

## Tariff Reform Roadmap

Sri Lanka power sector is going through a reform process, and in line with that process the tariff setting process shall also be reformed to suit the new industry structure. Ministry of Power and Energy has already set up a Working Group to study and propose improvements in the current processes to suit the reformed industry. PUCSL being the economic regulator is taking a forward-looking approach and is in the process of reforming the tariff setting processes.

### *Envisaged reforms and the implications on the tariff setting process.*

The draft Bill to reform the electricity industry has been submitted to the Cabinet of Ministers and the envisaged reforms is expected to subdivide the Ceylon Electricity Board to many small corporate entities, including several distribution utilities, transmission utility, Independent System Operator, several Generation companies and so on. While the current Tariff Methodology is mostly suited for such structure; where the tariff for each activity is already reviewed and approved separately, there may be few adjustments required to fully accommodate the new structure. The envisaged reforms also provide for a separate National Tariff Policy to be declared by the Minister upon recommendations by a Policy Advisory Council.

Considering all the new developments, a road map to reform the tariff setting process is proposed as given in the sections below.

### *Phase 1: Preparation and Consultation Stage*

Assuming the new legislation is in force by end of December 2023, the first stage from January 2024 to June 2024 is named as preparation and consultation stage. The main activities in this stage are listed below;

- Develop and consult on proposals on the principles to guide future tariff regulation, including on matters such as benchmarking, end-user tariff determination, cross-subsidies, and responsibility for each step of a tariff review process, eg, who determines the end-user tariff. These can subsequently form the basis for the National Tariff Policy, and for the guidance on cross-subsidies to be issued by the Minister, once Sri Lanka Electricity Act (SLEA) has been approved<sup>1</sup>. The development of these proposals will require coordination with PUCSL as well as the Ministry of Power and Energy (MOPE) and Power Sector Reform Committee (PSRC).

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<sup>1</sup> It is important to confirm whether the National Tariff Policy can be adopted after the SLEA has been approved but before it becomes effective. This may depend on whether the entity responsible for issuing the National Tariff Policy will be established before the SLEA becomes effective, or whether another entity may have the ability to do so before this. Any delay in the National Tariff Policy becoming effective will delay the approval of subsequent regulations and methodologies (although we expect that, in practice, they will be developed

- Review and consult on the existing tariff methodologies and make proposals, including outline drafts, on amendments required to accommodate the power sector reforms. In the first instance, this will reflect the reallocation of sections of the existing methodology to new headings that represent the new corporate entities<sup>2</sup>. Other aspects of the tariff methodology that may be reviewed include the determination of consistent and transparent cost-reflective fixed (and/or demand and/or reactive power) and variable (including time of use) costs and charges for all customers, notably distributed generators and net metering prosumers, and for new adjustment mechanisms under envisaged reforms.
- Review and consult on customer tariff structures to establish the optimum number of categories and application of volume differentiation, while also making tariffs more easily understandable.
- Review and consult on existing timelines, processes, and templates for tariff filings and for PUCSL's consultations and decisions on these filings and make proposals on revisions and enhancements required to improve consultation processes, to address the identified weaknesses and the requirements of envisaged reforms.
- Review and consult on existing subsidy mechanisms, the quantum of subsidies provided, and targeting and payment mechanisms. This should result in a clear methodology that identifies deserving customer groups, the value of the subsidies provided to them, the source of those subsidies (with cross-subsidies being phased out, per the current methodology guidance), the mechanism for identifying beneficiaries, and the mechanism for paying the subsidies.
- Commence drafting and consulting on the National Tariff Policy, supported by the other activities in this phase. The final version of the SLEA will identify which entity will publish the National Tariff Policy. If this is an entity that will be established by the SLEA, then drafting will be led by another entity such that publication can be made as soon as the relevant entity is established.
- Identify opportunities for supporting CEB and PUCSL with data collection, organisation, and submission, including upgrading information management systems and determining customer-specific data such as load profiles.

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together), and then any tariffs for the new successor companies that should be in place on the day they are created, or risk the requirement to prepare interim tariffs until the fully reviewed tariffs can be applied.

<sup>2</sup> For example, section 2.5.2.2, detailing the methodology for determining the Forecast Transmission Tariff, will be reallocated from under the Determination of Bulk Supply Tariff (2.5) to a new section specific to Transmission Charges and Tariffs for the new transmission company, leaving the Determination of Bulk Supply Tariff to focus on determining the costs and charges for the operations of the single buyer and system operator, with the bulk supply tariff then adding the charges for power purchases and transmission that are determined in other sections of the methodology.

