



Georgian National Energy and Water Regulatory Commission

Tariff Regulation

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Legal framework

- **The tariff influencing authority of the Commission is defined by the Law of Georgia on Electric Energy and Natural Gas**
- **Commission sets the tariffs in accordance with the methodologies approved by the Commission in 1998**
- **Methodology is based on the full-cost principle**

Basic principles of tariff regulation

- **Methodologically tariff setting is based on full-cost (FC) principle;**
- **Methodology allows utility recovering economically reasonable costs;**
- **Supports growth of utility's financial results;**
- **Protects consumers from monopoly pricing, especially in the fields where there is no competitive market;**
- **Reflects various costs for the services provided to various categories of consumers.**

Basic principles of tariff regulation

- **Tariff shall ensure financial viability of regulated utility;**
- **All justified costs shall be compensated;**
- **Tariff regulation shall create incentives for efficient performance for the utility;**
- **Tariff regulation shall be transparent;**

Revenue Requirement (RR) Calculation

- Revenue Requirement (RR) includes following components:
- Operational expenses;
- Depreciation;
- Taxes;
- Profit.

Revenue Requirement (RR) Calculation

- **Operational expenses, including repair;**
 - **Services provided to other organisations;**
 - **Administrative expenses, including;**
 - **Payroll expenses**
- **Various expenses;**
 - **Normal network losses;**
 - **Other**

Revenue Requirement (RR) Calculation

- **depreciation is non-monetary cost, which is reflected in the financial statement and reduces the asset price;**
- **The investment expenses related to the asset are distributed through wear over the entire life period the asset;**
- **Tariff includes the taxes set out in the respective legislation.**

Revenue Requirement (RR) Calculation

- **Profit norm (WACC) – ensures receiving profit by the utility, and this profit is defined as weighted average costs of capital. Or, in other words, profit norm multiplied by equity plus interest rate multiplied by the cost of the loan;**
- **Cost of equity: share financed by the investor's own capital;**
- **Cost of loan: volume of loan, which is used for financing part of company's activities.**

Revenue Requirement (RR) Calculation

Cost of capital can also be determined by Capital Asset Pricing Model (CAPM).

- **Profit norm is defined for the equity;**
- **Defining profit norms is usually done through definition of risk factors;**
- **The regulated tariff base includes only the assets that are directly linked with the regulated activity**

Tariff Setting

- **Commission defines tariffs for power generation, transmission, dispatch, distribution, transit, import consumption, as well as for services of system commercial operator and the mandatory capacities and capacity reserves to be purchased by system commercial operator;**
- **tariffs for transportation, distribution and consumption of natural gas;**
- **Water supply tariffs;**
- **Import tariffs are set on basis on import agreements;**
- **For the newly constructed power stations, product of which is subject to full or partial purchase under standard act adopted by the ministry, the long-term tariffs for power to be mandatorily purchased by the commercial system operator are set;**
- **For the reserve sources the two-rate tariffs are set.**

Tariff types

Commission regulates the following tariff types:

- **Generation**
- **Transmission**
- **Dispatching**
- **Distribution**
- **Consumer**
- **Import**
- **Transit**
- **Commercial operators service**
- **System capacity reserve**

Tariff Types

Import
Capped

Transmission
Fixed

Distribution
Fixed (differentiated by the voltages)

Generation	
Fixed	Capped

Dispatching
Fixed

Consumer		
Fixed (differentiated by the voltages)		
35-110 KV	6-10 KV	0,4 KV



Block tariff

Tariff setting procedures

- **Commission considers Tariff Application submitted by the Licensee**
- **Application forms are approved by the Commission**
- **Tariff Application shall be accompanied by audit and financial information**
- **Tariff enters into force after 15 days from the day of its publishing**

Tariff setting

tariff = revenue requirement / power volume

Revenue requirement:

- 1. Depreciation**
- 2. Operation expenses**
 - repair
 - externalities
 - raw materials and supplies
 - payroll expenses
 - fuel for power generation
 - losses
- 3. Taxes**
 - Profit tax
 - Property tax
 - natural resources use tax
 - land tax
- 4. equity return**

