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CAYMAN ISLANDS  
GOVERNMENT

**Minister  
of  
Planning, Lands, Agriculture, Housing and Infrastructure  
(PLAHI)**

4<sup>th</sup> October 2016

Mr. Frederick McTaggart  
President and CEO  
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Dear Mr. McTaggart,

**Re: Cayman Water Company – Comments re Utility Regulation and Competition Office**

The Ministry of PLAHI thanks CWC for its comments.

Four bills intended to facilitate the reform of the utilities sector (in particular the regulatory arrangements) have been gazetted and are to be taken at the next sitting of the Legislative Assembly, scheduled to commence on October 4, 2016.

The objective is to establish a multi- sector regulator to be known as the Utility Regulation and Competition Office (the Office), by merging the operations of the Information and Communications Technology Authority and the Electricity Regulatory Authority, and expanding the role to regulate the provision of water and waste water services and to have responsibility for the fuel markets.

The Bills are

- The Utility Regulation and Competition (URC) Bill, which establishes the Office, provides for its governance and broad multi sector functions.

- The ICTA Amendment Bill which repeals certain sections of the ICTA Law, to give way to the Office and other consequential amendments
- The ERA Amendment Bill which repeals certain sections of the ERA Law, to give way to the Office and other consequential amendments
- The Dangerous Substance Handling and Storage Amendment Law to give the Office responsibility for the administration of that law and to transfer the Chief Petroleum Inspector to the Office.

Of necessity, the URC, the ICTA (Amendment) and ERA (Amendment) Bills have to be taken together as the establishment of the Office and dissolution of the Authorities must occur simultaneously.

CWC's comments are specifically addressed to the URC Bill and by extension certain concerns are raised which arise from the absence of the water sector related Bills which have not yet been gazetted. The Ministry now sets out its responses to CWC's comments but in doing so should like to emphasize that in the drafting the Ministry is mindful of the existing licensing arrangements for CWC which will be fully reflected in the "Water Supply and Waste Water Services Regulation Bill".

The Ministry however believes that in establishing the Office and embarking on the programme of regulatory reform, the regulatory arrangements should reflect current best international practices, provide for increased transparency and heightened responsiveness to all stakeholders.

The Ministry notes the concern about the "absence of consultation" with the industry in the legislative process. While, it would be reasonable to assert that the consultation did not take place prior to the Bills being gazetted, the Ministry is using the 21 day period (statutorily provided for consultation) diligently and has considered and responded to all inputs received, of which there have been a few.

The Ministry now sets out its responses, seriatim, as comprehensively as possible.

## **1. Application of the Bill**

### **CWC Comments**

"As drafted, the Bill does not really cover licensees under *The Water (Production and Supply) Law, 2011*, and *The Wastewater Collection and Treatment Law, 2011* i.e. CWC although that may have been the intention. Schedule 1 of the Bill sets out the Markets and Sectors for which the Office has Responsibility and this does include "production, distribution and supply of potable water and non-potable water as a utility service, and provision of waste water service as a utility service". "Utility services" is defined as "networks operated or services provided by a sectoral utility". "Sectoral utility" is defined as "a utility market or sector for which the Office has specific responsibility under any sectoral legislation". "Sectoral legislation" means any legislation specified in Schedule 2. However, Schedule 2 does not include *The Water (Production and Supply) Law, 2011*, and *The Wastewater Collection and Treatment Law, 2011* or indeed *the Water Authority Law*."

### **Ministry Response**

The omission of "*The Water (Production and Supply) Law, 2011*, and *The Wastewater Collection and Treatment Law, 2011* or indeed *the Water Authority Law*" is in fact not an oversight. The laws relevant to the water sector will be added "By Order" pursuant to Section 112 simultaneously with the enactment of the relevant water sector laws.

