



LESOTHO ELECTRICITY AND WATER AUTHORITY

In the matter regarding a

**DETERMINATION OF LESOTHO ELECTRICITY COMPANY (Pty)
Ltd's APPLICATION FOR A TARIFF INCREASE FOR 2013/14**

1. DECISION

After duly considering the application, the written and oral submissions from stakeholders during public consultation process, reasons, facts and evidence provided, the Lesotho Electricity and Water Authority (LEWA) Board, at its meeting held on May 17, 2013, decided and resolved as follows:-

- a.** A 15.2% tariff increase on the energy and maximum demand charges for all customers;
- b.** The current charges for connection, wiring testing, wiring re-testing, survey, re-survey, licensing for wiring, meter testing and house extension remain the same for the financial year 2013/14 until the applicant has provided justification and the Authority has considered and approved the proposed charges; and
- c.** The energy and maximum demand charges for all customer categories be increased as shown in tables 1 and 2 below.

Table 1: Approved LEC Energy Charges for 2013/14

Customer Categories	Old Energy Charges (M/kWh)	Approved percentage (%) change	New Energy Charges (M/kWh)	Adding Customer Levy @M0.0254/kWh (M/kWh)	Adding Rural Electrification Levy @M0.02/kWh large customers and @M0.035/kWh for others (M/kWh)	New Approved Energy Charges (M/kWh)	Old Energy Charges including levies (M/kWh)	Final Tariff Percentage (%) increase
Industrial HV	0.1169	15.2	0.1347	0.1601	0.1801	0.1801	0.1599	13
Industrial LV	0.1294	15.2	0.1491	0.1745	0.1945	0.1945	0.1724	13
Commercial HV	0.1169	15.2	0.1347	0.1601	0.1801	0.1801	0.1599	13
Commercial LV	0.1294	15.2	0.1491	0.1745	0.1945	0.1945	0.1724	13
General Purpose	0.9555	15.2	1.1011	1.1265	1.1615	1.1615	1.0135	15
Domestic	0.8453	15.2	0.9741	0.9995	1.0345	1.0345	0.9033	15
Street Lighting	0.4799	15.2	0.5530	0.5784	0.6134	0.6134	0.5379	14

Table 2: Approved LEC MD Charges for 2013/14

Customer Categories	Old Maximum Demand Charges (M/kVA)	Approved Percentage (%) Change	New Approved Maximum Demand Charges (M/kVA)
Industrial HV	164.6143	15.2	189.6973
Industrial LV	192.2747	15.2	221.5725
Commercial HV	164.6143	15.2	189.6973
Commercial LV	192.2747	15.2	221.5725

The figures in tables 1 and 2 exclude VAT

2. THE APPLICANT

LEC is a Government owned company registered in terms of the Companies Act of 1967. It was established in terms of the LEC (Pty) Ltd Establishing and Vesting Act 2006 wherein the assets, liabilities, rights and obligations of the former Lesotho Electricity Corporation were vested in the company. It was subsequently issued a Composite License in terms of Section 50 of the Lesotho Electricity Authority Act 2002 as amended; (hereinafter referred to as LEA Act) to transmit, distribute and supply electricity.

3. THE APPLICATION

The Authority received an application for a Tariff Review from LEC on 15 March, 2013, requesting a 36%¹ increase on energy and maximum demand charges. The Application also included the review of other LEC charges as shown in table 3 below, and further requested the Authority to suspend the 'Electricity Connection Charge Guidelines'.

Table 3: LEC Other Charges to Customers

Activity	Current Charges		Proposed Charges		Percentage increases	
	Domestic	General Purpose	Domestic	General Purpose	Domestic	General Purpose
Wiring Testing	0	0	50	100	100%	100%
Wiring Re-testing	20	0	50	100	150%	100%
Survey	100	250	100	250	0%	0%
Re-survey	100	250	100	250	0%	0%
License for wiring premises						
Initial Application	250	0	250	0	0%	0%
Annual Renewal	100	0	100	0	0%	0%
Meter testing	20	40	50	100	150%	150%
House Extension	0	0	50	100	100%	100%

LEWA Management, on 27 March 2013 wrote a modification letter to LEC requesting the company to provide additional information and clarity regarding compliance with the 2012/13 Authority's Tariff Determination, Tariff Filing and Review Procedure and Electricity Connection Charge Guidelines. The company provided the required clarifications, together with additional information on 9 April 2013.

¹ The proposed 36% would, if approved, automatically increase the customer and electrification levies by the same percentage increase. The levies are recommended by LEWA to the Ministry for approval and should not form part of LEC's request for a tariff review.

The LEC's application stated that it is in line with the LEA Act which requires the utility to submit tariff application at the end of each financial year. The application covers the revenue requirement for 2013/14.

