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By email only to: consultations@ofreg.ky
Utility Regulation and Competition Office
PO Box 2502
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85 North Sound Road
Grand Cayman KY1-1104
CAYMAN ISLANDS

Re: E&U 2019 – 3 - Consultation on Proposed Regulatory Accounting Rules

We refer to the E&U 2019 – 3 - Consultation launched by the Utility Regulation and Competition Office (“OfReg” or the “Office”) on September 20, 2019. Please find below the subject consultation response from Caribbean Utilities Company, Ltd (“CUC”).

Under Part F – Consultation Questions, the Consultation invites interested parties to comment (paragraph 37), particularly with respect to a list of questions (paragraph 38). CUC provides substantive comments in the following Preface section. While the prescribed questions are also addressed, each response thereto is wholly conditioned by the comments in the Preface section.

Preface:

For much of its history, CUC was regulated under an exclusive license arrangement. This arrangement was appropriate and effective for our small island utility. The electricity service on Grand Cayman was then and continues to be a model for the whole Caribbean region. Rather than simply renew that exclusive license, however, the Cayman Islands Government initiated negotiations with CUC in 2004 with the understanding that (a) CUC was not broken and therefore did not need to be fixed, and (b) Government wanted to introduce competition for generation. Upon culmination of this negotiation in 2008, new licenses were issued to CUC, a new regulatory structure was implemented and a new regulatory body was created.



The Regulatory Accounting Rules will require Licensees to prepare an additional set of annual accounts and reports to the Office. In order to be in a position to prepare those accounts at year end Licensees will have to keep additional records and employ additional permanent staff. They will also have to engage specialist accountants and auditors to prepare and review an additional set of accounts and reports at year end. CUC estimates that the additional annual cost to CUC of producing the Regulatory Accounts proposed by the Office will be over \$400k. Other Licensees will have their own additional costs. These costs will ultimately be passed on to all consumers of electricity in Grand Cayman.

We note also that in order to review and comprehend the new accounting reports required by such new regulation, the Office itself will undoubtedly expand its use of consultants or permanent staff, or both and that cost too will ultimately be passed on to all consumers of electricity.

It is likely, if this regime is implemented, that the new reports will lead to dialogue between the Office and Licensees over the content and implications of the reports, which will lead to yet further costs for both the Office and Licensees.

Pursuant to section 6(c) of the URC Law (2019 Revision) one of the principal functions of the Office is *“to protect the short and long term interests of consumers in relation to utility services and in so doing: ... (ii) ensure that utility services are satisfactory and efficient and that charges imposed in respect of utility service are reasonable and reflect efficient costs of providing the services ... “*

The consultation document explains that the Office is attracted to regulatory accounting having regard to its use elsewhere and track record as a regulatory tool (§22). CUC is aware that the regulation envisioned by this Consultation has been implemented in many advanced regulatory structures world-wide. In many markets it is not only appropriate and necessary but also cost-effective – typically, the size of the service territory and the number of service providers are both huge compared to Grand Cayman. In those markets, standardization of reporting requirements enables a regulatory body to efficiently monitor an endless stream of generation additions, transmission extensions, wholesale and retail rate case filings, resource plans and territorial issues. Regulatory accounting is a sophisticated regulatory tool, but it comes at a cost. That cost is reasonable and efficient in much larger service territories but is unreasonable and inefficient in a service territory as small and with as few consumers as Grand Cayman.

Now with this Consultation, OfReg intends to advance its regulatory oversight to levels that were not even imagined during the negotiation of the new law and licenses. While the proposed framework may be appropriate in some jurisdictions, we do not see in the Consultation any evidence that such a framework in Grand Cayman would be an efficient or cost-effective approach and the consultation does not contain any explicit evaluation of cost benefit. The only thing that is clear is that the proposal will undoubtedly increase already significant existing costs of regulatory administration and compliance for consumers.



As the Office is aware, the pricing of electricity is currently controlled by a price capping mechanism in CUC's T&D license that will remain in effect until 2032. Under the current regulatory structure, Grand Cayman benefits from continuation of CUC's outstanding service in a regulated environment. The Consultation does not demonstrate (or even suggest) that this is inadequate or does not work or that changes to the industry warrant such a significant change in regulatory reporting.

To be clear, CUC is not opposed to utility regulation. However, the benefits of regulation must not outweigh its costs, each as considered from the consumers' perspective. The new regulation envisioned by this Consultation will definitely add to costs for the consumers. But we fail to see commensurate benefits to consumers.

Question 1: Do you agree that the accounts of the bulk generation and T&D licensed business units should be separated from each other, from the accounts of the unregulated business units of Licensees (if applicable), and from the accounts of related parties?

No. While this may be appropriate in other larger, more advanced regulatory environments, we do not agree that it is appropriate for Grand Cayman.

Our view is that this approach will only increase the cost of electricity in Grand Cayman. CUC's current cost structure provides the most significant price benefits to consumers in a small Island grid such as ours. See our comments in the Preface

This pricing benefit is best evidenced in the results of the 2014 generation expansion bid where CUC's bid was 22% lower than the next lowest priced bidder.

Question 2: Do you agree that, for every licensed business unit, the elements that need to be reported include operating costs, revenues, current assets and current liabilities, and fixed assets?

No. While this may be appropriate in other larger, more advanced regulatory environments, we do not agree that it is appropriate for Grand Cayman. See our comments in the Preface

Operating cost and revenue allocation

Question 3: Do you agree with the approach to allocating all operating costs and revenues to the individual business units?

No. While this may be appropriate in other larger, more advanced regulatory environments, we do not agree that it is appropriate for Grand Cayman. See our comments in the Preface



Assets and liabilities allocation

Question 4: Do you agree that assets should be allocated to the regulatory accounts of their main user, where the main user should make a transfer charge to any other business unit that also uses that asset?

No. While this may be appropriate in other larger, more advanced regulatory environments, we do not agree that it is appropriate for Grand Cayman. See our comments in the Preface

Question 5: Do you agree that current assets and current liabilities should be allocated to the business units in line with the principles of cost and revenue allocation?

No. While this may be appropriate in other larger, more advanced regulatory environments, we do not agree that it is appropriate for Grand Cayman. See our comments in the Preface

Question 6: Do you agree that long-term liabilities should be allocated to business units only if they are directly associated with a particular business unit, or are collateralised with assets that are associated with particular business units?

No. While this may be appropriate in other larger, more advanced regulatory environments, we do not agree that it is appropriate for Grand Cayman. See our comments in the Preface

Transfer charges and related party transactions

Question 7: Do you agree that, as far as is practical and proportionate, transfer charges and transactions with related parties should be valued at arm's length?

No. While this may be appropriate in other larger, more advanced regulatory environments, we do not agree that it is appropriate for Grand Cayman. See our comments in the Preface

Question 8: Do you agree that, for every licensed business unit, Licensees should provide a breakdown of operating costs and revenues by internal transactions, external transactions with related parties, and external transactions with independent parties?

No. While this may be appropriate in other larger, more advanced regulatory environments, we do not agree that it is appropriate for Grand Cayman. See our comments in the Preface

Third-party transactions disclosure

Question 9: Do you agree that third-party transactions need to be disclosed in the notes to the regulatory accounts?

No. While this may be appropriate in other larger, more advanced regulatory environments, we do not agree that it is appropriate for Grand Cayman. See our comments in the Preface



Yours faithfully,

A handwritten signature in blue ink, consisting of a stylized 'L' followed by a horizontal line that extends to the right.

Letitia T. Lawrence
VP Finance & CFO