

OUR's Determination Notice of April 28, 2008
NWC's Reconsideration Request

We note the Determination Notice based on a review of National Water Commission's (NWC) rates. Set out below are our comments on the Determination Notice, following our preliminary comments of Friday, March 28.

OFFICE DETERMINATION

1. Section 5.17

The OUR provided \$1,606.971 in the determination for the 2007/08 Administration Expense, which is some \$85.4M less than NWC budgeted amount of \$1,692,330M. Based on the need in areas such as rental, security services and insurance, we believe that the amount provided in our budget is appropriate.

2. Section 5.12

The OUR indicates that Employee Costs has been reduced by \$770.6M, the amount of the interest expense of the non-contributory pension, because it would be double counting given that provision was made for actual interest payment.

- IFRS19 stipulates that an assessment of the pension benefit is required each financial year. The benefit for any given year has six components of which Current Service, Past Service and Interest Costs are included.
- Current service cost is the increase in each member Present value of benefit obligation (PVBO) for additional benefits accrued in the preceding year.
- Interest cost is the increase in the PVBO as the projected time of settlement is closer by one year.
- Past service cost is the increase on PVBO due to changes in benefits which are retroactive benefits for service already rendered.
- The NWC pension benefit obligation is calculated in accordance with the Projected Unit Credit (PUC) Method. The PUC method takes into consideration each period of service which creates an additional increment of benefit entitlement and measures each unit of the benefit entitlement separately. It should be noted that the entire post employment benefits are discounted. The use of this method involves making a number of actuarial assumptions which are NWC's best estimates of variables used in the determination final costs of the post employment benefits.

- The OUR has stated that the majority of the NWC's employees opted to remain with the non-contributory pension scheme which means that the majority of current and interest cost reflected in the Statement of Operation relates to the non-contributory pension scheme. In principle, Accrual accounting requires that obligations be accounted for in the period that they are recognized. These costs should be provided for and an asset (Special Fund) be created for this purpose.

3. Electricity Costs, Section 5.16

The current electricity charge at March 2008 was \$327,493 for the month. This would be annualized at \$3,929,916 with no expected increase which would be prudent. A projected 30% increase is conservative as electricity movement in the financial year 2007/8 was 71% (\$191,865/month to \$327,493/month).

4. Foreign Exchange Loss , Section 5.19

The OUR has indicated that the reason for disallowing the foreign exchange loss is that loans represent assets on the Balance Sheet and which translate into an increase in asset values and depreciation charges. It should be noted that loans are represented as liabilities and as stipulated by IAS 21 assets purchased in a foreign currency are converted at a specific date and there are no further adjustment as it relates to foreign currency. In short any foreign exchange loss or gain is borne by the entity. In addition, the PAM is calculated on a monthly basis using the various components and depreciation is calculated on the value of the assets at the conversion date.

5. Revenue Requirement, Section 8.12

It is stated that if NWC had achieved the target level of efficiency set out in the 2003 Determination the profitability would have been 14% of the current revenue – some \$1.4B. The Office has assigned a deemed revenue of \$580M, after consideration the mitigating circumstances that had contributed to NWC not meeting this target. NWC is of the view that the estimated level of profitability based on efficiency gained is over-stated. NWC had implemented NRW reduction projects within its capacity and demonstrated a commitment to reduce the level of NRW through the various projects. The Office makes the point that with a more widespread effort, the NRW reduction target set at the last Determination Notice could have been achieved. This is not the reality, hence the decision of the Office regarding expectations of revenue arising from these activities should be tempered by this reality. We are of the view that the provision of the “deemed revenue” should, in fact, be less than the \$580M indicated and would prefer that it were removed altogether

RATE STRUCTURE

K-factor Program, Section 9.9

6. NWC supports the proposed K-Factor programs. We propose, however, that the following adjustments be made.
 - That the introduction of any X-factor be delayed by at least 2 years, to allow NWC sufficient time to implement the projects and obtain benefits.
 - i. The first 4- 6 months of the program will involve preparatory work – including finalizing financing for the K-factor projects.
 - ii. NWC is required to comply with the government's procurement guidelines, and therefore some 3-4 months is likely to be required for the contract award process.
 - iii. The improvement works are therefore likely to commence near the beginning of the next financial year. The benefits would therefore not begin until a point within the next financial year.
 - The level of the annual X-factor from Year 2009 is high and should be reduced.
 - i. The basis for deriving the X-factor is not clear
 - ii. A downward adjustment to a level more in keeping with anticipated benefits is needed.
 - iii. The provision for sewerage rehabilitation will not result in a net improvement in NWC's revenues
 - iv. The sewerage of KSA, would increase revenue, an increase which would not be sufficient to offset the investment required based on the level of the sewerage tariff
 - v. Leakage reduction will reduce losses and increase the opportunity for water sales; there is no direct correlation between water sales and savings due to leakage
 - The OUR does not seem to have a clear basis for determining the value of the X-factor. NWC is therefore proposing that the OUR commit to a review of the X-factor in the future when data will be available from the K-factor works program.

7. The Commission is proposing that given the current global economic climate and rising oil prices that the electricity component of PAM be separate and represent a direct pass through to the customer. This should be reflected on the customer bill as a single line item and would be directly linked to the monthly JPS bill.

