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Strategy for Sustaining the Guyana Power & Light, Inc.

Government of Guyana, Electricity and Energy Sectors

Government of Guyana

Strategy for Sustaining the Guyana Power & Light, Inc.

DATED MARCH 2007

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FOREWORD

This strategy is prepared in compliance with one of the Special Conditions prior to the First Disbursement of Phase 2 of the Investment Component of the UAEP.

In summary the Government does not intend to re-privatize the GPL within the medium term by way of seeking / offering equity investment in GPL. Instead Government will support GPL's initiatives to promote private participation through several methods, including addition of generation capacity by independent power producers and contracting of capital infrastructural works, network maintenance and certain commercial activities such as metering, disconnection and re-connection of electricity services.

Government will maintain 100% shares within GPL. In addition GPL' structure will largely remain unchanged. Over time various hinterland electrification schemes owned by Government Agencies may be merged into GPL.

1. BACKGROUND: Review of the structure of the Electricity Sector over the last decade

(a) State of the Electricity Sector in the early to mid 1990's

When the PPP Administration was elected to Government in 1992 the electricity sector was on the brink of collapse – the transmission and distribution infrastructure was in a dilapidated state and required significant amount of capital investment for maintenance and upgrades; generation was in short supply; the existing generating units lacked proper maintenance thereby resulting in recurring outages; commercial operations needed to be modernized in order to improve the level of service to consumers; there was wide spread collusion between employees and consumers of all categories and in all places, resulting in high commercial losses through theft of electricity; many new housing schemes, squatter settlements and long standing villages along the coast never had access to electricity; and tariffs charged to consumers fell far short of recovering total costs thereby requiring substantial subsidies by Government.

In a plan to rehabilitate the then state owned Guyana Electricity Corporation (GEC), which supplied electricity to residents along the coast, the Government continued the Electricity Sector Rehabilitation Programme, which was completed in 1997. Through this project several power stations were refurbished, including Kingston, Garden of Eden, Onverwagt and Cane Field, and the transmission and distribution system on the West Demerara was upgraded. GEC installed additional new generation totaling 44 MW at Garden of Eden and Kingston Power Stations between 1994 and 1997 which was financed through lease financing with the Government providing the required down payment.

(b) Previous Privatization Schemes

About mid 1990's Government embarked on a programme to privatize the Guyana Electricity Corporation (GEC) with the aim of achieving efficiency gains, particularly the reduction of losses. The first attempt by Government to privatize the GEC was unsuccessful when negotiations with the preferred bidder, SaskPower, the principal supplier of electricity in Saskatchewan, Canada were terminated due to public pressure on the government of that province.

Following a second public tender process, the Government and America & Caribbean Power (ACP {a partnership between Commonwealth Development Corporation of the UK – CDC and the Electricity Supply Board International of Ireland - ESBI}) signed the Agreements on October 1, 1999, which required ACP to invest US $23.45 M in the newly incorporated Guyana Power & Light Inc. (GPL) and receive 50% of the shares in GPL. To cushion the impact on rates the investor's equity was phased in four tranches. In addition, ACP was granted the contract for the management of the utility – ACP subcontracted ESBI Facility Management.

Privatization was expected to bring about:

(i) phasing out of subsidies by the Government;
(ii) reliability in electricity supplies through refurbishment of existing and installation of new generation;
(iii) improved quality of service in billing and commercial services;
(iv) extension of electricity to unserved areas;
(v) reduction in losses; and
(vi) transmission and distribution refurbishment and upgrades.

Further, it was intended that in addition to the investor's equity injection, a Private Placement of 5% of shares within two (2) years of GPL's

operation, an Initial Public Offering of a further 15% by 2004 and debt financing would have contributed to the capital investment programmes.

Separate arrangements were agreed to with respect to funding for the Unserved Areas Electrification Programme (UAEP) and this was set out in GPL's Licence. GPL was committed through a licence provision to finance 25% of the project cost, up to a maximum of US $1M per annum for five years and the remaining 75% was required to be financed by a combination of sources, including consumers and Government, through support from funding agencies.