### **CWC Comments**

"We note that while Bills to amend *The Electricity Regulatory Authority Law* and *The Information and Communications Technology Law* to dissolve the respective Statutory Authorities established under those Laws and to transfer their powers, functions and responsibilities to The Utility Regulation and Competition Office (the "*Office*") were published, no equivalent Bill has been published to amend *The Water Authority Law* to transfer its regulatory powers, functions and responsibilities to the Office or to make the consequential amendments to *The Water (Production and Supply) Law* and *The Wastewater Collection and Treatment Law* to provide that the licences for those sectors will be issued by the Office rather than The Water Authority. This seems odd in view of the fact that The Water Authority is the only statutory authority which has an inherent conflict of interest in exercising its regulatory functions while also being a sectoral provider. We understood that removing that conflict by transferring the regulatory functions from The Water Authority to the Office was one of the drivers for the Bill yet it fails to accomplish that purpose. Without accompanying Bills to amend *The Water Authority Law* etc. we contend that it serves no purpose to introduce the Bill in the Legislative Assembly at this time."

### **Ministry Response**

The Bills relevant to the water sector are being drafted and are scheduled to be gazetted in time for the first sitting of the Legislative Assembly in the New Year. The Ministry for the reasons indicated has treated the URC Bill and the ICTA and ERA Bills as the priority and while it would have liked to have advanced the four Bills associated with the water sector at the same time, a number of unexpected circumstances prevented this being accomplished. CWC should be advised that the Bills relating to the water sector are four in number:

- A new law – the "Water Supply and Sewerage Services Regulation Law", to give effect to the new institutional arrangements which transfers the economic regulatory functions from the Water Authority to the Office and other consequential provisions including the role and functions of the Office in that sector.
- Consequential amendments to the Water Authority Law; to repeal the economic regulatory functions of the Authority and any provisions necessary to clearly demarcate the functions of the Water Authority as (i) utility service provider and (ii) water resources manager and regulator of those resources; and (iii) clarify potential overlap between any residual regulatory roles of the Water Authority and that of the Office.
- Consequential amendments to the Water (Production and Supply) Law to provide for the Office functions and powers to issue licences under that law; and

- Consequential amendments to the Wastewater Collection and Treatment Law to provide for the Office functions and powers to issue licences under that law.

The Ministry is of the view that there is every reason to introduce the Bills at this time.

## **2. Sectorial Utility Representation on the Board**

### **CWC Comments**

“Pertinent to the foregoing point, section 14 and section 29 of the Bill do not provide for an Executive Director of Water Production and Supply or Wastewater Collection and Treatment and so it appears that no Director is required to have expertise in this area. If the intention was to cover water production and supply and wastewater this must have been an oversight on the part of the draftsman.”

### **Ministry Response**

The Executive Director for Energy and Utilities (emphasis added) will carry the portfolio for water as well as for electricity. The Ministry is of the view that these portfolios can be adequately and appropriately assigned under a single executive director. Competent and expert staff support will be needed in all sectors which will be an organizational matter for the Board of the Office.

The omission, as CWC has suggested, was therefore not an oversight.

## **3. One size does not fit all**

### **CWC Comments**

“We appreciate that it was a monumental task to attempt to bring all the various utility sectors under one regulator. However, we consider the Bill fundamentally flawed insofar as it attempts to introduce complete uniformity in the mode of regulation for a very broad spectrum of sectors and appears to take little account that there are fundamental differences between sectors like fuel supply where the suppliers have dominant market positions and their retail prices have hitherto been completely unregulated, on the one hand, and licensees who have licences issued under the existing regulatory regimes which were negotiated to ensure that the licence contained a cost recovery mechanism or pricing methodology which serve to promote efficiency and fair pricing to the consumer while allowing the licensee a reasonable rate of return on capital efficiently employed.”

### **Ministry Response**

The Ministry agrees that “one size does not fit all”. It is for this reason that the decisions were taken to enact the URC Bill as an instrument to establish the Office, provide for its general duties, functions and governance arrangements as well as for those functions which would have general application across all sectors. The sector specific Bills, the ERA, ICTA Bills and the water sector bills, address the peculiar sector specific issues and the duties/functions of the Office in the respective sectors.