LEC stated that electricity is one of the major drivers of the Lesotho economy and it is essential that the country has adequate supply which is reliable, of good quality and reasonably priced. The company went further to say it needs financial resources to maintain and replace the equipment that has reached its useful life and invest in new generating stations and other infrastructure in order to meet increasing demand due to economic growth. LEC pointed out that, unlike other utilities such as Eskom of South Africa, it is not allowed new infrastructure funds² from tariffs. LEC was initially regulated by the then Ministry of Natural Resources and in 2004 the Ministry implemented a tariff transition plan for a four (4) year period. LEC further alleged that it has effectively been subjected to financial erosion by regulation.

LEC argued it will continue to import power from Eskom and EDM of Mozambique as there are no prospects of developing new generation facilities in the short and medium terms which means bulk supply costs will always increase. The company said it will carry out demand side management as a strategy to alleviate the current power deficit.

LEC further stated that the textile industry was facing some serious challenges due to global competition and the extension of AGOA beyond 2015 was likely to give the textile industry some certainty that was likely to result in increased demand. The projected connections of 167 000 by the end of the financial year showed that there was demand for electricity and the GOL target of 35% access by 2015 would be met, argued LEC.

The application indicated that the company was faced with the following challenges:

- a.** Increased growth due to more connections;
- b.** Inability to raise private funding for electrification projects;
- c.** Unavailability of funds to refurbish its infrastructure;
- d.** Lack of some strategic inventories;

² The regulatory Accounting Guidelines provide for allowance of funds for capital work in progress (CWIP). Based on the principle of 'used and useful' there is no provision for allowing funds for projects to be initiated.

- e. Increasing costs of imports from Eskom and EDM;
- f. Non-cost reflective charges for connections;
- g. Antiquated network and network equipment;
- h. Shortage of power to drive the economy;
- i. Reliance on Eskom and EDM as marginal suppliers which in turn compromise the national security of supply in Lesotho; and
- j. The company used activity³ based costing and budgeting instead of the incremental budgeting implied by the use of the indexing by LEWA.

The application mentioned that the cost of supply methodology was applied to derive the proposed tariffs. The following cost items formed the basis for the applied revenue requirement of M714.7 million.

- a. **Operating expenses:-** These costs were mainly driven by customer numbers, customer load and density. The company had substantially increased connections by 105% since 2008/09 and its customer/employee ratio was 315⁴. The company spent M560.00⁵ per trip of attending to customer calls. Other factors that affected LEC operating expenses were network size, complexity and climatic conditions. The company would be taking over Government constructed projects and it would need at least 15% of their capital costs to operate them. The company had under-recovered in operating expenses⁶ and needed to be compensated.
- b. **Cost of sales:-** The company had under-recovered in bulk supply costs by over M45 million. The bulk supply costs for 2013/14 would be M285 million and this had factored in the 8% tariff increase by Eskom. On average, bulk supply costs are M0.36/kWh for 2013/14.
- c. **Return on assets:-** The company needed M81.7 million as the return on its assets.

³ Activity Based Costing and Budgeting is only applicable to LEC's budget on repair and maintenance as operating expenses are mainly administrative.

⁴ Increasing the number of employees will reduce the ratio and thereby affect the company's efficient staffing levels.

⁵ This figure was never supported with data from the company's Financial Statements.

⁶ Operating expenses are not treated as pass-through as the company has a full control over these costs. Again, the figures used for calculating the under-recovery are not consistent. The company has not substantiated the number of connections made in 2012/13 and the total revenue from tariffs.

- d. Labour costs:-** The company has benchmarked itself with utilities in Botswana, Mozambique and Zimbabwe and found that it was the most efficient in terms of staffing levels. LEC asserted that it would be increasing its staff to 591 and it would remain efficiently staffed compared to the utilities mentioned. The company would also be reviewing its salaries in order to comply with its 'Median Remuneration Philosophy'. The company would also be restructuring its salaries and fringe benefits tax would increase.
- e. Depreciation:-** The company would be engaging a consultant to review the depreciation charges as they were currently based on 2009 assessment.

The costs were attributed to the business units established in the company with costs for non regulated activities apportioned to the regulated business units. LEC stated that assets that were financed by donors, government and customers do not form part of the regulatory asset base that is used for determining return on assets. These assets were however included in determining depreciation costs as LEC was responsible for their replacement regardless of the source of funding.

The application concluded that the required revenue for 2013/14 was M714.7 million which is composed of generation, bulk purchases, transmission, distribution, and supply and procurement costs.

4. APPLICABLE LAW, GUIDELINES, PRINCIPLES, PROCEDURES AND REGULATIONS

The legal mandate of the Lesotho Electricity and Water Authority (LEWA) to make a determination of tariff applications is derived from the LEA Act. In terms of section 22(f) of this act, it is the function of LEWA to regulate prices charged to electricity consumers. Tariffs filing and review processes are governed and guided by the following guidelines, principles, procedures and regulations:

- a.** Electricity Connection Charges Guidelines;
- b.** Licensees Regulatory Accounting Guidelines;

- c. Pass-Through Charging Principles for Bulk Supply Tariff and Procedure for Implementation Mechanism;
- d. Charging Principles for Electricity and Water and Sewerage Services;
- e. Lesotho Tariff Filing and Review Procedure for Electricity and Water Services; and
- f. Lesotho Electricity Authority (Electricity Price Review and Structure) Regulations, 2009.