Generation and import

1. **The small capacity HPPs are regulated since September 1, 2006 (below 13 MW)**

Georgia has 38 small HPPs. Commission defines tariffs for 17 HPPs – 2 of them have the fixed tariff, while 15 HPPs have tariff cap

2. **Georgia has 3 thermal PPs**
 - 2.1 **power generation tariff (capped).**
two component tariff:
 - **system capacity reserve tariff;**
 - **used capacity power generation tariff.**

Wholesale Tariffs

The wholesale power tariffs for the electricity purchased by direct consumers and distribution companies are determined by direct agreements executed by them with power plants and importers and transmission-dispatching licensees

■ In order to ensure energy security of the country, each wholesale power buyer (distribution companies and direct consumers) are obliged to retain the reserve capacities in volume of 10% of their consumption. The reserve capacity tariff for power distribution companies is included into their wholesale power purchase tariff.

Dispatching Tariffs

Georgian State Electricity System Ltd. is one legal person, which is involved in two licensed activities – transmission and dispatching

- **Costs are allocated by activities**
- **Dispatching tariff is calculated as follows: demanded revenues divided by power dispatched through system minus standard power losses**

Dispatching tariff – 0.15 Tetris/kWh

Distribution Licensees

There are three distribution licensees in Georgia

- **Tbilisi – JSC Telasi – privatised in 1998**
- **Regions – JSC Energo-Pro Georgia – privatised in 2007**
- **Kakheti – JSC Kakhetis Energodistribucia – under bankruptcy proceedings since 2005**

Natural Gas Tariffs Regulated by the Commission

■ **Authority of the Commission in tariff setting;**

*** By the Law of Georgia on Electric Energy and Natural Gas**
In the natural gas sector the Commission regulates the following tariffs:

- 1. Marginal supply tariffs only for those retail customers, who are receiving natural gas through distribution network**
- 2. Transportation tariff**
- 3. Distribution tariffs**
- 4. Marginal consumption tariffs**

*** Is not regulated by the commission (free prices):**

- 1. Tariffs for gas sold in automobile filling stations (was regulated until 2006)**
- 2. Supply (wholesale tariffs)**

Natural Gas Supply Tariffs

- **In 2007, Georgia started importing natural gas from Azerbaijan (in addition to Russia) for much lower prices than it was available from Russia (USD 62.4 and USD 120)**
- **In order to avoid the sharp rise in prices for the consumers, based on the 2007 Natural Gas Balance approved by the Ministry and applications from the gas supply companies, the Commission set weighted average price of Russian and Azeri gas in the amount of USD 167.0/1,000 cubic meters and the rise for the customers made just 52%**
- **The gas supply tariffs were set in 2007 and the customers connected to the gas distribution network are still supplied with the same tariffs**

Prices and Dynamics of the Imported Natural Gas in Georgia 1999-2008

#	Year	Source of Natural Gas Import	Price US\$ /1,000m3	Note
1	1999	Russia	60.0	
2	2000	Russia	40.0	
3	2001	Russia	50.0	
4	2002	Russia	56.0	
5	2003	Russia	60.0	
6	2004	Russia	60.0	
7	2005	Russia	60.0	
8	2006	Russia	110.0	
9	2007	Russia Shakhdeniz (Azerbaijan) Azerbaijan	235.0 62.4 120.0	The weighted average price was set for the suppliers 167,0 \$ /1000m3
10	2008	Not regulated by the Commission		

Natural Gas Transportation Tariffs

- **Capacity of natural gas transportation system and dynamics of gas volumes actually imported and transported in Georgia**
- *** Capacity of transportation systems makes 20.0 bln m³**
- *** Natural gas consumption reached its maximum by the end of 1980-ies and made 6.7 bln cubic meters then**
- *** In 2007 Georgia consumed 1.7 bln cubic meters and transited 2.0 cubic meters**

