

# ENERGY REGULATORY ENTITY OF ALBANIA

No xx, xx.xx.2016

Based on Articles 79(4), 83, 84, 85, and 109 of the Law on the Power Sector Law of Albania No.43/2015 and on ERE Decision Number xx 2016, "Imposition of Public Service Obligations upon Licensing the Electricity Sector of Albania", the Board of Commissioners of ERE adopts the following

## DECISION

### On Tariff Methodology for the Universal Service Supplier

#### Article 1 Scope

1. This Decision is adopted in order to specify the methodology to be used for the determination of regulated tariffs for the Universal Service Supplier (USS) as required by the Power Sector Law of Albania No.43/2015 and ERE Decision Number xx 2016, "Imposition of Public Service Obligations upon Licensing the Electricity Sector of Albania".
2. This tariff methodology applies to the following categories of consumers:
  - Consumers connected to the distribution network at 20 kV until December 31, 2016, at which time they are no longer eligible for supply by the Universal Service Supplier.
  - Consumers connected to the distribution network at 10 kV and 6 kV until December 31, 2017, at which time they are no longer eligible for supply by the Universal Service Supplier.
  - Consumers connected to the distribution network at 0.4 kV voltage until such time as ERE determines that those consumers entitled to universal service could buy electricity on the market at reasonable unregulated prices, as required by Article 9 of ERE Decision Number xx 2016, "Imposition of Public Service Obligations upon Licensees in the Electricity Sector of Albania".

#### Article 2 Terms

Terms in this Decision have the meaning prescribed in Article 3 and other sections of the Power Sector Law of Albania No.43/2015. Terms specific to this decision have the following meanings:

1. **Bad Debt Allowance** – an allowance in tariffs to reflect amounts owed by customers of the USS which are unlikely to be paid, as determined by ERE.
2. **Depreciation and Amortization Expense** – Depreciation cost related to fixed assets utilized to provide universal service, plus amortization cost related to intangible assets such as software required by the USS. as determined in accordance with the Regulatory Accounting Standards
3. **Distribution Use of System Costs** – Amounts paid to the Distribution System Operator for use of system, in accordance with tariffs approved by ERE.
4. **Energy and Capacity Cost** – The cost incurred by the Universal Service Supplier for energy and capacity needed to serve consumers eligible for Universal Supply Service including (1) purchases from the Government Owned Generator based on the terms of the annual contract between the parties approved by ERE in accordance with Article 5.2 of the Council of Ministers Decision No.244, dated 30.03.2016, (2) purchases required in excess of the amount to be provided by the Government Owned Generator, (3) a credit for the incremental amount paid to the USS by the Government Owned Generator in accordance with Article 5.3 of the Council of Ministers Decision No.244, dated 30.03.2016, (4) costs related to balancing charges, ancillary services, and any other costs related to acquiring energy and capacity, (5) purchases from Renewable Energy Suppliers, and (6) Market Operator Fees, in accordance with the Market Rules.
5. **EURIBOR** means the European Banking Federation Interbank Offer Rate for Euro deposits for a period equal to 3 months which appears on the appropriate page of the Reuters service at or about 11:00 a.m. Central European Time. The rate used shall be an annual rate.
6. **Operating and Maintenance Costs** - Costs incurred by the Universal Service Supplier for (1) direct operation and maintenance costs of the USS, (2) administrative and general corporate costs directly assigned or allocated to the Universal Service Supply function, and (3) any license fees assessed to the USS; in accordance with Regulatory Accounting Standards. The costs of advertising and other marketing for the purposes of encouraging consumption are not allowed to be included.

7. **Regulatory Period** – The 12-month period utilized by the regulator to determine the Revenue Requirement of a licensee for the purpose of computing tariffs.
8. **Revenue Requirement** – The amount of revenue needed by an efficiently managed licensee to carry out its licensed activity over a period of time, generally 12 months. This amount is proposed by the licensee and reviewed by the regulator.
9. **Regulatory Accounting Standards** - A detailed listing of every account in an accounting system that the regulator wants a licensee to use to record its assets, liabilities, equity, revenue and expense.
10. **Retail Margin** – A fixed percentage that is applied to Energy and Capacity Costs incurred by the USS
11. **Transmission Fees** -Amounts paid to the Transmission System Operator for Transmission Use of System and System Operation, in accordance with tariffs approved by ERE.
12. **Working Capital (WC)** –Funds needed to meet day to day payment obligations
13. **Working Capital Allowance (WCA)**– An amount necessary to compensate the USS for the cost of funds utilized in its day-to-day operations.

