Validation Workshop /Meeting Report

On

Competition Policy and Regulations in the Energy Sector in Kenya

Held on

3rd July 2009

1.0: Introduction and opening remarks.

The programme began by a brief introduction of participants to the meeting. The opening remark was made by Mr. Samson Awino, the Programme officer of CUTS ARC, Nairobi; in charge of competition Policy and Economic regulation Programme.He unraveled the CUTS programmatic activities under the competition policy and Economic regulation programme as envisaged in the CUTS Strategic plan 2009-2013. He also highlighted and affirmed the interface between the research project and the CUTS programme on competition policy and economic regulation. The meeting composed of the peer reviewers that were engaged in the analysing the draft of the research report.

2.0: Presentation of the Draft Report.

The presentation of the draft report was made Mr. Christopher Onyango, the Lead Researcher .Mr.Onyango made a detailed overview of the research project report and its findings. The following is a brief summary of the key research findings:

- The monopolies and Price Commission (MPC) has limited independence.
- About 86% of power is generated by a public utility.
- It is only the generation segment of the electricity sector that is subject to the national competition laws and regulations.
- There is weak enforcement of laws in petroleum sub-sector i.e. use of moral suasion by regulators.
- Existence of weak /lack of effective coordination between MPC and Energy regulatory commission (ERC).
- There are in-adequate technical capacities in both MPC and ERC.
- Enforcement capacity is constrained by staff shortages and technical capacity limitations affecting: (i) setting and monitoring standards for factories, buildings and electrical appliances; (ii) collecting, collating and maintaining energy data; and (iii) energy conservations and efficiency in the electricity subsector.
- There is Limited independence in decision making in the Electricity Sub-sector.
- There is law transparency ratings i.e. (62%) thought that the ERC is not transparent in its decision making.

2.1: The following are major problems in the Electricity Sub-Sector (% of Response) depicted in the research project.

Generation	
Monopoly by KENGEN/dominance behaviour	**44.6%**
Cumbersome licensing procedures	**37.3%**
Dependency of hydropower	**9.1%**
Transmission	
Inefficiencies	**45.2%**
Monopoly	**35.5%**
Transmission Losses	**12.9%**

Distribution	
High tariffs	36%
Monopoly/No competition	32%
Corruption	12%
Inefficiencies	10%

2.2: The following are major problems in the petroleum Sub-Sector (% of Response) depicted in the research project.

- There is Complex Regulatory framework i.e. functions shared by Ministry of Energy, ERC[1], NEMA[2], KEBS[3], PIEA[4], Provincial Administration and Local Authorities etc
- Lack of clear guidelines on coordination affects information exchange amongst various institutions
- Market Concentration: HHI 1650; CR 72.6%.

2.3: Challenges and constraints in the Competition-Related Regulations.

- Limited independence or autonomy from government
- Limited funding thus affecting staff recruitment, M&E and enforcement
- Existing laws do not provide for consumer protection and fair trading (incorporated in CB 2009)
- Exemptions of the public sector from application of the act (incorporated in CB 2009)
- Weak provisions for sanctions, fines and penalties

2.4: Challenges and constraints in the Electricity sub-Sector.

- Limited enforcement powers for competition-related regulations
- Uncoordinated enforcement of competition related regulations
- Inadequate technical and professional staff.
- Poor Infrastructure affecting data collection, information exchange, M&E etc
- Weak governance of transmission network and pricing structures

2.5: Challenges and constraints in the Petroleum sub-Sector.

- Inadequate capacities for regulatory efficiency and effectiveness
- External factors (international oil prices, global security etc)
- Enforcement of standards and quality
- Weaknesses in existing laws and regulations.

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[1] Energy Regulation Commission.
[2] National Environment Management Authority.
[3] Kenya Buarue of Standards.
[4] Petroleum Institute of East Africa.

3.0: Workshop Deliberations and Comments from the Peer Reviewers.