- **Natural gas transportation tariff**
- *** Transportation tariff is the same for all customers (except for thermal PPs) and makes GEL16.62/1,000 cubic meters, including VAT**

- **Natural gas transit**
- *** gas is transited to Republic of Armenia**
- *** Transit tariff is not regulated by the Commission**
- *** Transit revenues are taken into account in transportation tariff setting**

Natural Gas Distribution Tariffs

- **Application for tariff procedures and requirements**
 - * **Within the three days from submission of tariff application to the Commission by the Licensee, the respective service of Commission checks accuracy and completeness of the documentation. If the documentation is complete, the administrative application proceedings are announced open, if it is incomplete, the Licensee receives request for adding the respective documents**
 - * **The proposals prepared by the Commission apparatus is then considered on the Commission Meeting**
 - * **Commission shall come up with the decision not later then 150 days after submission of the proposal.**
 - * **The proposal submitted by the licensee shall be justified and accompanied by the audit approved financial statement for the past regulated period, as well as by any other additional information requested by the Commission**
- **Structure of natural gas distribution tariffs – tariff application forms, norms of basic gas distribution costs and net profit**
 - * **Depreciation norm _ determined on basis of tax code**
 - * **Salary rates _ by the categories of towns and districts**
 - * **repair costs _ up to 5% of the fixed assets**
 - * **At this stage the Commission defined net profit ceiling as 8% of the fixed assets**

Natural Gas Distribution Tariffs

- **The normal losses in gas distribution tariffs and their share**
 - * **The average share of normal losses in Kaztransgaz-Tbilisi tariffs makes 9%, while for the other companies the same indicator is limited by 5%**
 - * **The rise of gas import and supply tariffs in 2006-2007 significantly increased (almost doubled) the share of normal losses in distribution tariffs**

Differentiation of natural gas distribution tariffs by customer categories (pressure)

- * **According to the used methodology, the gas distribution tariffs are set for the high, medium and low pressure consumers**
 - * **So far, the Commission has set tariffs for 67 distribution licensees; for 21 of them the tariffs are differentiated (by the pressure); the remaining 46 companies have only low pressure (residual) customers**
 - * **Following distribution tariffs (including VAT) are set for the various companies:**
 - **High pressure – from 0.6 to 3.5 Tetris**
 - **Medium pressure – from 2.0 to 12.0 Tetris**
 - **High pressure – from 10.0 to 17.0 Tetris**

Natural Gas Distribution Tariffs

- **Monitoring of companies' activities and their financial status**
 - * **The companies shall quarterly submit information on their activities in the form determined by the Commission, and annually submit the audit approved financial statements**
 - * **Majority of gas distribution companies are unprofitable. In 2007, the loss of Kaztransgaz-Tbilisi amounted to GEL 72.00 mln., and this mainly is due to a major technical losses in the system**

- **Major problems of the gas distribution companies**
 - * **The obsolete underground networks and poorly arranged metering result in the major technical and, accordingly, financial losses; all the companies require Commission to increase the loss norms**
 - * **Major consumers try to leave the distribution systems and connect to the transportation system directly; this results in the reduced revenues of the distribution companies and, therefore, they require increase of the residual customers' tariffs.**

TAXATION SYSTEM IN GAS SECTOR

_ **Applicable taxes and their rates**

* **Property tax - 1%, non-agricultural land tax – 0.25 Tetris/m², profit tax – 15%, VAT – 18%**

_ **Tax allowances**

* **Released from 12% customs tax**

* **gas supplies to the thermal PSs is released from VAT**

_ **Share of taxes in consumption tariffs**

* **Before 2005, the share of taxes in consumption tariffs made 23-25%**

Since 2005, (according to new Tax Code) the number of taxes, as well as their rates were reduced: road, entrepreneurship, environmental taxes were abolished; social tax rate was reduced from 31% to 20% and in 2008 was totally abolished; VAT rate reduced from 20 to 18%; profit tax rate reduced from 20% to 15%.

* **Currently, the tax share (total) in consumption tariffs makes 17-18%.**



THANK YOU FOR ATTENTION!