5. PUBLICIZING OF THE APPLICATION

In terms of Section 24 (6) of the LEA Act, the Authority is required to publish a notice in the newspapers and other local media to allow electricity consumers and other interested stakeholders to comment on the reasonableness of the tariffs applied for. Accordingly, a public notice was issued on 03 April 2013 giving stakeholders until 12 April 2013 to submit their comments. It further requested stakeholders who had interest in making oral presentations before the Pricing and Tariff Committee of the LEWA Board to indicate their interest in writing, so that appropriate arrangements could be made. At the close of that day, comments had been received from Lesotho Textile Exporters Association (LTEA), Consumer Protection Association (CPA), Lets`eng Diamonds, Catholic Commission for Justice and Peace (CCJP), Department of Economics-National University of Lesotho and individual domestic customers.

6. PUBLIC CONSULTATION SESSION

Three public hearings were held on 12, 19 and 26 April 2013 in Moyaeni (Quthing), Hlotse (Leribe) and Maseru respectively. LEC and representatives from stakeholders⁷, Catholic Commission for Justice and Peace, LTEA, CPA, Lets`eng Diamonds, Lesotho Chamber of Commerce and Industry (LCCI) and Department of Economics - National

⁷ Participants at public hearings were afforded the opportunity to organize themselves into groups and air their views through their representatives, after LEC had made its presentation.

University of Lesotho (NUL) made presentations before the Pricing and Tariffs Committee of the Authority.

6.1 LEC's Presentation

In its presentation LEC described its business as being characterized by the following, among others:

- State owned monopoly;
- Regulated;
- Capital intensive;
- High fixed costs; and
- Used imported capital equipment.

The objectives of the company were stated as regulatory compliance, demand side management and security of supply. The presentation mentioned requirement of network reinforcement, low returns in electrification, inadequate redundancy in the network, need for old equipment replacement and regional power shortage as its constraints.

LEC mentioned that the 'Muela effect of stabilizing prices had started to diminish and as a result, long run marginal cost (LRMC) of electricity would be determined by ESKOM and EDM as they had become the marginal power suppliers. The company stated the reasons that prompted the request for tariff adjustment as the following:-

- ESKOM and EDM tariffs increases of 8% and 12% respectively that translate into bulk purchase costs increase; and
- Increased operating costs due to increased number of customers, increased length of network, required increase in the number of staff and plans to improve customer service.

LEC finally requested 36%⁸ increase on energy charges for all customer categories and the same percentage on maximum demand charges. The proposed tariffs are as shown in tables 4 and 5 below.

Table 4: LEC Proposed Energy Charges for 2013/14

Customer category	Old Tariff-inclusive of Levies (M/KWh)	Proposed tariff-including of levies (M/KWh)	Maloti increases (M)	Percentage (%) increase
Industrial HV	0.1599	0.2176	0.0577	36
Industrial LV	0.1724	0.2346	0.0622	36
Commercial HV	0.1599	0.2176	0.0577	36
Commercial LV	0.1724	0.2346	0.0622	36
General Purpose	1.0135	1.3791	0.3656	36
Domestic	0.9033	1.2292	0.3259	36
Street Lighting	0.5379	0.7319	0.1940	36

Table 5: LEC proposed Maximum Demand Charges for 2013/14

Customer category	Old Tariff-inclusive of Levies⁹ (M/kVA)	Proposed tariff-including of levies (M/kVA)	Maloti increases (M)	Percentage (%) increase
Industrial HV	164.61	223.9982	59.38	36
Industrial LV	192.27	261.6370	69.36	36
Commercial HV	164.61	223.9982	59.38	36
Commercial LV	192.27	261.6370	69.36	36

⁸ This proposed increase will result in energy tariffs for various customers increasing by more than 36% and LEC conceded to this during public hearings. The requested increase will only result to M675 472 793.00 in revenue.

⁹ Maximum demand charge does not include levies.

6.2 Issues Raised by Various Stakeholders

During the public hearings a number of stakeholders' groups were formed in order to allow the public to present their comments on the application. All groups did not agree with the 36% increase. They stated that the acceptable increase should be between 5% and 11.1% and the reasons were as follows:

- The inflation rate according to Bureau of Statistics was around 6%;
- Most people were not employed in the country;
- Public servants and most other companies salary increases were based on prevailing inflation rate which is 6.1%;
- The elderly with their pension could not afford the increase;
- Any increase beyond 6% should be paid for by the Government;
- LEC should improve its efficiency;
- Government should pay for its consumption, including its debts to LEC; and
- Pro-poor tariffs should be implemented in order to cater for poor households.

They further advised that LEC should come up with strategies that would cut on operational costs. In their presentations they mentioned that it was not convincing that LEC carried out activities allowed for in the approved tariff. As an example, stakeholders pointed out that since 2010 it requested funds for improving its services but such services continued to deteriorate and the consumers were worse off.

