



## **PRESS STATEMENT**

### **SPEECH BY THE ERB BOARD CHAIRMAN MR. SIKOTA WINA (GOEZ) ON THE ZESCO APPLICATION TO VARY ELECTRICITY TARIFFS FOR 2010/2011**

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MEMBERS OF THE BOARD;

MEMBERS OF THE PRESS

ZESCO MANAGEMENT;

ENERGY CONSUMERS;

INVITED GUESTS;

LADIES AND GENTLEMEN

#### **1.0 INTRODUCTION**

ON 21<sup>ST</sup> APRIL 2010, ZESCO LIMITED (ZESCO) APPLIED TO THE ENERGY REGULATION BOARD (ERB) FOR AN AVERAGE TARIFF ADJUSTMENT OF 36% FOR 2010 AND SUBSEQUENT ADJUSTMENTS OF 21% FOR 2011, 14% FOR 2012, 8% FOR 2013 AND 9% FOR 2014.

AFTER THOROUGH CONSIDERATION OF THE ZESCO APPLICATION AND CONSUMER SUBMISSIONS, THE ERB HAS NOW ARRIVED AT A DECISION. OUR DECISION HAS BEEN INFLUENCED BY A NUMBER OF FACTORS WHICH I SHALL HIGHLIGHT DURING THIS BRIEFING.

AS MEMBERS OF THE PUBLIC MAY BE AWARE, THE ENERGY REGULATION BOARD ADOPTED A MULTI YEAR TARIFF FRAMEWORK (MYTF), IN PRINCIPLE, IN DECEMBER 2007 FOR THE PERIOD 2008/9 TO 2010/11 IN LIGHT OF THE NEED TO ENABLE ZESCO ATTAIN COST REFLECTIVE TARIFFS ON ITS PATH TO COMMERCIAL VIABILITY. HOWEVER, THE MULTI YEAR TARIFF FRAMEWORK HAS NOT BEEN FULLY IMPLEMENTED BECAUSE IT IS NOT PROVIDED FOR UNDER THE CURRENT LEGAL FRAMEWORK IN THE ELECTRICITY ACT. IT IS FOR THIS

REASON THAT ZESCO HAS CONTINUED TO APPLY FOR TARIFF INCREASES ANNUALLY IN LINE WITH THE MIGRATION PATH TO COST REFLECTIVE TARIFFS.

## **2.0 LEGAL BASIS FOR REVIEW**

IN LINE WITH THE ELECTRICITY ACT CAP 433 OF THE LAWS OF ZAMBIA, THE ENERGY REGULATION BOARD UNDERTOOK A DETAILED REVIEW OF THE APPLICATION TO APPRECIATE THE BASIS UPON WHICH ZESCO WAS PROPOSING TO INCREASE ELECTRICITY TARIFFS FOR ALL CUSTOMER CATEGORIES OTHER THAN MINING AND EXPORTS, WHICH ARE BILATERALLY NEGOTIATED. IN ADDITION, THE ENERGY REGULATION BOARD ISSUED A PUBLIC CONSULTATION PAPER TO GUIDE CONSUMERS ON THE MAIN ASPECTS OF ZESCO'S APPLICATION. FURTHER TO THE ISSUANCE OF A PUBLIC CONSULTATION PAPER, TWO PUBLIC HEARINGS WERE HELD IN KITWE AND LUSAKA TO ACCORD ALL THOSE WHO HAD COMMENTED ON ZESCO'S APPLICATION AN OPPORTUNITY TO PRESENT THEIR VIEWS TO THE BOARD.

## **3.0 MAJOR ISSUES IN ZESCO PROPOSAL TO VARY ELECTRICITY TARIFFS**

ZESCO PREMISED ITS APPLICATION TO INCREASE TARIFFS MAINLY TO CHANGES IN THE ECONOMIC CONDITIONS OVER THE LAST TWO YEARS; CHANGES IN THE COST OF GENERATING, TRANSMITTING, DISTRIBUTING AND SUPPLYING ELECTRICITY; SYSTEM AND CUSTOMER BASE EXPANSION; RISING COST OF ELECTRICITY IMPORTS; AND COST REDUCTION AND REVENUE ENHANCEMENT MEASURES IT WISHES TO UNDERTAKE.

