Office of Utilities Regulation

Accounts Separation Guidelines for the Jamaica Public Service Company Limited

OUR's Comments on Responses to Notice of Proposed Rulemaking

OFFICE OF UTILITIES REGULATION

2019 July 15

DOCUMENT TITLE AND APPROVAL PAGE

1. DOCUMENT NUMBER: 2019/ELE/010/RES.001

2. DOCUMENT TITLE: Accounts Separation Guidelines for the Jamaica Public Service Company Limited: OUR's Response to Comments on Responses to Notice of Proposed Rulemaking

3. PURPOSE OF DOCUMENT:

This document presents the Office of Utilities Regulation's (OUR's) response to comments received on the Accounts Separation Guidelines for the Jamaica Public Service Company Limited.

4. ANTECEDENT DOCUMENTS

Publication Number	Publication Title	Publication Date
2018/ELE/008/NPR.01	Notice of Proposed Rulemaking – Accounts Separation Guidelines for the Jamaica Public Service Company Limited	2018 April 18

5. Approval

This document is approved by the Office of Utilities Regulation and the decisions therein become effective on 2019 July 15

On behalf of the Office:

Maurice Charvis
Deputy Director-General

Date: 2019 July 15

Abstract

This document presents the Office of Utilities Regulation's (OUR's/Office's) response to comments received on the Notice of Proposed Rulemaking for Accounts Separation Guidelines at the Jamaica Public Service Company Limited dated 2018 April 18 (Document No.: 2018/ELE/008/NPR.01 ("NPRM"). The document specifically outlines the Office's views on the issues/concerns raised by respondents.

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Chapter 1: Background

Section 46 of the Electricity Act, 2015 stipulates that the Single Buyer of electricity on the national grid, that is the Jamaica Public Service Company Limited (JPS), shall keep separate and distinct accounts for its transactions in the generation, transmission, distribution and supply of electricity. Furthermore, the Electricity Licence, 2016 (Licence) specifies that such accounts should conform to the criteria promulgated by the Office of Utilities Regulation (OUR/Office) and shall be consistent with generally accepted accounting principles and industry best practice.

Accordingly, on 2018 May 18, the OUR published a consultation document entitled Notice of Proposed Rulemaking - Accounts Separation Guidelines at the Jamaica Public Service Company Limited, Document No. 2018/ELE/008/NPR. 01, (Consultation Document). The Consultation Document, which included the proposed Accounts Separation Guidelines (Guidelines), outlined the legal basis for the accounts separation, identified the methodological approach and principles applicable, and laid out the scope of activities required in the preparation of the accounts.

The OUR received responses to the Consultation Document from Consumer Advisory Committee on Utilities (CACU) and JPS.

The OUR's intention in issuing its comments to the responses received on the Consultation Document, is to correct any factual errors highlighted by respondents; provide further arguments, if appropriate, in support of the position proposed by the OUR; and, where reasonable, accept recommendations made by respondents.

Chapter 2: General Responses

2.1 Timing and Cost Implications of Accounting Separation

2.1.1 Stakeholder Responses

JPS indicated that the matter of accounting separation is not simply an accounting exercise. The company noted that the accounting separation exercise will fundamentally reshape the way it organizes its business and account for the financial relationships across the vertically integrated utility.

JPS expressed the view that both the company and the OUR have an obligation to ensure realistic expectations of the process and schedule, and the full implication of the resource requirements and associated costs. There was also an expectation that both the OUR and JPS will continue to have ongoing dialogue on the matter.

2.1.2 OUR's Response

The OUR agreed with JPS that further dialogue was necessary to clarify some of the issues that it raised in its comments on the NPRM and as such, the OUR met with JPS' representatives on 2018 June 7, to explore and resolve the outstanding issues.

JPS indicated that modifications to its accounting and IT systems would be necessary to facilitate the account separation process. JPS also indicated that additionally, business and management processes would have to be re-organized.

The OUR requested that JPS prepares a plan to be submitted to the OUR by 2018 June 22 and which, should include timelines for the following components:

a. The roll out of the Accounting Cost Allocation Manual (ACAM),
b. The clean-up and realignment of the accounting system (to facilitate the required regulatory accounts),
c. The reconfiguration of the IT platform to appropriately assign cost/revenues and capture the information required for regulatory accounts,
d. Identify the structural changes required to make accounts separation happen.