In the presentations, it was also mentioned that LEC's monopolistic power made it a non performer. It was also stated that, if 36% was approved, electricity consumption would be reduced resulting in revenue lower than forecasted. In conclusion the presentations recommended the following:-

- LEC should consider implementing time-of-use tariffs;
- LEC should revisit the projected figure for bad debt provision which has a great jump from M 4 million to M 24 million;
- LEC should change its electrification strategy, by electrifying areas that are densely populated and are near towns as opposed to sparsely populated rural areas;

- LEC must prepare for and implement resource management as inefficiency was its greatest problem; and
- LEC must reconsider its application, as the basis for the high increase was not clear since it managed to make a profit after it was denied the percentage increase it requested in the last financial years.

CPA emphasized that electrification targets must be aligned to the market forces of demand and supply. It also stated that electricity units that are allocated as a benefit to LEC employees did not promote efficient consumption of electricity. CPA suggested that a portion of taxes generated from mining operations, increased VAT collections due to advent of shopping malls and complexes should be reinvested in financing of a very expensive target of increasing electricity connectivity to 35% by 2015. In conclusion, the Association advised that 36% tariff hike could force the poor who have access to electricity to use alternative sources and recommended an inflation related (6.1% as projected by BOS for 2013-14) allowance in the new tariff.

LTEA disagreed with 36% increase and recommended 6% and 0% for energy and maximum demand respectively. The following are some of the reasons it gave for its disagreement:-

- An increase in tariffs could raise prices for the whole country which would result in uncontrollable inflation that would inhibit national economic growth; and
- Buyers of the industries' products could not accept 36% increase in prices and that would accelerate recession of the industries.

Lets`eng Diamonds in its presentation requested LEC to justify the requested increase as ESKOM, its supplier has increased its tariffs by 8% only. It mentioned that such a substantial increase would jeopardize the sustainability of its operations and impact on the economy as a whole.

Department of Economics, NUL stated that empirical analysis of the sensitivity of electricity consumption to price fluctuations throughout the years in Lesotho showed that electricity consumption was not responsive to price changes. The presenter used a hypothetical example where he supposed that for economic growth to maintain the past

decade average growth of approximately 4%, electricity consumption should increase by 4% as it is a major role player in economic growth (he stated that further studies are required to determine the effect of electricity consumption on economic growth). With supposed electricity consumption increase of 4% LEC should have requested a price hike of 20.85% but if zero increase is assumed in electricity consumption then the requested price increase should have been 46.39%. An average of the two will be approximately 33%¹⁰, and supposedly what LEC had requested is slightly higher. Finally, the presenter recommended that LEC should carry out the analysis for individual consumer categories in order to determine which categories responded more to price change and redesign the tariff increase strategy accordingly.

6.3 LEWA's Views on LEC's Presentation at the Public Hearings

In order for the Authority to understand LEC's application better, clarifications were sought during the public hearings held. LEC should be commended for providing a detailed presentation in support of its application for a tariff increase. It is worth noting that LEC continued to provide information that was inconsistent with the application. This was mainly noticed in Maseru where depreciation charge, staff costs and operating expenses were no longer the same as those contained in the application. This has been a practice over the years and it confuses the stakeholders as they would be making their inputs based on what was in the application. It has also been noticed that LEC failed to honour undertakings that it made with respect to provision of all requested information. Some information was not provided until a final tariff decision was made.

The importance of provision of accurate and credible information cannot be over-emphasized. For instance, LEC alleged to have connected 29 417 (from 128 583 in 2011/12 to 158 000 in 2012/13). The numbers differ materially from those submitted monthly by LEC during the year. LEC was requested and it undertook to provide information supporting the above numbers but the information was never submitted. The company, further, alleged that it was subsidizing new connections, losing money on

¹⁰ The presenter acknowledged that his analysis needed to be backed by robust data in order to substantiate his analysis and conclusions.

attending to customers and has been subjected to financial erosion by regulation. To date, no information was provided to substantiate these claims. LEC is therefore advised to confirm the accuracy of information used in all its applications so as not to compromise the credibility of the contents of the applications.

LEC further undertook to submit a connection fee policy, before the end of May 2013, which embodied the application of 'Electricity Connection Charges Guidelines'¹¹. To date, the Authority has not yet received a new connection fee policy. LEC must ensure that it honours its commitments made to the Authority and the public at all times.

Though LEC acknowledged existence of various regulatory instruments dealing with the Authority's pricing philosophy, it indicated that it has not been fully implementing or complying with those instruments. While non-compliance is an issue that the Authority has consistently raised, failure to comply affects LEC adversely. LEC is advised to familiarize itself and comply with all regulatory instruments before it can submit its tariff application for 2014/15.

LEC indicated that though its financial ratios were based on qualified financial statements, the numbers were credible since the qualification was as a result of Auditor's inability to confirm or verify trade receivables and income of M45.15 million and M444.00 million, respectively and non-compliance with International Financial Reporting Standards (IFRS). The Authority is of the view that LEC, should amongst others, ensure that controls are tightened and implemented, and that compliance to IFRS is adhered to including the provision of audited financial statements on or before 30 September each year.