TO SUPPORT ITS APPLICATION, ZESCO FURTHER ADVANCED THE FOLLOWING REASONS:

- i. THAT THE DRAMATIC RISE IN PRICES OF COMMODITIES SUCH AS COPPER, STEEL, COBALT AND OIL IN THE LAST FIVE YEARS HAD TRANSLATED INTO INCREASED OPERATING COSTS OF PROVIDING POWER.THESE ARE MAJOR COMPONENTS IN THE ELECTRICITY SUPPLY INDUSTRY;
- ii. THAT THE KEY PERFORMANCE INDICATORS (KPIs) AGREED WITH THE ERB HAD INCREASED THE NEED FOR ZESCO TO RAISE MORE

RESOURCES TO UNDERTAKE CAPITAL INVESTMENT PROJECTS AS WELL AS RE-INVEST IN AND/OR REFURBISH ITS INFRASTRUCTURE IN ORDER TO IMPROVE SERVICE DELIVERY; AND

- iii. THAT THE RISING COST OF IMPORTED ELECTRICITY TO MEET RISING LOCAL DEMAND HAD NECESSITATED THE NEED FOR THE TARIFF INCREASE TO MITIGATE THE POWER DEFICIT. IN THAT REGARD, THE COST OF POWER IMPORTS HAD RISEN FROM AN AVERAGE OF UNITED STATES 4 CENTS PER KILO WATT HOUR IN 2006/7 TO ABOUT UNITED STATES 5 CENTS PER KILO WATT HOUR IN 2009/10.

#### **4.0 CONSUMER SUBMISSIONS**

IN RESPONSE TO ZESCO'S APPLICATION TO INCREASE TARIFFS, FORTY-SIX (46) SUBMISSIONS WERE RECEIVED FROM CONSUMERS OF ELECTRICITY FROM VARIOUS PARTS OF THE COUNTRY. SOME OF THE MAJOR ISSUES RAISED BY CONSUMERS INCLUDED THE FOLLOWING:

- i.* THAT THE PROPOSED 69% INCREASE IN TARIFFS FOR RESIDENTIAL CONSUMERS WAS TOO HIGH AND WOULD NOT MATCH THE LEVEL OF SALARIES EARNED BY WORKERS;
- ii.* THAT THE PROPOSED INCREASE WAS NOT REASONABLE ESPECIALLY THAT MOST CONSUMERS WERE CURRENTLY UNABLE TO PAY THEIR BILLS AND ZESCO'S QUALITY OF SERVICE WAS UNSATISFACTORY. FURTHER, THAT UNDER THE PRESENT CIRCUMSTANCES, SUCH AN INCREASE WOULD HAVE POLITICAL, ENVIRONMENTAL, ECONOMIC AND OTHER RAMIFICATIONS;
- iii. THAT THE MINING INDUSTRY WHICH CONSUMES OVER 50% OF ZESCO'S TOTAL PRODUCTION IS NOT SUBJECT TO FREQUENT TARIFF ADJUSTMENT AND THAT ZESCO SHOULD NOT DISCRIMINATE AGAINST RESIDENTIAL AND OTHER CONSUMERS;
- iv. THAT ZESCO WAS ABUSING ITS MONOPOLISTIC STATUS BY INCREASING TARIFFS CONTINUALLY WITHOUT A CORRESPONDING IMPROVEMENT IN THE QUALITY OF SERVICE, AND AT THE SAME TIME MAKING ITS OWN STAFF PAY UNECONOMIC TARIFFS;

- v. THAT NO INCREASE SHOULD BE MADE BEFORE PRE-PAID METERS ARE INSTALLED IN OTHER PARTS OF THE COUNTRY. FURTHER, THAT THE PROPOSED INCREASED TARIFFS WOULD BE UNFAIR TO CONSUMERS ON FIXED CHARGE WHO WERE ALREADY PAYING FAR MORE THAN THEY WERE CONSUMING;
- vi. THAT THE ECONOMIC CONDITIONS CITED BY ZESCO FOR AN INCREASE IN ELECTRICITY TARIFFS WERE NOT JUSTIFIED BECAUSE THE MINES HAD REDUCED OPERATIONS IN THE LAST TWO YEARS, WHILE THERE WAS INCREASED ACTIVITY IN OTHER INDUSTRIES;
- vii. THAT IF ZESCO REDUCED ITS OPERATING COSTS AND NON TECHNICAL LOSSES THERE WOULD BE NO NEED TO INCREASE TARIFFS TO THE EXTENT BEING PROPOSED;
- vii. THAT THE PROPOSED TARIFF INCREASES FOR DIFFERENT CUSTOMER CATEGORIES WERE DISPROPORTIONATE TO THE AMOUNT OF ELECTRICITY CONSUMED BY EACH CONSUMER CATEGORY;
- viii. THAT KEY PERFORMANCE INDICATORS DID NOT QUALIFY TO BE USED AS A REASON FOR INCREASING TARIFFS BECAUSE ZESCO'S PERFORMANCE IN RELATION TO KPIs WAS UNSATISFACTORY; AND
- ix. THAT THE PROPOSED INCREASE IN ELECTRICITY TARIFFS WOULD RESULT IN AN INCREASE IN PRODUCTION COSTS AND HAVE A KNOCK-ON EFFECT ON PRICES OF GOODS AND SERVICES.