(c) Assessment of the 1999 Privatization

The strategic investor ACP assumed full management responsibility for the company under a Management Contract signed on October 1, 1999. With the consent of the Government, the other shareholder in GPL, ACP subcontracted its management responsibilities to ESBI Facility Management, which assumed operational responsibility from October 1, 1999.

The Management Contract required the management to among other things: carry out all projects envisaged by the Business Plan; ensure that the Company's performance targets were achieved, particularly loss reduction; and raise all financing required for implementation of the programmes aimed at improving the reliability of electricity supply and the efficiency of the company's operations.

There were some improvements in the company during the period October 1999 to December 2002, including the injection of a total of US $20M by ACP, increased generation capacity and availability, noticeable increases in sales up to 2001, improved cash collection, and increased productivity.

- **Rising Difficulties**

- However by the end of 2002 the following were noted:

  (i) the company's financial situation declined due to cash shortfall resulting from the unexpected rise and volatility of fuel costs and significant increases in other costs;
  (ii) losses continued to deteriorate reaching a level of 44%;
  (iii) tariffs charged to consumers had increased significantly;
  (iv) sales were on the decline; and
  (v) the company recorded a loss position during each of the fiscal years 2000, 2001 and 2002 thereby resulting in no dividend

being paid to the investor, giving rise to an untenable basis on which to raise finance.

- In 2002 the company's financial situation was exacerbated by an order of the Public Utilities Commission, which ordered GPL to repay customers approximately US $7 million for not having achieved in 2001 the overall loss target of 29% as stipulated in the GPL licence as part of the Preliminary Performance Targets.

- GPL's financial situation further deteriorated in early 2003 when tariff adjustments scheduled to be implemented from 1 February 2003 which were, on average, in the order of 16% over the December 2002 rates were blocked by an order of the court. As a result, GPL's debt to creditors mounted; scheduled and major overhaul on operating equipment were deferred; spares and other T& D materials were in short supply; and the utility was forced to implement scheduled outages to conserve fuel supplies.

- Added to this, there was growing dissatisfaction by consumers which was exacerbated by the application of a fuel surcharge amounting to a further 15% increase on tariffs, to recover the higher cost paid for fuel in the first quarter.

- Following months of negotiations on the restructuring of GPL, Government and ACP failed to reach an agreement that was satisfactory to both parties and in April 2003 the parties reached an agreement which provided for ACP to sell its shares to Government for US $1 on release of the investor's final tranche payment which was held in escrow.

- **Subsequent Arrangements**

- Following the withdrawal of AC Power and the termination of the management contract with ESBI, Government became the sole owner of GPL on April 8, 2003. The Government then appointed a new five member Board, composed of the two persons with significant experience in the electricity business (one private sector; one public servant, the CEO for State Holdings and Divestments) who had served on the GPL board prior to April 8, 2003; a director from the Guyana Trades Union Congress; a pervious General Manager of the GEC; and an Insurance Executive. These persons still comprise the current Board except the Insurance Executive.

- In April 2003 Government also filled the key senior management positions, with persons experienced in electricity utility management. From 2003 to present the utility recruited qualified and skilled

management personnel and has since restructured the organization to achieve maximum manpower efficiency. All of the key management positions have been filled.

(d) Current Public Suppliers

- Guyana Power & Light Inc. (GPL)

GPL the principal public supplier is presently 100% state owned. Through its twenty-five (25) year licence, which became effective on October 1, 1999, GPL was granted the non- exclusive right to generate electricity and the exclusive right to supply electricity to the public throughout Guyana except:

(i) the right of anyone to self generate is enshrined in the laws;
(ii) Linden, an area approximately 65 miles south of Georgetown, until such time that GPL assumes responsibility for that area; and
(iii) any other area where GPL is unable to provide a service and for which other providers might be licensed.

Looked at from another angle GPL's Licence can be described as one of a right of "first refusal to supply electricity".

