REPORT OF THE MEETING OF EXPERTS ON BASES FOR ELECTRICITY RATES IN LATIN AMERICA

Addenda and corrigenda
ADDENDA

Some important conclusions

1. It was agreed that the average price for the sale of electric power should cover the average cost of the service, including a reasonable profit.
2. Given "normal" credits from international agencies, it was considered feasible to finance a moderate expansion of electric power services (at an annual rate of 6 to 8 per cent) out of the company's own resources, by means of depreciation funds and the reinvestment of profits. If higher rates of expansion were to be maintained, external contributions would have to be increased.
3. It was agreed that, essentially, there were two different methods, in legislation governing electricity, of ensuring a return on capital invested:
   (a) The first is based on "the principle of a fair return on the enterprise's net frozen investment" (in accounting terms, this method starts out from the entries under the enterprise's assets);
   (b) The second is based on "the principle of a fair return on the stock or risk capital invested" (in accounting terms, this method starts out from the entries under the enterprise's liabilities).

Analysis of the advantages and disadvantages of these two methods led to no definite conclusion as to the net superiority of one over the other (both are applied in Latin America).
4. The rate of return on capital invested should be the same for both State-owned and private capital, in the view of the majority of the participants.
5. It was generally agreed that a reasonable minimum legal rate of return would be the rate of interest at which the State contracted its debts; the legal maximum rate of return might be equivalent to the opportunity cost, or else to an index based on the ratio of business profit to public utilities profit.

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6. It was agreed that a clear distinction should be made between the legal rate of return on investment and the opportunity cost (or accounting price) for the purpose of investment decisions by the electricity enterprise. As a rule, the second figure should be higher than the first.

7. It was considered possible to envisage a rate structure so conceived as to imply certain subsidies, always provided that they were clearly identified and were an expression of an integrated economic and social policy.

8. To ensure that the rate structure was conducive to rational decisions by the consumer, discrimination in respect of hours of use should be linked as closely as possible to the additional costs of the service.

9. It was agreed unanimously that the prices of the various energy resources would have to be co-ordinated, in order to obviate decisions as to their use which were anti-economic from a national standpoint.

10. Since it was recognized that the principle of incentives to improve efficiency (both technological and administrative) was not incorporated in even the most up-to-date legislative systems in Latin America, it was recommended that the benefits of net reductions thus obtained in the unit cost should be distributed between producer and consumer, after deduction of any benefit resulting from changes not due to action on the part of the enterprise, such as variations in the prices of inputs. To preclude the possibility that rapid technological progress, or the fact that the enterprise started at a very low level of efficiency, might be reflected in returns out of proportion to the capital invested, a fresh basis of comparison would have to be established at regular intervals (say every five years).

11. It was considered that a system of criteria for the allocation of costs by consumer in an interconnected system should be formulated in Latin America, for which purpose the establishment of a working group was recommended.

12. Stress was laid on the desirability of establishing a standard accounting plan, primarily to value assets by physio-functional groups, and also to record utility costs by function. Its main purpose would be to provide a basis of comparison for Latin American statistics. It was requested that a working group should be set up to this end.

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13. It was generally agreed that electricity companies should include in their annual reports to stock and bondholders a balance-sheet drawn up in accordance not only with corporation regulations but also with the regulations established by the electric power industry.

14. It was felt that the benefits obtained from loans contracted by electricity companies on the basis of official guarantees or the assumption of financial responsibility by the State should not be monopolized by the undertaking concerned.

15. It was agreed that it would be advisable to make new individual revaluations of the assets of electricity enterprises at reasonable intervals (say every five years), while during the intervening periods an automatic revaluation system on the basis of an appropriate and generally applicable index should be kept in operation.

16. A principle similar to that adopted at the Conference on Fiscal Policy (E/CN.12/638) was advocated — namely, that State enterprises should be self-financing, through the adoption of adequate rates for the utilities supplied.

17. It was emphasized that all State electricity enterprises, even those acting under the authority of the Executive, should be given a degree of functional autonomy sufficient to allow them efficacious freedom of movement.

/CORRIGENDA
CORRIGENDA

Paragraph 21, line 2 For "financed assets" read "assets financed by the consumer"
Paragraph 32, line 3 For "intensity of the electricity service" read "intensity of use of the electricity service"
Paragraph 37, lines 1 and 2 Read "...the rates, calculated according to each of the methods referred to..."
Paragraph 40, line 2 For "three different means" read "recourse to three different sources of funds"
Paragraph 41, line 1 For "this distribution is also treated differently" read "these remunerations are also accorded different tax treatment"
Paragraph 42, line 3 For "prestige" read "responsibility"
Paragraph 44, line 7 After "user" insert "owing to possible ignorance of some of the variables of the problem"
Paragraph 47, line 11 For "loans" read "additional loans"
Paragraph 53, line 5 For "redress the legal inequality" read "redress the effect on rates of the legal inequality"
Paragraph 58, line 6 For "development" read "financial stability"
Paragraph 58, lines 7 and 8 For "an electricity enterprise" read "another electricity enterprise"
Paragraph 59, line 4 For "something similar" read "an expenditure similar"

Paragraph 102, lines 3 and 4 Read "demand and power costs. But even if this problem is solved, such questions arise"
Paragraph 103, lines 7 and 8 Read "in chronology, whereas in other production processes it results from the number of different products manufactured (the product-mix of a petroleum refinery, for example). Nevertheless, the basic problem"

Paragraph 109, lines 7, 8, 9, 10, 11, 12 and 13 Read "In Chile, there have been until recently three fundamental discrepancies between the two types of legislation: (i) for tax purposes, interest on loans is regarded as expenditure, whereas electricity legislation adopts the principle of method I; (ii) the charges admissible for depreciation were formerly not the same in both; and (iii) different criteria were used for the valuation of assets. The last two disparities were eliminated a short while ago."

/Paragraph 113
Paragraph 113, line 4  For "considerable" read "great"
Paragraph 114, line 8  For "anti-economic for" read "harmful to"
Paragraph 127, lines 2, 3, 4 and 5  For "preferential treatment should be accorded - especially during periods of acute inflation - to enterprises that had succeeded in thoroughly compensating for a lower rate of return" read "by its means enterprises that had succeeded in thoroughly compensating for a lower rate of return might find themselves in an unduly privileged position, especially during periods of acute inflation"
Paragraph 131, line 5  For "replace" read "restore"
Paragraph 164  Delete