WHILE MOST CONSUMERS OPPOSED THE PROPOSED TARIFF INCREASE, A FEW CONSUMERS SUPPORTED THE TARIFF INCREASE ON THE BASIS THAT THE CURRENT ELECTRICITY TARIFFS WERE BELOW THE COST OF PRODUCING ELECTRICITY, THUS COMPROMISING THE ELECTRICITY INDUSTRY'S CAPACITY AND VIABILITY.

FURTHER, THAT AN INCREASE IN THE COST OF INPUTS AS A RESULT OF HIGH COMMODITY PRICES OF BASE METALS AND THE DEPRECIATION OF THE KWACHA HAS HAD ADVERSE EFFECTS ON THE VIABILITY OF THE ELECTRICITY SECTOR.

## **5.0 ERB'S EVALUATION OF THE PROPOSED ELECTRICITY TARIFF VARIATION**

LADIES AND GENTLEMEN, IN CONSIDERING ZESCO'S TARIFF APPLICATION AND TAKING INTO ACCOUNT CONSUMER SUBMISSIONS, THE ERB CONDUCTED A DETAILED AND ANALYTICAL REVIEW IN LINE WITH THE FOLLOWING REGULATORY PRINCIPLES:

- i. RECOVERY OF PRUDENTLY INCURRED COSTS BY THE UTILITY;
- ii. RECOGNITION OF USED AND USEFUL UTILITY ASSETS, ONLY;
- iii. FINANCIAL SUSTAINABILITY OF THE UTILITY;
- iv. THE NEED TO ATTAIN COST REFLECTIVE TARIFFS;
- v. DELIVERY OF QUALITY SERVICE; AND
- vi. SOCIAL CONSIDERATIONS FOR THE INDIGENT CUSTOMERS.

AS A RESULT OF OUR DETAILED REVIEW OF ZESCO'S TARIFF APPLICATION IN LINE WITH THE REGULATORY PRINCIPLES, THE ERB, AMONG OTHER THINGS, MADE THE FOLLOWING ADJUSTMENTS:

1. DUE TO THE CONTINUED FAILURE BY ZESCO TO IMPLEMENT THE BOARD DIRECTIVE OF 2007 AND 2009 TO ABOLISH ITS STAFF TARIFFS, THE ERB HAS CONVERTED THE STAFF TARIFF TO PRE-PAID RESIDENTIAL TARIFF. THIS MEANS THAT IF ZESCO CONTINUES TO CHARGE THE UNECONOMIC STAFF TARIFF, THE UTILITY WILL FOREGO AN ESTIMATED REVENUE OF **K3 BILLION**. THIS MEASURE IS TO ENSURE THAT THE BURDEN OF UNECONOMIC STAFF TARIFFS IS NOT BORNE BY ORDINARY CONSUMERS BUT BY ZESCO ITSELF. IF ZESCO DOES NOT COMPLY WITH THIS DIRECTIVE, THE ERB WILL APPLY OTHER REGULATORY SANCTIONS AGAINST THE UTILITY;
2. SOME PROPOSED ZESCO CUSTOMER PROJECTS WHICH ZESCO HAD INDICATED WOULD COMMENCE IN 2010 HAVE BEEN PUSHED FORWARD AS AGREED WITH ZESCO BECAUSE THE CUSTOMERS HAVE RESCHEDULED THEM FOR VARIOUS REASONS;
3. CONSUMPTION BY SOME PROJECTS HAS BEEN REVISED DOWNWARDS;
4. THE FOLLOWING ADMINISTRATION COSTS HAVE BEEN DISALLOWED:
  - i. DONATIONS AMOUNTING TO K 9.5 BILLION;

- ii. ENTERTAINMENT COSTS AMOUNTING TO K 436 MILLION; AND
- iii. ZESCO UNITED FOOTBALL CLUB COSTS AMOUNTING TO K 4.7 BILLION.