3.1: The following is a brief summary of the deliberations from Ms.Beldine Omollo:

- The exact name of the document or source of secondary information should be included. This is important in case the reader wants to refer, confirm or verify the information and the source.
- Whereas it is important to give variables such as international prices of crude, it is also equally important, for comparative analysis, to report on or state their effect on local market prices.
- The correct interpretation of Section 5 of the Monopolies Act is that only practices of public enterprises (not public enterprises themselves) that have express provisions under their respective Laws are exempted from the provisions of the competition Law. In fact this section should be read together with section 73 of the same Law which subjects state corporations to competition enforcement.
- The structure of the Monopolies and Prices Commission does not include the Tribunal and the High Court since the two institutions are independent in terms of decision making. They can (reject), accept or modify the decision of the Commissioner.
- The market structure of the petroleum industry has changed a lot in recent years. For example BP and Chevron sold their stakes to Shell and Total respectively. It is important for the report to capture the changes.
- The most effective way of regulating prices of monopoly firms is to set a price cap and not a revenue cap. Profit motivated firms may device other ways of increasing revenues such as restricting production or supply in order to push up prices (and revenues). Price caps are more effective because it makes it necessary for the firm to device ways of minimizing costs through R&D, new innovations, etc. In this way, it will be able to promote consumer welfare through increased efficiency, and probably lower prices.
- In Kenya, the relationship between sector regulators and the competition authority is cordial. CCK and ERC have explicit competition provisions in their respective Laws but this has in no way affected the relationship between the two bodies and the Commission because of the informal mechanisms of consultation. The Commission always consults with sector regulators when handling cases falling within each regulator’s purview.
- The argument about the lack of competitive pricing within the electricity sub- sector is neither here nor there. Recall that price controls were made redundant but not officially repealed by Parliament. Therefore, MPC can still invoke the provisions of Part IV of the Law by controlling the price of electricity since it is provided by a monopoly firm. MPC is therefore not entirely powerless in this respect.

- It is also hoped that the enactment of the new Competition Bill 2009 which contains consumer welfare provisions will favorably address exploitative tendencies of monopoly firms.
- Though the appointment of the Commissioner is not clear in the Law, both the commissioner and other members staff of the Monopolies and Prices Commission are recruited under the Public Service Commission regulations.
- It is impractical for a macro regulator such as the Monopolies and Prices Commission to have an array of expertise in all jurisdictions or fields. This has necessitated the Commission to consult in areas it is deficient in. Similarly, sector regulators consult the Commission on competition matters.
- It is important to use the most current data (where possible) while undertaking a study because it gives the precise and correct facts required for drawing conclusions and recommendations.
- The structure of the Report is okay. However, more should have been done in giving clarity and precision on the Report contents
- The study objectives were satisfactorily addressed. A few study findings relating to aspects of competition and sector specific regulations were inaccurate as I have outlined above
- The Conclusions and Recommendations are true reflections of the study findings. However a concrete and detailed assessment of successes achieved through the reforms. Such assessment should include:
    a) Assessment of financial performance of the industry/ sector e.g. financial stability, efficiency improvements of the system, etc
    b) Assessment of electricity supply as a service to the public e.g. access, affordability, quality, etc
    c) Assessment of the performance not in isolation but in integration to development of the country e.g. sustainability, job creation, sovereignty, etc
- Lastly, it is important to note that the structure of competition policy and interplay between institutions is not necessarily predetermined by the existing legal frameworks. In some cases this may be the result of political and practical considerations such as management of existing human and financial resources, the development and size of the sector under consideration and the level of competition that exists in the market.

3.2: The following informs a brief summary of the deliberations and views from Dr.John Bonuke, Sector Regulation Expert.

- The executive summary in the report should include a summary of scope of the study and methodology .The research design should be stated clearly, in the following order; Research design; Sample design; Data source; Data analysis; Study limitations.
- **Table-8** should include ownership in terms government or Independent Power Producers and fuel used to generate the capacity. This will clearly indicate where investments were concentrated after reforms by independent power producers.
- **Table 10**-The units should be indicated i.e. Whether it is in MW or GWH and should explain the trend i.e. growth rate and relative shares.

- Information in **Figure 5** can also be supported by available data from the annual reports of KPLC. It is also better to explain the trend i.e. in terms of Growth rate which will clearly show the gap and the rate in electrification i.e. between rural and urban.
- The sources in **Figure 10** and **table 13** should be indicated.
- In the Conclusions and recommendations, the suggestions recommend are over-generalised not specific for example suggestion **2, regarding strengthening independence or autonomy of regulators.** The direct action points should be included in the recommendations.
- Furthermore, the loopholes that exist in the regulatory framework should be pin-pointed and urgently recommend the immediate solutions. For instance it has been realized that the non-effectiveness of the management of the energy sector in the country is due to interference from government especially the appointment of commissioner members, the chairman is appointed by the president of Kenya, while the other are appointed by the minister, this appointment situation is considered to significantly undermine Energy Regulatory agency's autonomy.