The above indicated that LEC needs to seriously consider changing its approach to regulation and compliance with its external auditing obligations.

¹¹ Stakeholders complained that LEC charges 'Pioneer Connectors' high prices and does not compensate them when other customers connect to the system. The Guidelines are meant to address this issue.

6.4 Analysis of Public Views during Public Hearings

The general public was not necessarily opposed to a tariff increase; they however argued that the proposed increase of 36% will have adverse effect on consumers and by extension on LEC. They argued that a reasonable increase would range from 0% to 11.1%. The public was despondent about LEC's customer care and service¹², quality of supply and misuse of resources.

LEC has continued to provide information that is inconsistent with its application. It has failed to put up a case for the increase in a number of its connections in a year; It has conceded that it has not been fully providing information to the Authority as required; Application of the simulation and the results thereof are inconsistent with the requested percentage increase; LEC admitted that it has not been fully compliant to the prescripts of regulation.

The above indicate that LEC needs to strongly change its approach towards its customers and it needed to adopt a better approach towards its regulatory obligations.

It is however pleasing to note that LEC has prioritized regulation and customer services in the current financial year.

¹²LEC was urged to explore alternative means to sell electricity units, speed up connections and improve on quality of service.

7. ANALYSIS OF LEC'S APPLICATION

7.1 LEC's Costs and Required Revenues

The LEC's revenue requirement is made up of the following major cost items:

- Bulk Supply Purchases;
- Operating Expenses;
- Labour;
- Depreciation; and
- Return on Investment.

7.1.1 Bulk Supply Purchases

In 2012/13 financial year, LEC was allowed M200 million for bulk supply costs and the company paid M245 647 982.54 as shown in table 6 below.

Table 6: LEC's Actual and Forecasted Bulk Supply Costs

Intake Point	Amount Paid in Maloti (M) in 2012/13	Forecasted amount to be Paid in Maloti (M) in 2013/14	Difference in Maloti (M)	Percentage (%) increase
Maseru Bulk Supply	115 087 278.13	129 404 671.30	14 317 393.17	12
Butha-Buthe-Clarens	46 601 279.32	51 848 825.00	5 247 545.68	11
Qacha's Nek	5 835 449.47	6 345 917.70	510 468.23	9
'Muela	50 056 724.60	63 371 226.31	13 314 501.71	27
EDM	28 067 251.02	34 291 109.09	6 223 858.07	22
Total	245 647 982.54	285 261 749.40	39 613 766.86	16

For 2012/13 Financial Year, LEC under-recovered by M45 647 982.54 in bulk purchases and in line with the Pass-through Principle and its Implementation Procedure, LEC is entitled to recover the M45.6 million in its tariffs during the

2013/14 financial year. Adjusting this figure by over-recovery in depreciation, diesel and oil of M7.4 million in 2012/13 and bulk costs of M16.4 million in 2011/12, the net under-recovery for 2012/13 is M21.8 million.

The amount of under-recovery is substantial and will result in large tariff increase in one year which may not be sustainable. Even though the current increase in bulk purchases looked reasonable, they may be slightly below what LEC has forecasted because Maseru Bulk and EDM Bulk supply costs are based on a scenario in which 'Muela was non-operational for two months. Again, EDM expenses on peak energy has increased by 236% and decreased by 68% on off-peak energy. This suggests that LEC will be buying more energy¹³ from EDM at an expensive price (peak price). In adjusting the allocation of energy based on last year's consumption, EDM costs reduces by M9.3million. Maseru Bulk expenses have also increased by 18% and this may be inflated as more energy will be coming from 'Muela. The forecasted bulk supply costs by LEC should be implemented as they are and monitored during the year and reconciled with M21.8 million under-recovery.

7.1.2 Operating Expenses

LEC's allowed operating expenses, excluding depreciation and labour costs, were M60.8 million in 2012/13 but LEC's actual operating expenses were M85.4 million, indicating 40% increase compared to the allowed costs by the Authority. For 2013/14, LEC proposes a budget of M95.7 million for operating expenses which is 57% higher compared to the 2012/13 allowed revenue.

While the company has provided the Authority with reasons for the high operating expenses, information supporting the advanced reasons is lacking as it could not be established in the company's Financial Statements. The reasons put forward included the costs of servicing customers, characteristics of the customer

¹³ Purchases from EDM have reduced by 16 213 743kWh compared to the last financial year purchases.

load and network size, complexity and climatic conditions. The company also treats operating expenses as pass-through meaning it cannot control them and therefore should be paid as they are by the customers. The company also compares itself with regional utilities (Botswana Power Company, EDM and ZESCO) and regards itself as efficient in terms of staffing levels (customer/employee ratio) and the percentage of its operating expenses to the operating and maintenance costs. Furthermore, LEC's operating expenses would be increasing due to the transfer of newly constructed electrification projects (Mphaki and Ha Sekake) from the Government to LEC.