- Work under this phase can begin immediately. Proposals may need to be adjusted to align with the final draft of SLEA, as approved by Cabinet, and the version approved by Parliament, and so the phase will only complete after these dates.

#### *Phase 2: Jul 2024 to Jan 2025 – Implementation*

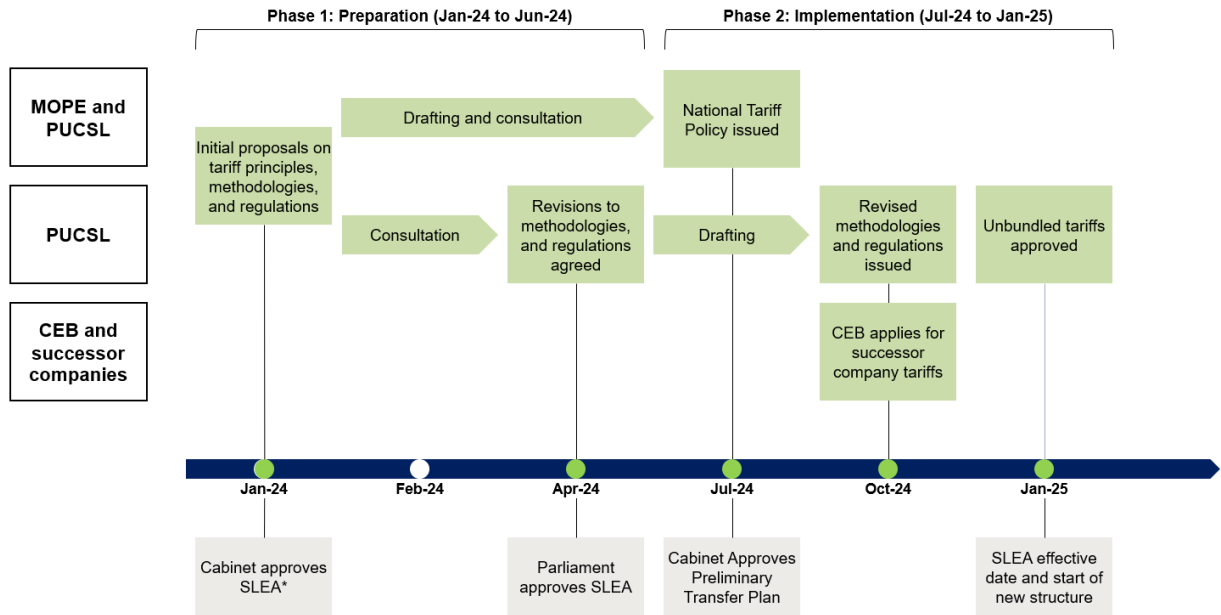
- Issue the National Tariff Policy that is drafted and consulted on in Phase 1. This assumes it is possible to issue the National Tariff Policy even before the SLEA becomes effective.
- Consult on and issue revised methodologies and regulations. These need to be in force no later than the effective establishment of the successor companies, and ideally earlier as they will be needed to guide the determination of tariffs for the new successor entities. Drafting these documents together with the National Tariff Policy will ensure that all are aligned.
- Undertake a full revised tariff assessment (applied for by CEB to PUCSL) prior to the SLEA becoming effective, determining regulated tariffs for each of the successor companies. The new tariffs should become effective on the same day as the SLEA. The time required to complete this activity will determine when it starts, such that it can be completed by the time the SLEA becomes effective. It may include support on drafting the final methodologies and regulations.
- Identify all tariff function responsibilities for each of the successor companies.

#### *Phase 3: Feb 2025 to Jan 2026*

- Further revise methodologies and regulations to conform to the National Tariff Policy, as formally approved and issued, and any changes introduced through the Final Transfer Scheme.
- Make the initial and successive regular adjustments to the bulk power purchase and supply tariffs (incorporating generation, transmission, and bulk purchase and system operation costs), which are adjusted quarterly under envisaged reforms, and transmission and distribution tariffs, which are adjusted annually.
- Monitor the operation of the revised methodologies and regulations and adjust as necessary to take account of actual experience.

This road map does not include specific provisions related to the introduction of open access, other than the separation of distribution and supply tariffs as required by envisaged reforms. The need for and scope of additional methodologies and regulations required for open access will depend on the design of the future power market which, in turn, is dependent on separate proposals to be developed by MOPE and PSRC.

The current ADB TA will provide support through to the conclusion of Phase 1, after which it is expected that MOPE and PUCSL will continue implementation.



Note – PUCSL actions of Phase 1 will start with the receipt of the Cabinet approved SLEA by PUCSL.