Chairman



Johnson Naviti Matarulapa Marakipule

Date: 22/07/14

CEO and Commissioner



Hasso C. Bhatia, PhD

Date: 22/07/14

Executive Commissioner



John Alilee

Date: 22/07/14

Seal of the Utilities Regulatory Authority



