GOUVERNEMENT DE LA REPUBLIQUE DU VANUATU

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GOVERNMENT OF THE REPUBLIC OF VANUATU

Utilities Regulatory Authority
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Press Conference - September 26, 2011

Revision of Electricity Prices in Vanuatu

A Step Forward for Vanuatu's Economic Reform Efforts

Commission Statement

The Utilities Regulatory Authority, or URA, was set up by the Government of Vanuatu in 2008 to **regulate electricity and water services**. It was established under its Act, which sets out its objectives and functions.

The primary objectives of the Authority are

- to ensure that utilities such as **UNELCO GDF SUEZ and VUI Pernix** provide **reliable, safe and affordable services** to customers;
- to **maximise access** to these services in and outside the concession areas;
- and to protect the **long term interests** of consumers.

It performs these actions in a **transparent fashion and acts independent** of Government, which it advices on matters related to electricity and water. In addition to this, the Authority is also responsible for managing customer disputes.

Today we aim to provide you with:

- **'independent and impartial' advice and information** about the electricity sector in Vanuatu, and
- an update about **current developments in tariffs**, **investments and issues** relating to the electricity sector across the country.

The Authority's aim is to protect the long term interests of consumers. That said, it must consider the interests of all stakeholders, specifically government policy in delivering services to the public.

We will provide an update on the facts relating to the new tariff applied in Luganville, Malekula, Port Vila and Tanna.

The Authority is well aware that energy costs are a significant factor in Vanuatu's economic development. In 2009 the Government, concerned over high electricity prices, requested the Authority to undertake a full tariff review and assessment of UNELCO's operations in Luganville, Malekula, Port Vila and Tanna.

The Authority initiated a transparent and consultative process, involving all relevant stakeholders, including UNELCO, the Government and the public, which led to agreements at each step along the process.

The review resulted in an appropriate methodology to set a tariff, which allows for operations and maintenance costs as well as a reasonable rate of return on investments for UNELCO.

In its final decision in May 2010 the **Authority set out a major reduction in the electricity tariff** for small domestic customers and an average price reduction of around 6.8 percent for most electricity customers.

The **Council of Ministers endorsed the Authority's decision** and expressed its desire that UNELCO agree to implement the new tariff. **UNELCO did not accept** the position of the Council of Ministers and proposed an alternative **higher level of tariff instead**. Subsequently, the Government entered into an **arbitration process** for the dispute to be settled by an **independent arbitration panel**.

The **Authority acted on behalf of the Government and defended its decision** during the arbitration process. In April 2011 the Panel of Arbitrators made their award, detailing the following points:

- In relation to the issue of the application of the Capital Asset Pricing Model (CAPM) formula applied by the Authority and disputed by UNELCO –
  - The **panel reaffirmed** the Authority's position that a CAPM model is appropriate for determining UNELCO's rate of a reasonable return; and
  - Determined values for a series of disputed inputs for the CAPM model.
- In relation to the issue of removing Luganville concession from the arbitration process –
  - The **panel reaffirmed** the Authority's position that for the purposes of the arbitration, the tariff awarded would include the operations of the Luganville concession.
- In relation to issue of passing through to customers benefits of the Wind Farm both retrospectively and in the new tariff over the next 5 years –
  - The panel determined that past wind farm benefits **could not be clawed back** from UNELCO to the detriment of customers; and
  - Noted the undisputed fact that **future benefits are passed on to customers** through the tariff going forward.
- In relation to the price adjustment formula –
  - The panel determined that, lacking other methods of determining a fair and reasonable price for coconut oil supplied by UNELCO subsidiary, **costs will be tied to the diesel price**.
- The award was factored in the Authority's tariff review financial model and resulted in –
  - A base price of 46.65 Vatu;
  - A modified monthly price adjustment formula which factors in fuel costs, use of renewables and variations of other indicators;
  - A tariff structure as outlined in the Authority's Final Decision May 2010; and
  - Resulting in an approximate average tariff decrease of 4.7 percent (compared to the Authority's initial decision of 6.8 percent) and reductions for low consumption customers (those customers under 60kWh per month) of more than 40 percent.
- The tariff review achieved the following positive outcomes for customers and the Government alike:

    - For the first time, **a reduced tariff determined under an independent review**
    - An appropriate **financial model** to apply to Vanuatu in future reviews; and
    - **Benefits are transparently passed through to the customer**
- The award was implemented by UNELCO as of 1 May 2011 in Malkula, Port Vila and Tanna.

The final award will be made public by the Authority in print and on its website. However, we would like to **highlight**, how some of the points discussed thus far **directly impact customers**, particularly the application of the financial model, the wind farm benefits and coconut oil prices.