JPS submitted its plan to the OUR in a letter dated 2018 June 27. In that plan, JPS identified four (4) key activities that it considered critical to the overall process. JPS' timelines for the completion of these activities are given in Table 1 below.

Table 1 – JPS' Timeline for the Completion of Key Accounting Separation Activities

Activity	JPS' Proposed Completion Date
Preparation of the Accounting and Cost Allocation Manual (ACAM)	Six (6) months after the finalization of the rules
Realignment of the Accounting System	End of third quarter 2019
The reconfiguration of the IT Platform	Not before 1st quarter 2020
Structural and Organizational Design Modification	Unable to provide an estimate

JPS further indicated that the estimated schedule is preliminary and would need further refinement. The company posited that it would not be in a position to confidently present a first full year of financial accounts consistent with the requisite framework until the financial year ending 2021 December 31. Based on the company's normal financial auditing cycle, the OUR interpreted this to mean that separated accounts for the company would not be available until 2022 March.

In order to obtain an objective assessment of the reasonableness of JPS' proposed completion time for issuing separated accounts, the OUR engaged PricewaterhouseCoopers (PwC) to conduct an independent review of the timeline proposed by JPS to:

1. Assess the reasonableness of the timeline provided by JPS to:
    - Prepare its Accounting Cost Allocation Manual (ACAM)
    - Align its accounting system
    - Reconfigure its IT platform
    - Modify its structural and organizational designs.
2. Evaluate whether the sequencing and timing of the activities identified above is consistent with the presentation of the first set of regulatory accounts for the financial year ending 31 December 2021.

The PwC evaluated JPS' proposed timeline using two (2) approaches:

1. Benchmarking against a forward driven duration model (FDDM) which is a model developed by PwC of the key activities required for each building block for the separation of accounts. The FDDM identifies the duration of time for executing each building block and considers critical activities that could accelerate the roll-out of the separation of accounts;

2. Benchmarking against leading practices in similar type utilities.

The benchmark analysis conducted by PwC indicates that the total estimated duration for the separation of accounts ranges between fifteen (15) to twenty (20) months (if JPS' timeline is excluded from the benchmark). The FDDM indicates a timeline of 18-months while the benchmark of leading practices indicates a timeline ranging from fifteen (15) to twenty (20) months. JPS' estimated timeline is approximately twenty-four (24) months.

Regarding the timeline to complete each of the four (4) major activities, PwC concluded as follows:

Activity	JPS' Proposed Completion Date
Preparation of the ACAM	JPS has estimated that this building block will take approximately six (6) months to complete subsequent to the finalisation of the rules. JPS' timeline is within the range of the timelines provided by the FDDM and leading practices.
Realignment of the Accounting System	JPS has estimated that this building block will take approximately six (6) months to complete subsequent to the finalisation of the rules. This timeline is within the range of the timelines provided by the FDDM and leading practices.
The reconfiguration of the IT Platform	JPS has estimated that this building block will take approximately twelve (12) months to complete subsequent to the finalisation of the rules. The JPS timeline is approximately 15% above the time calculated duration by the FDDM, but within the leading practice time range.
Structural and Organizational Design Modification	JPS was unable to provide an estimate for this activity.

PwC's report indicates that while JPS' timeline is longer than that predicted by the FDDM and leading practices, it is not significantly above these timelines, hence it is reasonable. As such, the OUR has determined that:

- The ACAM shall be submitted within six (6) months of the publication of the Guidelines.
- JPS shall submit its first full audited regulatory accounts by 2022 March 31.
- JPS shall clearly indicate the separation of the regulated business accounts from the non-regulated business in its 2019 Rate Review submission. Additionally, in that same submission, JPS shall identify and separate all customer contributed assets from those in the rate base.

Chapter 3: Comments Specific to Annex 'A' – Accounts Separation Guidelines for the Jamaica Public Service Company Limited

3.1 General Accounting Principles

3.1.1 Responses by Stakeholders

JPS indicated that it expects the Guidelines to include a specific timeframe where a response from the OUR will be provided on submission of the ACAM.

3.1.2 OUR's Response

The OUR is of the view that the request for a specific timeframe is reasonable as it is expected that consequent on OUR's review of the proposed ACAM, feedback will be provided to JPS and that further refinement of the document may be required via a process of consultation with JPS.

Section 5.4.2 of the Guidelines will be amended to include a provision for the OUR to provide comments on the ACAM within three (3) months of JPS' submission to the OUR.