In order to cater for costs associated with the expanding electricity system, the Authority increases these costs on the basis of annual inflation, increase in sales and customer growth. Based on the data provided by LEC, connections will increase by 6% and sales by 5% as shown in table 7 below. Based on the inflation rate of 6.1%, half the predicted growth in sales and the increased customer connections¹⁴, the operating expenses in LEC's allowed revenues would be M68.1 million, an increase of 12% instead of 57% proposed by LEC.

Table 7: Energy Sales (kWh), Connections and Revenue per kWh

Item	Actual in 2012-13	Projected in 2013-14	Increase in Percentage (%)
Energy Sales (kWh)	680 949 932.00	714 642 632.00	5
Connections	158 000 ¹⁵	167 000	6
Total Revenue (M)	480 668 005.00	572 351 309.31	19
Revenue (M) Required per kWh	0.7059	0.8009	13.5

¹⁴ Based on international best practices (incentive-based regulation), labour costs are allowed to increase in line with growth in business and in LEC this is shown by increase in connections and MWh sales.

¹⁵ LEC has not provided the Authority with information supporting this connection figure.

7.1.3 Labour

LEC's allowed labour costs for 2012/13 was M107.3 million but the actual costs are M104.1 million, indicating 3% lower than the allowed costs. For the financial year 2013/14, the company proposes M140.4 million for the labour costs indicating 31% increase compared to the allowed labour costs in 2012/13 financial year. Whilst the Company had provided the Authority with justification for the increased staff costs, mainly due to creation of 51 additional Engineering positions, salary restructuring, increased medical aid expenses and increased fringe benefits tax, the company's justification is not based on efficiently staffed utilities as it compares itself with Botswana Power Company, EDM and ZESCO in terms of employee/customer ratios, which are far below targeted 400 customers per employee. The 400 customers per employee is in line with the conclusions of the benchmarking study conducted by the Authority in 2009¹⁶, which concluded that the company's actual staff complement (excluding vacant positions) appeared excessive and staff numbers should not increase substantially as the number of connections continues to increase. The 31% increase in labour costs proposed by LEC is attributed to increases in salaries (at and above inflation rate) and staff numbers which are above the efficient levels recommended by the study.

In order to maintain efficient level of staffing at LEC, the Authority has considered increase in staff costs that is in line with inflation and customer numbers. This would mean labour costs are allowed to increase by half the increase in customer numbers plus the rate of inflation. On this basis, labour costs in LEC's allowed revenue would be M117.0 million instead of M140.4 million proposed by LEC. This would represent an increase of 9% compared to allowed labour costs in 2012/13.

¹⁶ Economic, Regulatory and Financial Model Study undertaken by ECA Consultants on behalf of LEA

7.1.4 Depreciation

The allowed LEC's depreciation charge for 2012/13 was M73.4 million and this figure appears to be high, compared to the actual figure of M66.4 million. For the Financial Year 2013/14, LEC proposes a depreciation charge of M75¹⁷ million, an increase of 13% compared to the actual in 2012/13. LEC has not provided all information as required by Tariff Filing and Review Procedure supporting the increased depreciation charge. LEC's depreciation charge has therefore been calculated by increasing the 2012/13 charge by 5%, to M69.8 million and this should be recovered from tariffs.

7.1.5 Return on Investment

While LEC has reviewed its return on investment downwards from its request of last years' figure of M93.7 million to M81 million, lack of proper asset register prohibits separation of assets so that grants, donations and customer financed assets do not form part of the regulatory asset base (RAB). The Authority has maintained last year's level of M12 million.

¹⁷ This figure was revised to M85 million during LEC's presentation in Maseru and is not consistent with net replacement values of 2009 assessment.

7.2 LEC's Adjusted Revenue Requirement

Adjustments made in 7.1 above lead to the revenue requirement shown in table 8 below.

Table 8: LEC Revenue Requirement in 2013/14 Financial Year

Cost Items	Approved Revenue in 2012/13 (M)	Actual Revenue in 2012/13 (M)	Variance between Approved and actual Revenue in 2012/13 (M)	Projected LEC Costs for 2013/14 (M)	Adjusted Costs for 2013/14 based on the approved costs in 2012/13 (M)	Adjusted LEC Cost minus projected for 2013/14 (M)
Cost of Sales	217 515 000.00	262 711 145.54	- 45 196 145.54	302 395 949.00	302 395 949.00	-
Bulk Purchases	200 000 000.00	245 647 982.54	-45 647 982.54	285 261 749.00	285 261 749.00	-
Repairs and maintenance	16 606 000.00	16 505 999.00	100 001.00	16 190 200.00	16 190 200.00	-
Diesel and oil	909 000.00	557 164.00	351 836.00	944 000.00 ¹⁸	944 000.00	-
Operating Expenditures	244 249 737.36	258 680 575.00	- 14 430 837.64	314 971 169.00	257 955 360.31	- 57 015 808.69
Labour	107 302 327.77	104 122 172.00	3 180 155.77	140 436 316.00	117 066 839.60	-23 369 476.40
Depreciation	73 398 105.00	66 444 792.00	6 953 313.00	75 630 297.00	69 767 031.60	-5 863 265.40
Other expenses	60 842 366.59	85 406 673.00	-24 564 306.41	95 683 148.00	67 900 081.11	-27 783 066.89
LEA License	2 706 938.00	2 706 938.00	-	3 221 408.00	3 221 408.00	-
Sub-total (Cost of sales and operating expenditures)	461 764 737.36	521 391 720.54	-59 626 983.18	617 367 118.00	560 351 309.31	-57 015 808.69
Return on Asset	12 000 000.00	- 16 369 071.00	-4 369 071.00	81 327 205.00	12 000 000.00	-69 327 205.00
LEC's Total Required Revenue (excl. levies)	473 764 737.36	505 022 649.54	-31 257 912.18	698 694 323.00	572 351 309.31	-126 343 13.69