At present GPL supplies areas along the coast of Essequibo, Demerara and Berbice. In addition, GPL operates isolated electricity systems in the Essequibo Islands of Wakenaan, Leguan and in Bartica. These systems total 113 MW installed capacity (exclusively thermal) and supply approximately 126,000 residential, commercial, and industrial customers.

- Omai Services Inc. (OSI)

The Linden Power Company (LPC) ceased operation in 2005 due to lack of financial and technical capacity. In March 2005 Omai Services Inc. was licensed as an Independent Power Producer and commenced operations as the power generation company in Linden. The utility currently operates a diesel power plant with a total generating capacity of 18 MW for supply to the bauxite company and to the Linden Electricity Company for distribution, in Linden.

- Linden Electricity Company, Inc.

This licensed utility distributes electricity within the Linden area and supplies about 5-6 MW of power to its 7,600 consumers. LEC also operates a 375 KVA generator in Ituni, a former bauxite mining settlement where it supplies electricity to about 200 consumers

- Lethem Power Company generates and sells electricity to approximately 560 consumers in a hinterland area. The Government of Guyana owns the company which has two diesel units totaling about 0.75 MW and a defunct two unit Moco Moco Hydropower unit of 0.5 MW.

- In addition there are other unlicensed and unregulated operators in hinterland areas including Kwakwani, Mahdia, Port Kaituma, Mabaruma, Santa Rosa, St. Cuthbert Mission, and Morakobai which are managed Regional Democratic Councils, Village Councils or Private operators.

The total public electricity demand in Guyana is currently supplied by the public suppliers while the forestry, mining, sugar and other manufacturing entities account for the balance to meet their industrial demand.

(e) Relevant Laws

The Legal / regulatory framework for the electricity sector is based on the following statutory instruments:

- Electricity Sector Reform Act 1999.
- Public Utilities Commission Act 1999.
- Guyana Energy Agency Act 1997.
- Hydro-Electric Power Act Chapter 56:03.
- Environmental Protection Agency Act 1996.
- Supply licences issued to Guyana Power & Light, Inc.; Lethem Power Company; Omai Services Inc.; and Linden Electricity Company.
- Exemptions to Licensing Requirements issued to other public and private suppliers.

2. GPL's ACHIEVEMENTS FROM 1999 TO CURRENT

(a) Unserved Areas Electrification Programme

Following the reformulation of the US $27.4 million IDB loan for the Unserved Served Areas Electrification Programme in the second semester of 2004, GPL aggressively commenced implementation of the grid expansion sub-component of the Investment Component. As at December 2006 GPL completed infrastructural works to provide over 12,000 connections to households in previously unserved areas which could be classified as, longstanding villages, new housing developments and regularized squatter settlements. Approximately fifty – four (54) communities in Regions 2, 3, 4, 5 & 6 benefited from Phase 1 of the UAEP at a total cost of approximately US $5.7 million (loan resources and counterpart resources).

Government and the Central Housing & Planning Authority provided funding for the electrification of additional areas in Regions 2, 3, 4 & 6 resulting in a further 22,000 households having access to electricity. It should be noted however that in a number of areas electrified by Government, buildings have been constructed on less than 50% of lots. Government sought to reduce complaints from lot owners that they could not move into new housing areas before electricity was available.

(b) Losses

At April 2003 GPL's system losses were calculated to be about 44%. In 2004 GPL commenced a special programme to reduce non-technical losses in the form of a house to house campaign to ascertain the accuracy of billings and verification of meter and service connections. Of the 108,000 consumers visited during field investigations, more than 63,000 defective meters were found. Consumers found tampering and those with defective meters were back-billed to the full extent permitted by law but it is compulsory that all defective meters be replaced and the new meter interface be installed.