3.2 Materiality

3.2.1 Responses by Stakeholders

According to JPS, while the Guidelines provide a general understanding of what should be considered material, for the purposes of the Account Separation Statements, it does not include any specific guidance regarding the basis to be used in the determination of that materiality. JPS has pointed out that for general purpose financial statements, the auditor is required to determine the materiality to be used in the course of their review based on International Standards on Auditing, ISA 320, which it believes provide sufficient guidance which are internationally approved to determine material levels. JPS recommended that the OUR adopt these standards for materiality in the context of the Accounts Separation Statements.

3.2.2 OUR's Response

The OUR accepts the merit of JPS' recommendation that the International Standards on Auditing ISA 320 be used as the standards for establishing materiality in the preparation of the regulatory accounts. The ISAS 320 is internationally recognized and is already being used by JPS' auditors in auditing its financial statements. Section 5.6 of the Guidelines will be amended accordingly.

3.3 Verifiability

3.3.1 Responses by Stakeholders

JPS suggested that the accounting information and data be retained for a period of seven (7) years, coinciding with existing statutory requirements.

3.3.2 OUR's Response

The OUR accepts JPS' recommendation as it is a requirement of the Tax Administration Jamaica Act, for companies doing business in Jamaica to keep financial records for a period six (6) years. However, the OUR reserves the right to specify from time to time that it may direct JPS to keep certain accounting records for a longer period if these are deemed to be material to a pending litigation or for any other reason.

Section 5.8 of the Guidelines will be amended accordingly.

3.4 Audit Requirements

3.4.1 Responses by Stakeholders

With regard to Section 5.11.4(d) of the Guidelines, JPS expressed the view that the auditing of the financial accounts already includes an assessment of the appropriateness of the company's accounting policies including the capitalization of costs and the depreciation of assets. Thus, the auditor's review of the Accounts Separation Statements should focus on the adherence to the Guidelines and the ACAM in particular, rather than a review of amortization and cost capitalization, which may result in redundancy of effort and possible at additional cost.

3.4.2 OUR's Response

JPS' request is reasonable, since the Accounts Separation Statements are derived from the financial accounts which should be prepared in accordance with the Guidelines and procedures laid out in the ACAM. Thus, a requirement that the auditor's review of the Accounts Separation Statements should focus on adhering to the ACAM will satisfy the objectives of the required audited regulatory accounts.

Section 5.11.4(d) of the Guidelines will be amended accordingly.

3.4.3 Responses by Stakeholders

With regard to Section 5.11.8 of the Guidelines, JPS stated that a re-audit of the Accounts Separation Statements would not be necessary since the Guidelines and the ACAM should provide sufficient details and clarity that would allow Management to appropriately prepare Separation Statements to meet the OUR's requirement. JPS also supported its point by stating that the audit of the financial statements and the review of the Accounts Separation Statements are designed to provide sufficient assurance that these have been prepared in accordance with the relevant accounting standards.

3.4.4 OUR's Response

The OUR envisions that there could be scenarios in which the Auditors may indicate that there are issues with material items in the Accounts Separation Statements or the Auditor's Report, which may not, in the OUR's view, provide a sound basis for confidence in the Accounts Separation Statements and in those scenarios, the OUR may consider it prudent to re-audit the Accounts Separation Statements based on the Auditor's Report.

Section 5.11.8 of the Guidelines will therefore remain as was initially stated in the Draft Guidelines.

3.5 General Information Sheet

3.5.1 Responses by Stakeholders

JPS has recommended that in addition to entities that owns JPS, the names of entities owned by JPS should be included on the General Information Sheet. The company also suggested that the Guidelines should allow for the approval of the General Information Sheet by the Board of Directors for a period of up to three (3) months prior to submission. The CEO or other designated representative approved by the Board (as required by Section 5.12.2 (a) of the Guidelines) can also sign and vouch that there have been no changes in the information included in the General Information Sheet as of the date of the Board approval.

3.5.2 OUR's Response

This request is reasonable as there may be instances where the Board is not available to sign the General Information Sheet fourteen (14) days prior to submission to the OUR. Therefore, OUR will:

- Amend Section 5.12.1 (a) of the Guidelines to include names of entities owned by JPS;
- Amend Section 5.12.2 (b) of the Guidelines to allow the Board of Directors to sign the General Information Sheet for a period up to three (3) months prior to submission, provided that the JPS' CEO or designated representative approved by the Board, shall sign and vouch that there have been no changes to the information included in the General Information Sheet, as of the date of the Board approval. This should be done no more than fourteen (14) days prior to submission to OUR.