¹⁸ LEC has requested M16.3 million for generation and this was explained as a budget for feasibility studies for generation projects. The figure included in the budget is for purchase of diesel and oils for Semonkong mini-hydropower plant.

Based on the figures in the table 8 above, on average, tariffs would need to increase by 13.5% without levies and 12.9% inclusive of levies. The average increase is consistent with a 13.5% increase in revenue required per kWh as shown in table 7.

7.2.1 Average Tariff increase

In order to achieve the adjusted required revenue indicated in table 8 above, the average increase in tariffs would be 13.5%¹⁹ and the tariffs would be increased as indicated in tables 9 and 10 below.

Table 9: Approved LEC Energy Charges for 2013/14

Customer Categories	Old Energy Charges (M/kWh)	Approved percentage (%) change	New Energy Charges (M/kWh)	Adding Customer Levy @M0.0254/kWh (M/kWh)	Adding Rural Electrification Levy @M0.02/kWh large customers and @M0.035/kWh for others (M/kWh)	New Energy Charges (M/kWh)	Old Energy Charges including levies (M/kWh)	Final Tariff Percentage (%) increase
Industrial HV	0.1169	15.2	0.1347	0.1601	0.1801	0.1801	0.1599	13
Industrial LV	0.1294	15.2	0.1491	0.1745	0.1945	0.1945	0.1724	13
Commercial HV	0.1169	15.2	0.1347	0.1601	0.1801	0.1801	0.1599	13
Commercial LV	0.1294	15.2	0.1491	0.1745	0.1945	0.1945	0.1724	13
General Purpose	0.9555	15.2	1.1011	1.1265	1.1615	1.1615	1.0135	15
Domestic	0.8453	15.2	0.9741	0.9995	1.0345	1.0345	0.9033	15
Street Lighting	0.4799	15.2	0.5530	0.5784	0.6134	0.6134	0.5379	14

¹⁹ Average price increase is equal to expected total revenue divided by expected sales (M/kWh) compared to previous year's average M/kWh.

Table 10: Approved LEC MD Charges for 2013/14

Customer Categories	Old Maximum Demand Charges (M/kVA)	Percentage (%) Change	New Maximum Demand Charges (M/kVA)
Industrial HV	164.6143	15.2	189.6973
Industrial LV	192.2747	15.2	221.5725
Commercial HV	164.6143	15.2	189.6973
Commercial LV	192.2747	15.2	221.5725

The figures in tables 9 and 10 exclude VAT.

The above tariffs would enable the utility to generate **M572.4** million from its customers. This is shown in table 11 below.

Table11: LEC 2013/14 Total Revenue Based on the Approved Tariffs

Customer Categories	Approved LEC Energy Charges (M/kWh)	Approved Maximum Demand Charges (M/kVA)	Forecasted Energy Sales (kWh)	Forecasted Maximum Demand (kVA)	Total Revenue to LEC (M)
<i>Industrial HV</i>	0.1347	189.6973	211 180 198	397 501	103 853 505.99
<i>Industrial LV</i>	0.1491	221.5725	33 168 224	147 843	37 703 798.05
<i>Commercial HV</i>	0.1347	189.6973	63 332 071	177 779	42 255 838.57
<i>Commercial LV</i>	0.1491	221.5725	63 879 083	161 933	45 405 400.94
<i>General Purpose</i>	1.1011		89 236 704		98 258 004.60
<i>Domestic</i>	0.9741		248 152 462		241 725 899.63
<i>Lighting</i>	0.5530		5 693 890		3 148 861.53
Total					572 351 309.31

7.2.2 Other Charges

The Authority has been requested to review charges such as connection fee, wiring testing, wiring re-testing, survey, re-survey, licensing for wiring, meter testing and house extension. Except for connection fee, other charges to be increased are not supported by detailed information to assist the Authority in making its determination. These charges should therefore remain the same until supporting information has been provided.

For the connection fee, detailed costs breakdown has been provided. However, the request from LEC not to standardize the connection charge within 50 meters is not consistent with Electricity Connection Charge Guidelines. The current connection fees should remain in force until LEC has provided all the information regarding its proposal, especially on the implementation of the proposed charging methodology for connections.