QUALITY OF SERVICE STANDARDS

Quality of Service Standards, Section 11

8. All claims should be in writing for administrative and legal purposes.
9. WGS 5 - Exceptional cases should not be allowed, e.g. where a customer has deliberately misrepresented the facts in applying for a new connection and a previous delinquent account remains outstanding.
10. WGS 8 - Defect should be verified by NWC in order for breach to be established.
11. WGS 11 - Should remain a claim until change over to the new CIS due to the challenges associated with determining reconnections for payments made at external agencies.

Metering, Section 11:14

12. The NWC is applying for an extension of the time required to achieve 85% functional meters as required: “The Commission must restore itself to 85% metering within fifteen (15) months.” NWC is requesting that the requirement be extended to 24 months to restore itself to 85% functional meters as the whole process of procurement would take about 9 -12 months from invitation to award of contract. Once meters are received, installation would require a further 10 to 12 months.

Manufacturing Sector – Economic Development Wastewater Tariff (EDWT), Section 11.16, 11.17

13. The continuance of sewerage rebates under the EDWT should not be a requirement of the tariff determination as this would be a cost to the NWC, provisions for which have not been made in the tariff determination.

Reconsideration request – Quality of Service Standards

14. The National Water Commission is applying for a reconsideration of Quality of Service Standards WGS7 and WGS11. Due consideration should be given to the inherent constraints that dictate the Commission’s scope of operation. The NWC cannot be penalized for breaches that are subject to factors outside of its control or occur as a result of sound business decisions. It is therefore proposed that all compensations especially those that are automatic be made subject to the following qualifying conditions:
 - o Customer’s account must be in good standing.
 - o Penalties are not due for breaches due to factors outside of the Commission’s control.

WGS 7 – Meter Installation

15. The NWC is expected to operate as a viable commercial entity and will therefore have to operate in a prudent manner when making business decisions. In order for the Commission to be liable under this standard it is only reasonable to stipulate certain qualifying conditions:
- It should be required that a customer’s account be in good standing (a definition would have to be developed and would include accounts with payment arrangements being honored and queries in progress with customers) in order for the company to have any obligation to incur further expenses associated with providing a meter for the said connection.
 - The prevailing Jamaican socio-economic reality dictates that there are some areas (“red areas”) where it is not safe for the Commission’s employees to read meters. These areas have a payment rate of less than 10% of billing where flat rates are applied and the Commission is not able to carry out disconnection or meter reading functions in them. It does not therefore make good business sense with these prevailing factors to install meters in these areas and subsequently the NWC should not be penalized for its prudence.

WGS10 – Meter Reading

16. Due to technical issues with the company’s billing cycle (there may be more than two months between bill issues), we are requesting that this standard be reworded to state that a customer should receive no more than two consecutive estimated bills where there is access to a functioning meter.

WGS 11 – Reconnection after Payment of Overdue Amount

17. The geographical characteristics that prevail in the rural areas inhibit the company’s ability to reconnect all supplies within the stipulated 24 hours. Where connections are separated by miles over rough terrain the company would have to engage the services of additional contractors who may not find it feasible since remuneration is based on a piece rate.

Rural areas are not only characterized by accessibility problems but also difficulties locating accounts since there is usually no specific address and the customers’ names are the only identifying feature. Statistics show that in urban areas a contractor is able to perform 10 reconnections per day on average while for rural areas this rate is only 5 per day and significantly less in sparsely populated rural communities with frequent rainfall and poor roads. Parishes such as Manchester (hilly) and St Elizabeth (swampy) with their terrain and communities such as Mount Pleasant, Airy Castle and Belvedere in St Andrew stand out as areas where the 24 hour target may not be met at all times even with the best efforts of the NWC. We are therefore proposing that the previous requirement of at least 48 hours remain for rural areas.

NWC

Request for Reconsideration

12/5/08

18. Illegally connected accounts, which are disconnected, should be considered new supplies when reconnecting. Illegal supplies are usually disconnected thoroughly (a backhoe is more often than not used) and reconnecting these supplies requires an assessment of the resources required. Hence, 24 hours would not suffice for reconnection due to the works and equipment involved.

CAPITAL EXPENDITURE

Capital Program Section 6.1.1, 6.4

19. The OUR stated that costs and revenues associated with the capital works program in NWC's tariff application were not included in the tariff determination as NWC had not presented robust information in regards to the added revenues which would flow from these investments. Revenue and cost data associated with the capital works program were included in the tariff model submitted to the OUR but not at the level of detail expected.

RATE STRUCTURE

NRW, Section 9.9.10

20. OUR has set a target Non-Revenue Water (NRW) of 55% within three (3) years. Non-Revenue Water represents water that has been produced and has been 'lost' before it reaches the consumer expressed as a percentage. The original premise of the last determination that NRW increased from 57% to 65% is incorrect in that the 57% NRW of December 2003 referred to is in fact the Unaccounted For Water (UFW) – the NRW of 60% should be used. UFW is defined as all water that cannot be accounted for through measurement or estimation. At that time, NRW would be closer to 60% as certain aspects of NRW (e.g. hydrant water) are not included in UFW.

PERFORMANCE BENCHMARKS

Bad debt provision, Section 10.1.4

21. The OUR has determined that bad debt provision should be no more than 5% of billing. We propose that the bad debt provision remains at 8% as the OUR has recognized that NWC may face challenges with the increase in rates due to an increased rate of disconnection, bad debt and theft (Section 12.2.2 Operational impact).

NWC will endeavour to achieve higher levels of collection than 92%.