#### **4. Unilateral Modification**

##### **CWC Comments**

"It appears that the intention of section 3 of the Bill is to override the provisions of the existing sectoral legislation and any licences issued in respect of the powers of the Office and in respect of fixing rates and service and therefore give the Office unilateral power to modify any licences issued in those respects. It appears therefore that the intention is to give the Office the ability to require rates and service standards to be adjusted to meet these objectives even where the licence issued has provided a mechanism for determining rates and service standards. A contract which is subject to unilateral modification by one party has ceased to be a contract.

As you know, the parent company of CWC, Consolidated Water Co. Ltd., ("Consolidated water") is a publicly listed company and this a matter which constitutes a substantial investment risk which investors will take into account and may dramatically affect the share price of the Consolidated Water and the cost of obtaining future inward investment."

##### **Ministry Response**

The Ministry notes CWC's concerns as expressed and in particular the contention that, arguably, Section 3 appears to give "the Office unilateral power to modify any licences". This is certainly not the intent as the government is anxious to convey the important principle of certainty in the regulatory framework. While the sector specific Bills will address the Office's powers regarding licensing (in this case the water sector Bills) the Ministry agrees that there should be no ambiguity in regard to ensuring that investor confidence is not compromised. The concern will be raised with the Legislative Counsel with a view to proposing committee stage amendments to address this concern.

#### **5. Significant Market Power**

##### **CWC Comments**

"Section 45 gives the Office power to impose specific conditions on licensees determined to have significant market power in the relevant markets, including obligations relating to cost recovery and price controls and retail prices. Section 45(7) specifically provides that the Office may require the significant market power licensee to provide full justification for its prices, and may, where appropriate, require prices to be adjusted. Significant Market Power is defined in section 2(3) as where a sectoral provider enjoys individually or jointly with others a position of economic strength affording it the power to behave to an appreciable extent independently of competitors, customers and consumers. Since CWC would have an exclusive Licence Area under its Licence there can be no doubt that it would fall into this category as would CUC and The Water Authority. These provisions appear to take little account of the fact that the licensee's dominant position in the market and that the factors set out in section 45(2) will have been taken into account in negotiating and designing whatever the retail pricing structure is in its licence."

##### **Ministry Response**

The Ministry considered the inclusion of this approach to promoting competition, which reflects best practice, very carefully. There is little doubt, as CWC suggests, that CWC enjoys a position of



dominance (and therefore significant market power) in its exclusive service area. This section does not negate the current regime for issuing licences to monopoly service providers which set out obligations relating to cost recovery and price controls and retail prices. The fact that CWC has been issued with a licence, the conditions of which will be preserved in the relevant Water Bills, is not inconsistent with the principle provided at Section 45.

CWC should note Section 15 of the ERA Amendment Bill, intended to preserve existing licences, reproduced below.

93. (1) A licence or other enabling instrument issued to a person to provide any aspect of generation or transmission and distribution of electricity in the Islands granted by the Cabinet and valid and in force immediately prior to the operative date shall continue valid and in force for the remainder of the term as if it were a licence granted under this Law on the operative date and such licence shall continue to be subject to each and every one of the terms, conditions and exemptions attaching to such licence as if the terms, conditions and exemptions had been imposed or granted under this Law on the operative date but shall otherwise be subject to the provisions of this Law.

## **6. Merger Control**

### **CWC Comments**

"Section 46 provides that a licensee shall not issue shares and there shall be no transfer or other dealing or disposal of the legal or beneficial interest in shares of a licensee without the prior written consent of the Office. While the Office's consent may not be unreasonably withheld, the Bill provides that the Office may refuse where the giving of the consent may result in a lessening of competition in the operation of networks or the provision of utility services. Since water supply and electricity transmission and distribution are natural monopolies we think the primary concern here is with electricity generation, telecommunications and broadcasting etc. Unlike section 24 of the ERA Law there is no 10% threshold to trigger this requirement. Note that Section 46(5)(a) also affects changes in the shareholding of Consolidated Water as the parent company of CWC even though its shares are listed on a recognized stock exchange. While prior written consent is not required there is an obligation to notify the Office as soon as reasonably practicable of the acquisition by any person or group of persons of shares representing more than 10% of the issued share capital or total voting rights of Consolidated Water. Since there is a general obligation to obtain prior written consent for any transfer of legal or beneficial interest in the shares of a licensee it is difficult to understand why particular provisions are required to obtain prior written of the Office for changes in control of a licensee as set out in sections 47 to 54. It appears that these two sets of provisions may have been combined from different sources."