### **Article 3**

#### **Tariff Review Process**

1. The retail tariffs of the Universal Service Supplier (USS) will be reviewed and approved by ERE on an annual basis, as required by Article 85 of the Law on the Power Sector.
2. The Regulatory Period upon which the retail tariffs of the USS are to be determined is an estimate of the upcoming 12-month period.
3. The tariff review process will require the USS to provide the following information to ERE for review and approval:
  - A schedule of the actual revenues and expenses of the USS for the most recently available actual 12-month period, prepared in accordance with the Regulatory Accounting Standards Regulation of ERE.
  - A schedule of the energy acquired by the USS (by source) and the energy sold to each customer class for the most recently available actual 12-month period.

- A forecast of the energy to be procured by the USS during the upcoming 12-month period to satisfy the requirements of each customer class eligible for Universal Supply Service.
  - A forecast of the Revenue Requirements of the USS for the Regulatory Period.
  - The allocation of the Revenue Requirement for the forecast period to each of the tariff classes served by the USS
  - The design of tariffs to recover the Revenue Requirement for each of the tariff classes from that tariff class.
4. ERE will review the information provided by the licensee and determine if it is complete. In the event it is not complete, ERE will notify the licensee of any deficiencies and provide a time period for the licensee to submit additional or corrected information. The information provided by the licensee will be made available to the public. ERE staff (or its advisors) will analyze the information submitted by the licensee and provide its opinion as to the reasonableness of the information provided and, in the instances where ERE disagrees with the information provided, ERE will state the reasons for the disagreement and propose alternative values. ERE's Preliminary Tariff Proposal will be documented in a Consultation Report to be provided to the licensee.
  5. The Licensee will be provided thirty (30) days to provide comments on the Consultation Report to ERE and those comments will be considered by ERE in its tariff decision which will be made public on its web site.
  6. If the USS is not satisfied with a tariff decision of ERE, it can appeal the decision to the appropriate court, in accordance with the laws of Albania.
  7. At the current time, retail prices for low voltage customers are not cost reflective. The regulated prices for these consumers shall be gradually increased until they reach full cost-reflectivity by 31 December 2017, as required by Article 9 of ERE Decision Number xx 2016, "Imposition of Public Service Obligations upon Licensees in the Electricity Sector of Albania".

#### **Article 4**

##### **Determination of the Revenue Requirement**

1. In accordance with accepted regulatory practices, the Law on the Power Sector of Albania No.43/2015, and on ERE Decision Number xx 2016, "Imposition of Public Service

Obligations upon Licensees in the Electricity Sector of Albania”; the **Revenue Requirement(RR)** of the USS shall consist of the following elements:

**a. Energy and Capacity Cost (E)**

This category will include the cost of energy and capacity needed to serve consumers eligible for Universal Supply Service. As such it will include:

- Energy and capacity procured from the Government Owned Generator based on the terms of the annual contract between the parties approved by ERE in accordance with Article 5.2 of the Council of Ministers Decision No.244, dated 30.03.2016.
- Energy and capacity required in excess of the amount to be provided by the Government Owned Generator, in accordance with the Market Rules.
- A credit for the incremental amount paid to the USS by the Government Owned Generator in accordance with Article 5.3 of the Council of Ministers Decision No.244, dated 30.03.2016.
- Costs related to balancing charges, ancillary services, and any other costs related to acquiring energy and capacity.
- Purchases from Renewable Energy Suppliers
- Market Operator Fees, in accordance with the Market Rules.

**b. Transmission Fees (TF)**

This category will include expected amounts to be paid to the Transmission System Operator for use of system and system operation, in accordance with tariffs approved by ERE.

**c. Distribution Use of System Costs (DUOS)**

This category will include expected amounts to be paid to the Distribution System Operator for use of system, in accordance with tariffs approved by ERE.

**d. Operating and Maintenance Costs (OM)**

These costs include direct operation and maintenance costs of the USS as well as administrative and general corporate costs directly assigned or allocated to the Universal Service Supply function in accordance with the Regulatory Accounting Standards. Any license fees assessed to the USS will be included in this cost category.

The cost of public communications for electrical safety, energy conservation, encouraging prompt payment and discouraging unauthorized use of electricity are allowable costs to be included in the allowable Operating and Maintenance costs, however, the costs of advertising and other marketing for the purposes of encouraging consumption are not allowed to be included.

**e. Depreciation and Amortization Expense (DA)**

The depreciation cost related to fixed assets utilized to provide universal service, as determined in accordance with the Regulatory Accounting Standards. Also to be included is any amortization cost related to intangible assets such as software required by the USS.