7.2.3 Regulatory Accounts

LEC is yet to submit to the Authority Cost Allocation Manual for approval and on the basis of the approved manual and allowed revenues prepare regulatory accounts for 2013/14. These accounts will be the basis for 2014/15 preparation and submission of regulatory information to the Authority.

7.2.4 Compliance with Regulatory Decisions and Tariff

Filing and Review Procedure

Whist the company's tariff submission was partially in line with the Economic and Financial Regulatory models, full compliance and provision of accurate and reliable data to the Authority remains a challenge to LEC. Information

supporting a tariff application, such as a budget was not approved by the Board as per earlier directives by the Authority in its previous Tariff Determination and approved procedures for tariff filing and review. LEC should begin to provide evidence to support some of the allegations it makes in the application. For example, LEC alleges that it has been subjected to financial erosion by regulation. Bare allegations are not enough. Facts and evidence to support any claims are necessary for the claims to be considered during the tariff application reviews.

8. CONCLUSIONS

From its analysis of LEC's Tariff Application, the written and oral submissions from stakeholders during public consultation process, reasons, facts and evidence provided, and LEC's response to both LEWA and public comments, the Authority has found justification for a M714.7 million revenue requirement inadequate. The Authority has, therefore concluded, as follows:-

- A.** The requested 36% Increase in energy and demand charge, requested by LEC in order to meet its revenue requirement of M714.7 million, is not sufficient as energy charges for various customer categories will have to increase as follows:-
 - a. Industrial HV by 86.1%;
 - b. Industrial LV by 81.3%;
 - c. Commercial HV by 86.1%;
 - d. Commercial LV by 81.3%
 - e. General Purpose by 44.3%;
 - f. Domestic by 45.4%; and
 - g. Street Lighting by 52.5%.
- B.** LEC revenue requirement resulting from 36% increase in energy and maximum demand would be M675 472 793.00, not M714.7 million as stated by LEC.
- C.** LEC revenue requirement, after making the adjustments, is M572.4 million and to achieve this adjusted required revenue, the average increase in tariffs would be 13.5%.
- D.** The Company's return on assets is relatively low and needs further investigation and to be addressed in line with tariff restructuring exercise being undertaken by the Authority.
- E.** The Company's operating expenses are proposed to increase by 57% and this is not related to inflation, increased sales and customer connections.

- F.** LEC's staff costs increase of 31% is high and the increase is not consistent with the recommendations of the Benchmarking Study that was undertaken by the Authority; and
- G.** LEC's forecasted bulk supply costs are slightly over-estimated and would be monitored during the year and reconciled with the net under-recovery of M21.8 million from 2012/13.

9. APPROVAL

- A. The Board therefore approved the LEC tariffs that are proposed in tables 12 and 13 below.

Table 12: Approved LEC Energy Charges for 2013/14

Customer Categories	Old Energy Charges (M/kWh)	Approved percentage (%) change	New Energy Charges (M/kWh)	Adding Customer Levy @M0.0254/kWh (M/kWh)	Adding Rural Electrification Levy @M0.02/kWh large customers and @M0.035/kWh for others (M/kWh)	New Approved Energy Charge (M/kWh)	Old Energy Charges including levies (M/kWh)	Final Tariff Percentage (%) increase
Industrial HV	0.1169	15.2	0.1347	0.1601	0.1801	0.1801	0.1599	13
Industrial LV	0.1294	15.2	0.1491	0.1745	0.1945	0.1945	0.1724	13
Commercial HV	0.1169	15.2	0.1347	0.1601	0.1801	0.1801	0.1599	13
Commercial LV	0.1294	15.2	0.1491	0.1745	0.1945	0.1945	0.1724	13
General Purpose	0.9555	15.2	1.1011	1.1265	1.1615	1.1615	1.0135	15
Domestic	0.8453	15.2	0.9741	0.9995	1.0345	1.0345	0.9033	15
Street Lighting	0.4799	15.2	0.5530	0.5784	0.6134	0.6134	0.5379	14

Table 13: Approved LEC MD Charges for 2013/14

Customer Categories	Old Maximum Demand Charges (M/kVA)	Approved Percentage (%) Change	New Maximum Demand Charges (M/kVA)
Industrial HV	164.6143	15.2	189.6973
Industrial LV	192.2747	15.2	221.5725
Commercial HV	164.6143	15.2	189.6973
Commercial LV	192.2747	15.2	221.5725

The figures in tables 12 and 13 exclude VAT

- B. The current charges for connection, wiring testing, wiring re-testing, survey, re-survey, licensing for wiring, meter testing and house extension remain the same for the financial year 2013/14 until the applicant has provided justification and the Authority has considered and approved the proposed charges.

10. EFFECTIVE DATE

The effective date of the new tariffs was 1 June 2013.

11. COMMUNICATION

The decision of the LEWA Board has been communicated to the applicant, LEC, by a letter dated May 17, 2013 and to the general public on the same date via a press conference and a press release.



CHAIRPERSON THE LEWA BOARD

DATE 10 June 2013