Actions taken by GPL to curtail fraudulent activities and reduce losses include:

- Replacing and upgrading meters for all categories of consumers, including maximum demand consumers. In excess of 16,000 defective meters were replaced leaving about 47,000;
- Mandating consumers found tampering to comply with the new standards for wiring interface so as to reduce the possibility of tampering;

- Validating information on the billing system to determine accuracy of the tariffs;
- Determining whether active meters were omitted from the system;
- Review over time readings to ascertain whether there is any suspicion of tampering and defective meters;
- Where there is suspicion of tampering or defective meters field inspectors are assigned to conduct an examination of consumers installed capacity; details on the meters (manufacture, type, location of meters, type of meter circuit, type of supply), and record the ampere reading.
- Conduct frequent raids in areas where the unlawful consumption of electricity is widespread to remove illegal connections.

In late 2005 GPL commenced implementation of the Loss Reduction Sub-Component under the Unserved Areas Electrification Programme by contracting a firm with international experience in the area of loss reduction to:

- Assess and profile GPL's overall loss;
- Prioritize a programme for technical and non-technical loss reduction;
- Analyze the impact accruing benefits would have on tariffs;
- Develop a strategy for loss reduction and methodology for evaluating the impact;
- Develop a monitoring system for baseline data.

The methodology used by the Consultant for assessing GPL's non-technical losses included: (i) site surveys to residential and commercial consumers; (ii) visits and investigation of the maximum demand consumers; and (iii) billing analysis. In its Final Report presented in August 2006 the Consultant established that GPL's non-technical losses accounted for 28.79% of net generation and resulted primarily from illegal connections, defective and stopped meters and collusion of employees in billing and administration. Technical losses were computed at 11.60%.

GPL projects that its total system losses net of auxiliary use could be reduced to 12.9% by 2011. The IDB loan for the Unserved Areas Electrification Programme provides US $6.2 million for loss reduction investments. In its Loss Reduction Strategy GPL identified the following non-technical loss reduction investment initiatives in 2007-2008:

1. Installation of a new state of the art billing system.
2. Replacement of 12,500 meters per year over two years, with the intention of replacing every defective meter over time and rewiring interface to curtail the possibility of by-passing consumption.

3. Acquisition of vehicles to equip teams investigating and removing illegal connections.

(c) Tariffs Less Than Calculated

Since 2003 GPL has not implemented the full tariff increase computed under the licence. This resulted in an increase in sales following the decline in 2003.

(d) Maintaining Service Levels

Generation and network maintenance which was lagging in 2003 is now carried out in a timely basis thereby resulting in even obsolete equipment maintaining levels of 80% availability.

Two (2) 2.5 MW Electro Motive Diesel units inherited by another Government Agency, were made available to GPL in 2006. In addition, 10 MW of rented generation capacity was installed in Demerara in December 2006 to stabilize the system during the Christmas Season and for Cricket World Cup 2007.

Major rehabilitation was completed on all four 69 KV lines and over G $1B (US$ 5 million) was spent on network maintenance and meter replacement.

3. PLANS TO SUSTAIN GPL IN THE MEDIUM TERM (2007 – 2011)

GPL's Rolling Five-Year Development & Expansion Programme for 2007 – 2011 presents an optimistic outlook for sustaining the utility over the next five (5) years. The D&E Programme addresses crucial matters such as:

- Generation & Expansion Programme;
- T&D Expansion and Modernisation Plan;
- Loss Reduction Strategy;
- Sales & Revenue Collections;
- Statements on Operating Cost & Capital Expenditure;
- Funding Sources; and
- Tariff Rebalancing.

In order to maintain tariffs at the lowest possible rate, Government will continue to forego its return on capital.

(a) Generation

GPL's peak demand in the combined Demerara and Berbice Inter-connection Systems is expected to grow from 93 MW in 2007 to 109 MW in 2011. GPL predicts that 72 MW additional generating capacity should be added to the grid by 2011, of which 46.5 MW is for replacement capacity. Much of the new generating capacity will be provided by Independent Power Producers in accordance with Power Purchase Agreements.