## **Ministry Response**

The Ministry notes the question as to why particular provisions are required to obtain prior written approval of the Office for changes in control. This goes to the core of the concern for the preservation of competition; allows the Office to reflect on the impact that any such change may have on a competitive market and to make any interventions deemed appropriate to mitigate any negative impacts. The Ministry will however review the section in light of CWC's comments in relation to consents.

## **7. Abuse of Dominant Position**

### **CWC Comments**

"The conduct which is specifically recognised as constituting abuse of dominant position is set out in section 70(2). Section 70(1) provides that conduct on the part of a licensee which amounts to abuse of a dominant position in a market or sector for which the Office has responsibility is prohibited. However, somewhat oddly, there is a special exception that licensees under the ERA Law shall be entitled to protect their legitimate business interests subject to this Law and any other relevant Law. We can see no reasonable justification why licensees under any other sectoral legislation should not have an equal entitlement."

### **Ministry Response**

The Ministry agrees that this is not a particularly elegant treatment of the particular issue where the Ministry has attempted to preserve a provision in the ERA Act, which as you would appreciate, would be a material change to agreements between the CUC and the Government.

## **8. Appeals**

### **CWC Comments**

"Part 14 of the Bill. "Administrative Fines". These provisions are significantly more onerous on licensees than the equivalent provisions in The Electricity Regulatory Law. It appears that this is deliberate since much of the drafting otherwise tracks those provisions. Under section 91(4) of the Bill the Office "may in its discretion" allow a request for a licensee to be heard in person or through a representative while section 59(3) of the ERA Law says that the Authority "shall" allow such a request. Section 91(9) limits orders the Office may make to warnings and fines and does not provide for a period within which to rectify any contravention by the licensee. Section 91(11) shortens the period within which to make an appeal to the Court against a determination of the Office to 21 days as compared to 28 days in The ERA Law and The Water Authority Law. There is no provision for reconsiderations of determinations by the Office which could take into account further relevant information presented by the licensee and avoid an expensive appeal to the Court. The grounds upon which one may appeal are not provided. There is no provision as to the powers of the Court upon appeal, for example, to confirm, vary or reverse the determination or to remit the matter back to the Office with the opinion of the court. It does not state whether the appeal would

have the effect of suspending the execution of the determination by the Office pending the outcome of the appeal so the licensee would have to apply to the Court for an injunction as interim relief.”

### Ministry Response

There are a number of issues raised:

Administrative fines – The level of fines proposed is consistent with the recent amendments to the ICTA Law. On the question of appeals to the Court – The Ministry will seek Committee stage amendments to increase period referenced in Section 91(11) from 21 to 28 days.

Reconsideration of Office Decisions - Section 7 of the URC Bill provides a procedure to be followed before the Office makes an Administrative Determination, where it must issue the Determination in Draft in order to allow affected parties to comment.

7. (1) Prior to issuing an administrative determination which, in the reasonable opinion of the Office, is of public significance, and subject to specific procedures under sectoral legislation, the Office shall -

- (a) issue the proposed determination in the form of a draft administrative determination;
- (b) allow persons with sufficient interest or who are likely to be affected a reasonable opportunity to comment on the draft administrative determination; and
- (c) give due consideration to those comments with a view to determining what administrative determination (if any) should be issued.

This provision affords affected parties to comment on the draft Decision and thus provide the basis for the Office to “reconsider” its position prior to issuing a final Decision, noting that the Office shall give due consideration to those comments. The Ministry is of the view that this procedure affords affected parties sufficient opportunity to proffer arguments for “reconsideration” and that the logical next step would therefore be judicial review.

The Ministry has been advised that as the process for appeal is Judicial Review, the rules applicable for judicial review would, of necessity, apply. However this will be discussed again with Legislative Counsel.

Yours sincerely,



Hon Kurt Tibbetts OBE JP

Minister of Planning, Lands, Agriculture, Housing & Infrastructure