3.6 Reporting Requirements

3.6.1 Responses by Stakeholders

Section 5.13.3 of the Guidelines requires that the OUR reserves the right to require JPS to provide interim or additional information it may reasonably specify from time to time. JPS has suggested that the Guidelines should also indicate that JPS should be allowed a reasonable time to prepare and supply the additional information being requested by the OUR.

3.6.2 OUR's Response

The OUR has always acted in good faith in requesting information from JPS and has allowed JPS reasonable time to prepare and supply any additional information being requested. Therefore, the OUR has no objections to modifying the wording in Section 5.13.3 of the Guidelines to explicitly include JPS' recommendation.

3.7 Changes to Accounting & Cost Allocation Manual/Modification of Guidelines

3.7.1 Responses by Stakeholders

JPS suggested that changes to the Accounting and Cost Allocation Manual and Guidelines should coincide with the Five (5) Year Rate Review as it allows for an appropriate assessment of the implications of the changes and the proper planning surrounding its implementation. JPS argued that furthermore, any modifications, which are made to the ACAM and Guidelines, should be implemented on a prospective basis so that it is reflected in financial periods subsequent to the period that the change has been finalized.

The company also suggested that it should be given the opportunity to conduct an appropriate assessment of the benefits surrounding these modifications as compared to the requisite costs and that JPS' management should be able to determine whether such modifications are appropriate.

3.7.2 OUR's Response

With regards to the timing of modifications to the ACAM or the Guidelines, the OUR considers JPS' position to be reasonable, but since the tariff process is forward looking, changes can be allowed at any time even though these changes would not take effect until the next Five (5) Year Rate Review. The Guidelines will thus be modified to state that modifications can only take effect at the next Five (5) Year Rate Review following the amendments. The OUR agrees that modifications should be implemented on a prospective basis.

The OUR however, does not accept that modifications to the ACAM should only be done if JPS deems it beneficial or appropriate. The OUR reserves the right to request amendments as it sees fit and based on its own assessment of need.

The OUR will set up an ACAM review committee which will determine, along with JPS and other pertinent stakeholders, whether amendments are necessary and appropriate. The review committee will be chaired by the OUR and will include two (2) representatives from the OUR, two (2) from JPS, one (1) member from the Ministry with responsibility for energy and one (1) representative from the Consumer Advisory Committee on Utilities.

3.8 Accounts Separation Statement by Business Segments

3.8.1 Responses by Stakeholders

JPS expressed discomfort with the idea of preparing accounting information by business segments as specified in Section 6.5 of the Guidelines. JPS indicated that the separation of accounts by business function aligns with its interpretation of section 46 of the Electricity Act, 2015 and that the additional requirements specified in Section 6.5 are onerous and unnecessary.

3.8.2 OUR's Response

In addition to the requirements outlined in section 46 of the Electricity Act, 2015, Conditions 5(2) and 8 of the Licence empowers the OUR to specify regulatory accounts that may be reasonably required.

The OUR is of the view that in addition to the requirements for preparing accounting statements by business functions, it is also necessary to report by business segments. This is because reporting on business segments provide information on key services delivered by the utility, and will allow the regulator to establish and maintain objective reference points for evaluating information provided by JPS, in relation to specific studies which are required by the regulator from time to time (e.g. cost of service studies). The business segment reports will also provide a sound basis for setting tariffs for services such as transmission interconnection, auxiliary connection and power wheeling. It will also facilitate easy access to information required for data analysis, risk assessment, performance measurement and the promotion of transparency.

Subsections (1) and (2) of section 45 of the Electricity Act, 2015 specifies that the System Operator shall separate its dispatch activities from its transmission activities and activities related to the generation, distribution and supply. The subsections further state that the System Operator shall establish a discrete system operation department whose staff shall be employed in undertaking dispatch activities, and the head of that department shall report directly to the System Operator's board of directors. This means that at the very least, JPS should maintain separate accounts for system operation activities, in addition to information for business functions.

Given the foregoing, the OUR requires that JPS provide accounting statements for business segments as specified in Section 6.5 of the Guidelines. The OUR is cognizant of the impact that this may potentially have on the cost of regulation and as such, will allow for the phased implementation of the accounting statements for business segments. On the submission of the first full audited regulatory accounts in 2022 March 31, JPS shall only be required to provide accounting statements for the following business segments:

- System Operations
- Transmission Connection Services
- Distribution Connection Services