A significant amount of the generation will be supplied from renewable energy including:

- Installation of a 13.5 MW wind farm at Hope Beach, East Coast Demerara by the developer Delta Caribbean to supply about 4 MW firm power to the grid in the first quarter of 2008;

- Construction of a bagasse fired co-generation facility supplemented by HFO fired generation plant by GUYSUCO in Skeldon, Berbice to supply 10 MW to the grid from HFO fuelled engines by the third quarter in 2007 and steam capacity of 10 MW in 2008;

- Government is committed to fostering the development of hydropower resources in Guyana. To this end the Government, GPL and the Synergy Holdings, a developer who has been steadfastly pursuing the development of the Amaila Falls Hydroelectric Project site since 1996, entered into an MOU in May 2006 which provides for 100 MW of hydropower being made available to the national grid by December 2010. As an interim measure Synergy Holding has committed to provide 25 MW of HFO fired capacity to GPL's grid by the last quarter of 2007.

Generation expansion plans for the isolated systems in Essequibo include:

- installation of a 500 kW set at Leguan in 2007;
- relocation of a 1.2 MW mobile unit from Berbice to Anna Regina 2007;
- relocation of two 1.2 MW sets from Berbice to Bartica in 2007 and 2008 respectively.

(b) Transmission Links

To enable efficiency in generation through consolidation of generating stations and reduced reserve requirement, it is necessary to link the Berbice and Demerara Systems. In addition GPL plans to install sub-stations in order to improve the quality of supply. Longer feeders will be shortened to reduce losses. Other system upgrades include:

- Frequency conversion and upgrade of the remaining 50 HZ system in Georgetown.
- Conversion of the Wartsila built Kingston Plant from 50 HZ to 60 HZ.
- Redesign of the distribution network in areas with sub-feeds.
- Improved design standards and switch from wallaba poles to concrete poles in key areas.
- Formal acceptance and construction of a new distribution system at Timehri. In this regard approaches will be made to the Bank for any excess funds allocated for grid connection to be utilized for associated infrastructural works estimated at G$140 million.

(c) Network Maintenance

GPL has over the years promoted the development of local T&D contractors through training of personnel and outsourcing of maintenance and capital works, including the network extensions under the UAEP which were carried out by private contractors.

Benefits realized in the past from this approach include: (i) improved efficiency (for instance the UAEP infrastructural works carried out by private contractors were completed ahead of the scheduled time); (ii) greater reliability of the system and reduction in energy not served due to system faults and maintenance activities; (iii) cost savings (reduced operational cost and investment in equipment); and (iv) separate roles between performance and supervision of works leading to enhanced customer service standards.

GPL will continue capacity building of private T&D contractors.

(d) Loss Reduction

During the period 2007 – 2011 GPL intends to implement a menu of measures to reduce losses to 12.9% at the end of 2011, these include:

- Replace about 75,000 meters and interface;
- Introduce more reliable and tamper resistance meters for maximum demand consumers;
- Install a state of the art customer information system;

- Seek to have stiffer penalties for persons found stealing electricity and prosecute perpetrators;
- Introduce hand held reading loggers with compatible meters.

(e) Financial & Commercial Operations

- Much of the loss reduction investments and Phase 2 grid connection will be financed from the IDB loan.
- During the period 2007 – 2011 the Government will continue to forego any dividend to allow for a cash surplus to be reinvested.
- Investments in generation capacity will be met by independent power producers.
- No funding through debt or equity injection is anticipated.
- Approximately 11.2% of the loss reduction gains will be translated into sales. Cash collection as a percentage of sales is projected at 99%.

4. PROPOSED STRATEGIC APPROACH (GPL's structure and Sector Regulation)

(a) GPL's Licence Reviewed: Significant Carve Outs

GPL operates as the principal public supplier of electricity throughout Guyana under a twenty five (25) year licence granted on October 1, 1999.

Notice needs to be taken of the significant carve outs enshrined in the ESRA and GPL's Licence, which provide that:

(i) Every person, natural or corporate, has the unquestioned right to self generate;

(ii) Others may be licensed to provide an electricity service in unserved areas wherever GPL may not be able to or is not ready to supply provided that GPL should have had the right to supply at the same conditions including prices as the default licensee.