3.3: The following informs a brief summary of the deliberations from Mr. David Ongolo, Competition Policy Expert.

- All the reference cited should be included in the bibliography/list of reference. For instance Green et al (2006) is cited but not included in the reference.
- There are several places where the figures mentioned do not agree with the text. For example on pg.23,…..there was a large price reduction in the regulated transmission and distribution charges in the UK from 30% to 50% respectively between 1993 and 2005(Green et.,2006)
- Need to relate the findings more to best practice as reviewed in the literature review and contextualizing these to the Kenyan situation.
- The IRM model is well discussed for the subsectors in terms of its attributes though not all the 10 attributes of the IRM have been adequately discussed.
- The section on the specific interface ;gave a critique how different approaches relates to different regulator .However the section failed to bring out what is best for Kenya.

3.4: The following informs a brief summary of the deliberations from Mr. Joel Imitera, Senior Manager, Economic Regulation, Energy Regulation Commission.

- **Reference to Petroleum Act Cap.116 in the paper**: This piece of legislation is no longer in existence. The Act was consolidated with the Electric Power Act of 1997 into the Energy Act No.4 of 2006.
- **Reference to Electric Power Act (EPA) of 1997 in the paper**: This piece of legislation is no longer in existence. The Act was consolidated with the Petroleum Act Cap.116 into the Energy Act No.4 of 2006.
- The paper variously states that there is shortage of technical capacity within the regulator to effectively deal with its mandate. Kindly motivate this statement by stating competencies are necessary and therefore missing within ERC.

- The paper suggests signing of agreements between ERC and the monopolies commission as a way of increasing market competition. Please note that the two organizations are established by Acts of Parliament and any agreements outside these legislations would be difficult to enforce.
- Some statistics are very old. The per capita electricity consumption and electricity access rate are uplifted from the Energy Policy of 2004. The profile has changed and the statistics need to be updated.
- Electricity Consumption and sales tables: the numbers should be validated wit the annual accounts of KPLC and KenGen.
- The paper variously states that the petroleum market is concentrated, oligopolistic and uncompetitive. Evidence should be provided by computing some concentration parameters such as Herfindahl-Hirshman Index (HHI), Concentration Ratios etc.
- Reference of Ministry of Energy as the administrator of the Rural Electrification Programme. This is not correct as the rural electrification programme is now under the Rural Electrification Authority. The Ministry gives policy direction and seeks funding from exchequer and other sources.
- Reference to the current institutional structure in the power industry as the purchasing agency model. The industry terminology is the Single Buyer Model where KPLC buys power from all generators for onward transmission and distribution.
- The further unbundling of transmission from KPLC has already been implemented with the establishment of the Kenya Transmission Company. A geothermal development company has also been set.
- The generation capacity from IPPs does not include 26MW from Mumias that started operations in May 2009.
- Reference to price cap regulation in the power industry in Kenya: The model applied in Kenya is Rate of Return Regulation.
- Reference to Government interfering with tariff setting: Evidence of interference by the government should be provided.
- Reference to Ministry of Lands as the ones that issue construction permits for petroleum installation: These permits are issued by ERC under the Energy Act
- Reference to “observance of stickiness in retail petroleum market”: Sticky prices should not be observed but validated by undertaking a pass through analysis of the prices. References to oligopolistic structure should be motivated by empirical evidence/data.
- The structure of the paper needs to be better organized. The study recommendations should seem to stem from the study analyses and should be in tune with the challenges facing the sector.

4.0: Conclusion, Way forward and Closing Remarks.

Mr.Chrotopher Onyango agreed to improve the report and to produce the first final draft of the report against the proposed comments from the reviewers. Finally, Mr.Clement Onyango, the Centre Manager for CUTS CITEE (Centre for International Trade Economics and Environment) gave vote of thanks to the research team and to the reviewers in the Closing remarks of the meeting.