



N A R U C
National Association of Regulatory Utility Commissioners



ERB/NARUC REGULATORY PARTNERSHIP

REGULATORY AUDIT FRAMEWORK

ERB/PUC 3rd Activity, 22/03/06
Lusaka, Zambia



Introduction

- One of the key mandates of the ERB is to monitor the performance of undertakings.
- Regulatory audits are one major tool that assists regulators in carrying out their monitoring role.
- The ERB has been in existence for 10 years now. During this period, various regulatory processes have been developed as the ERB continues to build its regulatory capacity.

Introduction

- One of the ERB's key tasks for 2006 is to commence annual regulatory audits of electricity utilities.
- To this end, the department of Economic Regulation is developing key performance indicators to form the basis for the audits due to begin in the third quarter of 2006.
- Additionally, the department is in the process of developing an audit framework that will define the scope and parameters of the regulatory audits.

Purpose of Regulatory Audits

- The main purpose of these audits is to ensure that utilities are being fair to the consumers by following standards required by the regulator and improving their operations to facilitate savings to the consumers.
- In other words, they help restrict the utility's propensity to pass on their inefficiencies to the consumer through user fees and tariffs.
- Audits also help ensure the financial viability of the utilities, thus guaranteeing security of supply

Scope of Regulatory Audits

- There are various types of audits carried out by utilities. Common ones include:
 - Financial Audits – mainly connected to the tariff/rate process, e.g. verification of costs and asset values for purposes of ascertaining the reasonableness of revenue requirement claims.
 - Management Audits – Broader in nature and normally done after about 3-5 years. They assess management effectiveness and operating efficiency.

Regulatory Audit Models

- Dedicated Audit Teams:
 - This is where the regulator has set up a specialised audit department/team that carries out audits on day to day basis. Common in established regulatory agencies with adequate capacity.
- Audit role mixed with other roles:
 - The audit role is performed in addition to other roles such as tariff setting, etc.

Regulatory Audit Models

- Outsourcing of audit services:

This is common for both models above. Helps where there're capacity limitations (skills, time) and useful for capacity building through skills transfer where regulatory staff are attached to the consultant.

ERB Model

- At the moment, the audit function is part of the roles assigned to the financial and economic analysts in the Economic Regulation department.
- The current limited number of regulated utilities also makes this model relatively efficient for the mean time.
- The ERB also plans to outsource some audits both for reasons of capacity constraint as well as to exploit capacity building opportunities for staff.

ERB Model – Scope of Audits

- The main thrust of the ERB's regulatory audits for the next two years will be to strengthen ZESCO's commercial orientation.
- The scope will therefore be a hybrid of both financial and management audits.
- The initial strategy for 2006 is to develop KPIs and commence regular monitoring of the utility's performance with respect to the KPIs.

ERB Model – Scope of Audits

- The focus for 2007 will be on financial audits to strengthen the tariff review process.
- Beyond 2007, the ERB hopes to constitute a small audit team that will be able to handle more comprehensive management audits and some special audits as need arises.

Conclusion

- The ERB has a long way to go in developing its regulatory audit capacity.
- However, the journey of a thousand miles starts with the first step - The ERB is making a start this year!
- The ERB is privileged to be in partnership with the PUC which has a well established and experienced regulatory team; and looks forward to the exchange of ideas on this important topic.