**f. Retail Margin (RM)**

The Retail Margin shall be a fixed percentage that is applied to allowed wholesale energy and capacity costs. It shall be set at such a level such that it: provides the USS with a reasonable return that compensates it for the risks it assumes in serving customers eligible for Universal Supply Service. This shall be calculated with reference to the margins earned by similar utilities in countries elsewhere in Europe, taking account of the similarities between the electricity industry in those countries and that of Albania. Therefore, Retail Margin (**RM**) is computed as follows:

$$**RM = E * \% Allowed**$$

**g. Working Capital Allowance (WCA)**

The base for the allowed working capital value shall be calculated as 1/12th of the sum of allowed:

- Energy and Capacity Cost (**E**)
- Transmission and Distribution Fees (**TF + DUOS**)
- Operation and Maintenance Costs (**OM**)

The formula is as follows:

$$WC = \frac{1}{12} * (E + TF + DUOS + OM)$$

The cost of financing working capital (**WCC**) shall be determined based on the cost of short term borrowing of the licensee. In the event that such a value cannot be determined, the cost to be applied will be equal to EURIBOR plus an adder of X percent. The adder (X) will be based on the situation in regional financial markets at the time. For the purpose of the first tariff review utilizing this methodology, the adder will be set equal to 3%.

The Working Capital Allowance (**WCA**) is therefore determined as follows:

$$WCA = WC * WCC$$

**h. Bad Debt Allowance (BD)**

The Licensee will propose a bad debt allowance which ERE will review for reasonableness. In making this determination, ERE will consider the efforts being made by the USS as well as the support provided by law enforcement officials and the judicial system to enforce the collection of amounts due from consumers. In order to encourage the USS to manage its accounts receivable in a cost effective manner, ERE may decide to establish a target level to provide the incentive to reduce this cost from the level experienced in the prior year.

**i. Adjustment for Incentive Regulatory Mechanisms (ADJ1)**

Performance Standards related to quality of supply are specified in ERE Decision Number XXX dated dd.mm.2016. In the event that ERE decides to reflect any monetary value (either plus or minus) related to the licensee performance in relation to the standards, that amount would be reflected in this mechanism.

**j. Adjustment of Prior Year Over/Under Recovery of Revenue Requirement (ADJ2)**

An adjustment will be made in the event the licensee recovered more or less of the revenue requirement for the prior year due to:

- Differences between forecast and actual billed electricity;

- Differences between forecasted and actual Energy and Capacity costs on a per kWh basis;
  - Differences between forecasted transmission and distribution fees on a per unit basis.
  - Differences in the sales mix between the customer classes
2. The **Revenue Requirement (RR)** can, therefore, be expressed as follows:

$$RR = E + TF + DUOS + OM + DA + RM + WCA + BD + ADJ1 + ADJ2$$

### **Article 5**

#### **Allocation of the Revenue Requirement to Tariff Classes**

1. The Revenue Requirement determined in accordance with Article 4 must be allocated to each tariff class utilizing the following basic principles:
- a. Energy and Capacity cost is to be allocated to customer classes based on available load research data reflecting time of use, including seasonal usage patterns and on-peak vs. off-peak usage for each customer class.
  - b. Distribution Use of System charges are to be assigned to customer classes based on the voltage level at which service is provided.
  - c. Transmission Use of System charges are to be allocated to customer classes based on the percentage of kWh utilized by each customer class.
  - d. Working Capital Allowance will be allocated to customer classes based on the proportion of items a, b, and c above allocated to the class.
  - e. Operation and Maintenance, Depreciation Expense, and Retail Margin will be allocated to customer classes based on the percentage of energy sales to each class.
  - f. Bad Debt Expense will be computed for each customer class based on the percent of bad debt experienced in the most recent 12-month period, adjusted for any incentive factor determined by ERE.
  - g. Adjustments for incentive regulatory mechanisms will be allocated to customer classes based on percent of kWh sales.

### **Article 6**

#### **Tariff Design for Each Customer Class**



1. The Revenue Requirement for each tariff class, as determined in Article 5, will be compared to the estimated revenue based on current tariffs for each customer class. The revenue excess or deficiency for each class will be identified.
2. The licensee shall review the current billing determinants for each tariff class and propose any changes to those billing determinants which may include (depending on the customer class and metering capability):
  - Fixed customer charge per month
  - Energy charge (in LEK per kWh) by time of day, season, and/or consumption block
  - Capacity (Demand) charge (in LEK per kW)
  - Reactive Power Charge (in LEC per kVarh)
  - Other
3. The licensee shall propose new tariffs for each customer class with the objective of recovering the allocated Revenue Requirement from each customer class.
4. Effective 01 January 2017, the USS is no longer authorized to offer a tariff for unmetered service. The USS will work with the Distribution System Operator in its efforts to meter the consumption of all consumers.
5. ERE will review the proposal of the licensee and make adjustments it feels necessary in order to achieve full cost reflective tariffs for each customer class by 01 January 2018, as required by Article 9 of ERE Decision Number xx 2016, "Imposition of Public Service Obligations upon Licensees in the Electricity Sector of Albania".