5. THERE HAS BEEN A DOWNWARD ADJUSTMENT OF FINANCE COSTS.

THE NET EFFECT OF THESE MEASURES IS THAT ONLY THE JUSTIFIABLE REVENUE REQUIREMENT IS TAKEN INTO ACCOUNT WHEN DETERMINING ZESCO'S TARIFFS.

LADIES AND GENTLEMEN, YOU MAY RECALL THAT IN THE 2009 TARIFF DECISION, THE BOARD DID NOT TAKE INTO ACCOUNT ZESCO PERFORMANCE AS REGARDS THE KPIS AND SUSPENDED THE KPI TARIFF DETERMINATION MECHANISM FOR THE REST OF THIS MULTI-YEAR TARIFF FRAMEWORK. THIS WAS DUE TO THE FACT THAT ELECTRICITY TARIFFS HAD NOT YET REACHED COST REFLECTIVE LEVELS AND THE UTILITY WAS IN A WEAK FINANCIAL POSITION.

IN THAT REGARD, RESTRICTING REVENUE REQUIREMENTS TO THE KPI SCORES WOULD HAVE RESULTED IN THE UTILITY GETTING LOWER REVENUES THAN THE APPROPRIATE REVENUE REQUIREMENTS. THE UTILITY WAS THEREFORE GIVEN A GRACE PERIOD OF UP TO MARCH 2011. DURING THE INTERVENING PERIOD, THE ERB HAS CONTINUED TO MONITOR ZESCO'S PERFORMANCE IN RELATION TO KPIS. I WISH TO RE-EMPHASISE THAT FROM APRIL 2011 ONWARDS, THE KPI SCORES WILL BE A KEY FACTOR IN DETERMINING SUBSEQUENT TARIFF AWARDS.

## **6.0 BOARD FINDINGS AND OBSERVATIONS**

LADIES AND GENTLEMEN, AFTER DUE CONSIDERATION OF THE ZESCO APPLICATION, I WISH TO EMPHASISE THE FOLLOWING ISSUES:

- i. THAT THE VARIATION OF TARIFFS IN ITSELF IS NOT THE ONLY SOLUTION TO ZESCO'S OPERATIONAL CHALLENGES. THE UTILITY NEEDS TO RE-ENGINEER ITS INTERNAL BUSINESS PROCESSES AND TRANSFORM ITSELF INTO A FULLY FLEDGED COMMERCIAL ENTITY;
- ii. THAT THE TURN-OUT OF SUBMITTERS AT THE PUBLIC HEARINGS WAS POOR AND DISAPPOINTING WHEN COMPARED TO THE NUMBER OF SUBMISSIONS RECEIVED. ONLY 20 OUT OF THE 46 PEOPLE WHO HAD

MADE WRITTEN SUBMISSIONS TURNED UP AT THE HEARINGS TO ARTICULATE THEIR POSITIONS;

- iii.* THAT ZESCO SHOULD CONSIDER IMPLEMENTING LOAD SHAVING AS AN ALTERNATIVE TO LOAD SHEDDING THROUGH THE USE OF SPECIFIC APPLIANCES SUCH AS RIPPLE SWITCHES FOR GEYSERS;
- iv. THAT ZESCO'S QUALITY OF SERVICE HAS GENERALLY DETERIORATED AS INDICATED BY THE UTILITY'S 2009 KPI SCORES;
- v. THAT ZESCO HAS NOT YET SHIFTED ITS STAFF TARIFF TO THE REGULAR RESIDENTIAL TARIFFS, CONTRARY TO THE BOARD'S DIRECTIVE; AND
- vi. THAT THE POWER REHABILITATION PROJECT HAS EXPERIENCED DELAYS IN COMPLETION AND THE UTILITY IS FACING POST REHABILITATION CHALLENGES ON THE PROJECTS.