In the context of evolving concepts and practices locally and internationally, and in view of questions asked, the right to self generate is now seen as having opened the door to companies who elect to satisfy the right of individuals to self generate, effectively competing with GPL. This possibility was not foreseen and was not intended in October 1999 when ESRA was drafted and enacted, however the Government intends to

let the possibility stand as it helps to provide pressure on GPL to keep tariffs as low as possible.

Taken altogether GPL's apparent monopoly right to supply all areas across Guyana is in effect little more than a right of first refusal. GPL in effect faces 'competition' from self generators, including those supplying equipment to satisfy self generation and those may want to supply in unserved areas.

The Government however does see and is desirous of Guyana benefiting from the potential contribution towards unifying the country by means of GPL establishing an electricity distribution grid within the reach of all Guyanese. The government looks towards the steady extension of the grids of GPL and other suppliers and the provision of electricity at industrialized locations and population clusters away from areas being served. There are a number of initiatives in this direction including one component of the UAEP, which is directed towards construction of demonstration electrification schemes in unserved hinterland communities. Further, the Government looks towards the past trend to continue interconnection and incorporation of isolated areas into GPL at appropriate times.

Hence, the Government does not contemplate any fundamental changes in GPL's licence with respect to the right of GPL and others to generate and /or supply electricity in Guyana.

(b) Unbundling Not Judged Appropriate Nor Timely

There has been much discussion and consideration on the pros and cons of unbundling GPL geographically and / or vertically.

The Government does not see merit in reversing the trend of the last three decades towards consolidation and integration of the electricity sector, particularly so in light of the small total demand in Guyana (less than 200 MW total with 100 MW on the grid), the rudimentary stage of development of electricity infrastructure, and public understanding of electricity operations in Guyana.

In the past a number of groups have approached the responsible Minister with suggestions of parceling the utility geographically; pointing to how readily the utility could be unbundled into a number of vertically integrated companies in each of a number of our administrative regions. Government does not accept proposals to unbundle GPL geographically because of the loss of economy of scale, and the loss of integrating effect of uniform electricity rates across the current grid.

One variation of the above proposes that in the future the small hinterland utilities be developed as partly owned subsidiaries of GPL which then becomes a holding company, inviting direct investment into each subsidiary separately but GPL maintaining the controlling interest in each.

There have also been proposals to disaggregate GPL vertically, separating generation, transmission, distribution and sales to allow retailing and wheeling of electricity.

Generation is already fully opened to competition. Under its Licence GPL was required to facilitate competition in generation from October 2004 for any capacity addition or replacement of a size larger than 10 MW. Further, GPL must participate in an international tender process if it wishes to provide the proposed capacity addition. All GPL's generating capacity over the next five (5) years is expected to be provided by Independent Power Producers.

Any power purchase agreement between GPL and independent power producers must be approved by the PUC and such independent power producers must be licensed to generate electricity for sale to a public supplier.

Having regard to the above considerations Government intends to maintain basically the current sector structure where generation is open to competition and transmission and distribution services would remain a limited monopoly to be carried out principally by the Guyana Power & Light, Inc.

(c) Sector Regulation Reconsidered

The current legislative framework assigns sector regulatory functions to the following three (3) agencies: Public Utilities Commission (PUC); Office of the Prime Minister (OPM); and Guyana Energy Agency (GEA).

The Public Utilities Commission is the primary agency regulating the interface between the utility and the consuming public through confirming the determination of the maximum tariff that could be charged, monitoring the public suppliers' compliance with their licence provisions, in relation to Operating Standards & Performance Targets and Development & Expansion Programmes. The respective agencies regulatory roles are outlined in the chart below:

PUC	OPM	GEA
▪ Confirms rates to be charged by public suppliers. In the case of GPL a tariff setting mechanism is established in the Licence, which provides for verification by Independent Firm of Accountants (IFA). If the IFA issues a certificate of non-compliance, the PUC will make a determination on the matter. ▪ Approves PPAs between IPPs and any public supplier including GPL; ▪ Authority to recommend suspension or cancellation of suppliers licence; ▪ Enforces expansion and Development Programmes for GPL and approves and enforces EDPs for other public suppliers; ▪ Conducts hearings, performs investigations and in general receive and handle complaints filed against public suppliers.	▪ Formulates and implements national energy policy and sector legislation and regulations; ▪ Issues and enforces terms and conditions of licence to public suppliers and independent power producers and exemptions from licensing requirement; ▪ Modifies, suspends and revokes licenses; ▪ Approves GPL's annual rolling five year EDPs.	▪ Provides advice to the Minister on the issuance of licences and modifications and extension of licences; ▪ Advises on the national energy policy; ▪ Monitors and regulates the importation of petroleum products. ▪ Monitors the development of any hydroelectric project.