The application of a Capital Asset Pricing Model (or CAP M) ensures that beyond the actual costs, UNELCO is rewarded with a return on investments at a **fair and reasonable level**. This ensures that UNELCO maintains investments in network infrastructure, which is paid by customers through the tariff. It also ensures that UNELCO does not benefit from profits beyond fair returns for those investments. The Authority has provided for almost **3.5 Billion Vatu** for investments over 5 years, which is **already being paid for by customers** through the tariff. The Authority has made a point in its tariff decision that only investments included in an approved investment plan will be allowed to be passed through to customers. Should such a plan not meet defined requirements, the **Authority will make a claim for customer moneys to be clawed back at the next review.**

The arbitration panel also dealt with the topic of renewable energy sources, in particular the wind farm in Port Vila, which **generates electricity at a lower cost** compared to diesel. The panel concluded that it could **not award past benefits** earned from the lower cost wind farm since its establishment and up to 30 April 2011. Thus, up until recently, benefits of operating the wind farm were **not passed on by UNELCO, to the detriment of its customers**. However, from 1st of May 2011, as determined under the Authority's decision, benefits from renewable generation sources, including the wind farm, are **passed on through the tariff to the benefit of customers going forward**.

In regard to coconut oil prices, the Authority, in its decision, voiced concern over **UNELCO procuring coconut oil from a subsidiary** at costs not comparable to market prices. The Authority voiced its concern once again with the arbitration panel, however, lacking other methods of determining a fair and reasonable price for coconut oil supplied by UNELCO subsidiaries, the price **will now be tied to the diesel price**. This means that benefits of purchasing locally sourced coconut oil at low prices are not shared with customers. The Authority will monitor developments closely in an attempt to devise a fair methodology to **determine the real cost of coconut oil in Vanuatu and ensure that any benefits are passed on in the future**.

With a tariff decision now in place, the Authority has set the base tariff for electricity; however the actual price for each unit of electricity (in kilo-Watt-hours) is not necessarily charged to all customers. In its decision, the Authority also defined a **so-called tariff structure** which sets out how much of the base price applies to different tariffs **categories, or plans, from which customers can choose from**.

Continuing its mandate of ensuring affordable access to electricity, the Authority has, since the decision, **initiated an evaluation of the various tariff categories, or plans**, that customers may sign up for. These categories can have a **significant influence on customer bills**.

The evaluation of tariff categories for customers in Malekula, Port Vila, and Tanna is currently ongoing, however is being **delayed due to UNELCO's refusal** to provide required information.

In the meantime **Luganville customers are benefiting** since January 1 2011 from the Authority's

original 6.8% reduction of the base tariff, 48% for small customers. The Authority, aided by cooperation of VUI, has also put in place a **revised tariff structure which streamlines the various plan options** to the benefit of customers. The Authority understands that this has been **well received by the majority of customers** in Luganville.

In summary, following the Authority's tariff review process, an independent arbitration panel affirmed the Government's position that the **Authority's methodology for determining costs and a reasonable return for UNELCO were justified**. With the help of experts the panel also took into account economic figures to set the appropriate level for UNELCO's return on investments.

Key points of the Authority's decision, for example passing on the benefits of renewable energy sources to customers **were affirmed**, while some questions, such as reasonable prices of coconut oil, remained **to be dealt with in the future**.

We note that for the **first time in the history of Vanuatu**, the electricity base prices across the country has been reduced as a result of the Authority's transparent and independent review. This positive outcome **reaffirms the Government's initiative** to provide a regulatory framework that has the **long term interest of consumers** at its forefront and **encourages sustainable economic development for Vanuatu.**

Thank You.

About the Authority

The Utilities Regulatory Authority (URA) was set up under the *Utilities Regulatory Authority Act No. 11 of 2007*. It acts independently of the Government and its primary purpose is to increase access to safe, reliable and affordable electricity and water services, and to protect the long term interests of consumers throughout Vanuatu. In the electricity sector, the Authority monitors the concessions operated by UNELCO GDF SUEZ in Malekula, Port Vila and Tanna; and Vanuatu Utilities and Infrastructure Ltd (VUI) in Luganville. In addition, the Authority manages consumer disputes and advises the Government on matters related to electricity and water. It also renegotiates tariffs under the rules of the Concessions Agreements and relevant legislation.

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About UNELCO
Union Electrique du Vanuatu Limited (UNELCO) is a subsidiary of GDF SUEZ. It operates the electricity concessions for Port Vila, Malekula and Tanna. It has operated in Vanuatu since 1939.

About VUI
Vanuatu Utilities and Infrastructure Limited (VUI) is a subsidiary of Pernix Group, Inc. Pernix Group's Power Operations and Management Services (O&M) division provides an integrated scope of services to maintain and manage all aspects of power operations. VUI has operated Luganville's electricity concession since 1st January 2011.