IN VIEW OF THESE OBSERVATIONS, OUR FINDINGS AS RELATES TO ZESCO'S POSITION ARE AS FOLLOWS:

- i. AFTER THIS TARIFF INCREASE, ZESCO SHOULD BE ABLE TO GENERATE ADEQUATE RESOURCES TO OPERATE COMMERCIALY AND PROFITABLY;
- ii. THE UTILITY SHOULD URGENTLY DEAL WITH THE CURRENT ELECTRICITY SUPPLY CONSTRAINTS AND ACCELERATE NEW POWER PROJECTS WITH THE AID OF GOVERNMENT;
- iii. ZESCO IS UNDER-CAPITALISED AND GOVERNMENT SHOULD CONSIDER RECAPITALIZING THE UTILITY;
- iv. ZESCO STAFF COSTS IN RELATION TO ITS TOTAL OPERATING COSTS ARE STILL HIGH AT 51% OF TOTAL COSTS. THE INTERNATIONAL INDUSTRY STANDARD IS ABOUT 30%;
- v. ZESCO'S TRADE RECEIVABLES ARE STILL HIGH. GOVERNMENT SHOULD LIQUIDATE THE DEBT THAT IT OWES ZESCO, WHILE THE UTILITY SHOULD ACCELERATE THE INSTALLATION OF PRE-PAID METERS AT ALL GOVERNMENT INSTITUTIONS AND SHOULD BE PROACTIVE IN ITS DEBT COLLECTION; AND
- vi. THE UTILITY'S PERFORMANCE AGAINST THE AGREED KPIs HAS BEEN UNSATISFACTORY;

- vii. THERE IS A NEGATIVE PUBLIC PERCEPTION OF ZESCO, WHICH THE UTILITY NEEDS TO SERIOUSLY ADDRESS. WE WISH TO ENCOURAGE ZESCO TO PROACTIVELY INTERACT MORE WITH ITS CUSTOMERS;
- viii. IT IS IMPERATIVE THAT ELECTRICITY TARIFFS IN ZAMBIA ARE COST REFLECTIVE TO ENCOURAGE MORE INVESTMENT IN THE ENERGY SECTOR ESPECIALLY IN LIGHT OF THE PREVAILING POWER DEFICIT; AND
- ix. FURTHER, THAT COST REFLECTIVE TARIFFS ARE NECESSARY TO PROMOTE EFFICIENT USE OF ELECTRICITY WHICH IS KEY TO DEMAND SIDE MANAGEMENT.

## 7.0 BOARD DECISION

AFTER DUE CONSIDERATION OF THE APPLICATION AND TAKING INTO ACCOUNT THE VARIOUS SUBMISSIONS MADE THEREON, THE ERB NOW ORDERS AS FOLLOWS:

THAT WITH EFFECT FROM **1<sup>ST</sup> AUGUST 2010**, THE TARIFFS FOR THE YEAR 2010/2011 WILL BE VARIED BY **AN AVERAGE OF 25.60%**. THE CHANGES PER CUSTOMER CATEGORY ARE AS FOLLOWS:

1. WHILE ZESCO APPLIED FOR A 69% INCREASE FOR RESIDENTIAL CONSUMERS THE TARIFF HAS INCREASED BY **41%**. THE NEW TARIFF IS **K373.09** PER KILO WATT HOUR;
2. WHILE ZESCO APPLIED FOR A 6% INCREASE FOR LARGE POWER CONSUMERS (MAXIMUM DEMAND 3 AND 4) THE TARIFF HAS INCREASED BY **12%**. THE NEW TARIFF IS **K320.54** PER KILO WATT HOUR;
3. WHILE ZESCO APPLIED FOR A 14% INCREASE FOR SMALL POWER CONSUMERS (MAXIMUM DEMAND 1 AND 2) THE TARIFF HAS INCREASED BY **15%**. THE NEW TARIFF IS **K280.32** PER KILO WATT HOUR;



4. WHILE ZESCO APPLIED FOR A 41% INCREASE FOR COMMERCIAL CUSTOMERS THE TARIFF HAS BEEN INCREASED BY **27%**. THE NEW TARIFF IS **K338.44** PER KILO WATT HOUR; AND  
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5. WHILE ZESCO APPLIED FOR A 49% INCREASE FOR THE SERVICES TARIFF HAS INCREASED BY **33%**. THE NEW TARIFF IS **K254.10** PER KILO WATT HOUR.

OUR ROLE HAS BEEN THAT OF A BALANCING ACT TO ARRIVE AT A TARIFF THAT ADDRESSES ZESCO'S FINANCIAL VIABILITY OBJECTIVES AS WELL AS SAFE GUARDING THE CONSUMER INTEREST.

I THANK YOU FOR YOUR ATTENTION.

**Issued this 26<sup>TH</sup> Day of July 2010**

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**Mr. Sikota Wina (GOEZ)**

**Chairman**