In addition, GPL has to conform to all existing and applicable laws including those relating to occupational, safety and health; technical standards and environmental issues. Two special agencies need to be recognized on the question of regulation; these are the Environmental Protection Agency and the Government Electrical Inspectorate, with regulatory roles as follow:

EPA	GEI
▪ Determines requirements for environmental impact assessments and issues environmental permits; ▪ Formulates environmental regulations.	▪Inspects electrical installations to endure compliance with required standards and issues Certificates of Compliance; ▪ Licenses electrical contractors and maintains a register of such contractors; ▪ Determines any dispute between a public supplier and consumers in relation to the accuracy of meters.

The above approach to sector regulation is efficient and workable considering the limited resources in Guyana and the small electricity market that now exists. Similar to the position in a number of CARICOM countries, it is in line with Government's policy for the PUC to evolve into a fully autonomous Fair Trading Commission to regulate all sectors, where some degree of regulation is considered appropriate according to the laws, regulation and licenses prevailing in the sector.

Government intends to maintain the current regulatory structure whilst strengthening the capacity of the various regulatory agencies to enable such agencies to better undertake their individual responsibilities. To this end, under the Institutional Strengthening & Capacity Building Component of the Unserved Areas Electrification Programme the PUC and GEI benefited from requisite training and acquisition of equipment and tools to enhance capacity building. In addition new Technical Standards & Wiring Installation Regulations are expected to be promulgated by mid 2007.

5. GOVERNMENT'S DECISION ON GPL RE-PRIVATIZATION

(a) A brief review of the earlier decision to privatize is appropriate.

The Government of Guyana arrived at the policy decision to privatize the operations of the Guyana Electricity Corporation (GEC) only after repeated detailed debates. The benefits expected, were the universal ones including:

- Privatization would open the door for the private sector to enter the utility with its investment money, management skills and a focus on the bottom line for which the operation must be made efficient and effective.

- Establishing full cost recovery prices, ending historical Government subsidized prices which proved to be a burden on the Treasury, and which paradoxically offered greater benefits of subsidies to the better-off citizens who could pay for much greater subsidized consumption than less well off citizens.

- Full cost recovery prices would lead to more rational and sustainable economic choices by all citizens.

- A privately or partly privately owned and operated utility is not obliged like Government to be lenient to everyone, and would have more leverage to compel workers and the public to conform to the better norms achieved internationally.

- Price increases would be cushioned by improvements in the operations.

However these benefits were not to be realized without perceived risks:

- There can be surprisingly large increases in tariffs because the full extent of direct and indirect subsidies is often not realized. Further where a large percentage of the population has been finding their personal budgets already tight there will be significant resistance to allocating more money to electricity.

- Amongst the hidden subsidies were foregone earnings on capital which implicitly set the worth of the state owned utility at zero: it was no surprise that the higher the valuation put on the facilities to be privatized, the higher the subsequent tariffs.

- Foregone depreciation charges often reflected in a declining state of equipment is another unmet, hidden cost.

- The capitalization of GPL had the potential of adding 50% to the tariff just before privatization.

- The incoming top managers from developed countries would be receiving compensation up to 100 times that of lower level workers in developed countries. In the case of GPL, Management Fees added about 17% to tariffs at the time of privatization and about 9% to tariffs at the time of the departure of ACP.

