

On Electricity Tariff Revision

On December 26th GNERC completed the process of revising the tariffs in electricity sector for the year 2017, including those for generation, transmission-dispatch, reserve, distribution and consumer tariffs. It has been decided that in future, tariff revisions will take place annually.

Despite of a number of new macroeconomic and financial and technical circumstances, and despite the general expectation of tariff growth, GNERC did not change the tariffs for residential consumers and the tariffs for high and medium voltage users (industries and organizations) were increased only slightly.

Expectations of tariff increase were justified by several factors including: sharp devaluation of Georgian Lari, growth of Enguri/Vardnili HPP tariff, increased demand for import and electricity produced at thermal power plants (TPP), higher investment needs of electricity enterprises etc. However, several major circumstances played towards tariff reduction as well:

- According to GNERC, existing tariffs already encompassed an increased share of expensive imported and TPP energy, since the previous regulation period (16 months - September 2015 - December 2016) included a higher share of cold months;
- There is an expectation of reduced prices for electricity imports .
- Commission didn't include the effective exchange rate of 2.7 GEL/USD but rather relied on official budget figure of 2,5 GEL/USDⁱ.

Finally GNERC determined that the combined effect of all these factors netted to almost zero and didn't change the low voltage tariffs at all while increasing the medium and high voltage tariffs insignificantly compared to expectations. This decision demonstrates an element of caution in avoiding the drastic tariff changes and related social or political perturbations. It also includes an element of postponing the hard decisions for future. Although the tariff adjustment at least for inflation would look be quite natural, however we cannot decisively state that the GNERCs decision was politically biased. (It has to be mentioned, that the exchange rate for TPPs is 2.78).

The tariff hearings have emphasized the once again the organizational and legislative gaps, obstructing electricity market optimization and efficiency:

- The possibility of free market competition and sound regulation is impaired by existence of vertically integrated companies who simultaneously own generation and distribution facilities and purchase electricity from their own HPPs generators. This prevents the transparency and efficiency in tariff setting and hinders the competition.
- So called Guaranteed Reserve Capacity fee covers the expenses for TPPs operation no matter how useful they are for the power system and how much energy they produce during a year. This issue is going to become more problematic in the future and cause upward shift in tariffs, along with construction of new TPPs .
- In absence of proper competition and transparency, there is an important ambiguity in wholesale electricity prices. When it comes to distribution companies the cost of buying 1kWh is defined by Ministry's allocation of cheap Enguri power through projected Energy Balance, which is far from any good industry and market practices.
- Enguri HPP tariff, despite its recent increase, does not include the needed rehabilitation expenses and does not reflect unpaid consumption of Abkhazia. It's expected that these costs will be covered from the state budget.
- Georgia still does not have a long-term strategic view of energy sector development to assess the optimal level of investment needed in different subsectors that should be properly reflected in tariffs.

The above circumstances indicate towards the necessity of reform including development of the proper market model, improving the tariff system and achieving more regulatory independence and authority. It's crucial that Georgia develops an advanced and profitable energy sector, not the subsidized one.

ⁱ *This was not uniform across the whole tariff system as for TPP generation tariff calculation 2.78 GEL/USD exchange rate was used to enable the TPPs to purchase the needed amount of gas.*