It remains Government policy to seek the gains of privatization whilst limiting the upward pressure on prices by requiring the utility to:

(i) Sustain and then expand its current operations;
(ii) Require improvement in the performance of all employees and take measures to end collusion amongst the employees and customers to defraud the utility;
(iii) Maintain the lowest possible tariffs as a result of cost cutting and cost saving initiatives.

(b) Policy regarding private investors in GPL

Government saw the Shareholders and Management arrangements with AC Power as a transitional arrangement, which in 10 to 20 years would take the electric utility in Guyana to the following state:

- Equity being widely held by the public in Guyana;
- The Board elected directly by the shareholders, appointing and supervising directly the top managers of the company;
- Top managers coming largely from the development and promotions of Guyanese from within the ranks of employees.

The vision outlined above was reflected in the following:

- the intention after the expected favourable financial performance of the first two years to offer 1% of shares to each of five(5) widely held financial institutions in Guyana;
- the planned offer within five years of up to 20% of shares to the public in Guyana diluting the shareholdings of the Government and ACP to 40% each;
- the management contract was limited to 10 years with a provision that it would fall away even earlier at such time as the shares of ACP fell below 25%.

The Government's retention of 50% of equity was to maintain enough presence to manage this transition.

In this regard Government in 2004 solicited interest from local widely held institutions in Guyana (banks, insurance companies, private sector businesses). Besides adding equity, raising local financing was seen as offering the additional important benefits:

- a desirable learning experience for Guyana and Guyanese in mobilizing widely held funds for investments;

- a desirable reduction in the un-invested liquidity which the Government steadily needs to 'sterilize' at some cost to the Treasury;

- creating a wide identity between investors and consumers: harmony should be more readily arrived at between the differing interests of investors and consumers.

- an encouragement, possibly necessary, for earnest foreign investors to return to GPL.

This exercise generated little interest from local investors who had not yet developed the appetite for such large investments. A subsequent attempt to raise financing for the Berbice Bridge proved successful.

Government has given serious consideration to the feasibility of attracting foreign investors in the electricity utility, recognizing that a stable and reliable supply of electricity is critical to the overall economic development of the country.

In this regard the Government believes that in any case time must elapse and GPL must develop a new image, for the following reasons:

- ACP's failure to earn any dividend during the first three years of GPL's operation would undoubtedly be a negative factor.

- ACP's withdrawal leaving its investment behind would reinforce the loss of appetite of investors internationally to invest in electric utilities particularly in developing countries.

- Consumers' and regulators' confidence that private investment would result in improved efficiencies in the utility must be restored.

- Consumers are extremely sensitive to higher electricity rates in the presence of seemingly large returns/profits to investors along with high management fees.

(c) How Government views its participation in the sector

Whilst Government will continue to receive any earnest credible proposal to step into ACP shoes, for the immediate future, in view of the current reduced appetite of international investors to invest in electrical utilities particularly in developing countries, and in the particular circumstances

of Guyana, Government intends to maintain its position as sole holder of shares in GPL.

In about five years, that is by 2012 Government will reconsider its position on the re-privatization of GPL by which time the utility's system performance would have improved as a result of capital investments. At this point the GPL would have achieved the level of performance required to attract investors.

Meanwhile, Government will support GPL's decision to involve private participation through power purchase arrangements with private developers of power and encourage the outsourcing of transmission, distribution and commercial activities.

GPL will remain as a private limited liability company registered under the Companies Act. GPL's Licence will be reviewed to determine what changes might be required to:

- determine what incentives, if any, could be incorporated in the licence / rate structure to promote improved service, maintain cost effective prices and allow the utility to reinvest surplus;

- review the tariff structure and determine what method of tariff rebalancing should be applied that offers economic pricing to the different categories of consumers and thus serves to retain the large users and aid the utility in winning back the large consumers who moved to self generation;

- evaluate in what areas of regulation the PUC should be strengthened and the forms of affordable capacity building required for the regulator to effectively monitor and benchmark the performance of the utility to detect early stages of non-performance and enforce timely corrective action;

Consideration will also be given to possible amendments to the Electricity Sector Reform Act 1999 to provide stiffer penalties to persons found illegally consuming electricity.