

Electricity concessions: Uncertainties may cause shocks

Expiring concessions and inadequate regulation may stall the electricity sector.

Liliana Lavoratti, Rio de Janeiro

The debate over electricity concessions that will expire after 2015 indicates that Brazilian policy in this area is not yet consolidated. Besides doubts about capacity to supply more vigorous growth of the economy, competition for positions in major state utility companies, and blackouts in the Northeast and in big cities, there is acute uncertainty about what the federal government will do with the expiring contracts.

President Rousseff has important decisions to make before 2015: whether to extend concessions for about 31 gigawatts in electricity generation and contracts for transmission and distribution throughout the country.

Extension, which is not currently authorized, would require sending a bill to Congress and issuing an interim decree. The alternative, under current rules, is for the concessions to revert to the federal government, with compensation to current operators for investments made for which the costs have not yet been recovered, and then opening an auction for new concessions, says expert

"We believe the most pragmatic solution is extension [of the current concessions]. Although this is not the best solution for the economy, this government would not take the risk that assets belonging to state-owned enterprises would pass into the hands of the private sector."

ELENA LANDAU

Mario Roque Bonini of the Foundation for Administrative Development (Fundap).

Privatization

For Nelson Fonseca Leite, president of the Association of Electricity Distributors (Abradee), "This government, given its ideology, will not seek new bids, which would almost be privatization." Elena Landau, lawyer, economist, and consultant to the Brazilian Association of Electric Power Companies (ABCE), agrees: "We believe the most pragmatic solution is extension [of the current concessions]. Although it is not the best solution for the economy, this government would not take the risk that assets belonging to state-owned enterprises would pass into the hands of the private sector."

In any case, "If the government were interested in more concessions, promoting new companies in the market, allowing more competition, the process should have begun some time ago," says Cleveland Prates, professor of competition and regulation, Getulio Vargas Foundation of São Paulo, and partner and director, Economic Consulting Microanalysis. "The government may have left things as they are to consummate the continuity of concessions granted 20 years ago." He adds, "With its strong majority in Congress, it will not be difficult to get new rules adopted at breakneck speed."

Leite also thinks it more likely that the government will use renewal of the concessions to achieve reduction of energy prices for consumers or raise funds by charging operators for extension of the concessions. But he emphasizes that the energy distribution contracts provide for rate reviews every four or five years to incorporate operator productivity gains into final prices.

The Brazilian Association of Large Electricity Transmission Companies (Abrate) also thinks extension is "the safest way to protect consumers from possible power outages and provide stability to the electric power system," according to Cesar de Barros Pinto, Abrate chief executive. He points out that the law authorizes electricity transmission companies, unlike generators and distributors, to extend their current contracts. Currently 10 transmission contracts are expiring — the equivalent to 73,000 km of transmission lines (82% of the entire system).

Charles Lenzi, CEO of the Brazilian Association for Clean Energy Generation (Abragel), thinks the debate should focus not on whether the sector will remain largely in government hands but on ensuring that the regulatory framework stimulates private enterprise to carry out the necessary investments to definitively avert blackouts. Abragel also supports extension of concession terms but argues that any resources collected from the extension

should be invested in generating energy from renewable sources.

Conciliation

Regardless of whether the choice is extension or a new round of bids, what is important is a clear and enduring definition of policy, says Bonini. In addition to greater legal certainty, he says, "it is important to reconcile the goals of low tariffs and adequate and reliable expansion of energy supply." He acknowledges, however, that it is not easy to reconcile all these aspects given the complexity of the electricity sector and its generation, transmission, and distribution segments.

Companies that are already in the market are mainly state-owned, but other companies would like to participate. Prates adds that "Most disadvantaged in this story are consumers, who participate very little, given the complexity of the market. Unfortunately, they cannot even know whether or not the decisions made will make their electricity bill more expensive."

After profound changes over the past 15 years, the current model of the electricity industry is a hybrid. Unlike the state monopoly that prevailed until 1995, private enterprises are not heavily involved, but there is some competition.

According to Bonini, the federal government, which owns a controlling stake in companies that hold a large share of the maturing generation and transmission concessions, has an obvious interest in extending the concessions. States are also interested in that because they want to expand their utility companies, not privatize them. But private investors are divided: "There are those who wish to maintain the concessions, and there are potential investors that believe bidding is their only chance to enter the market," Bonini explains.

"Apart from greater legal certainty, it is important to reconcile the goals of low tariffs and adequate and reliable expansion of energy supply."

MARIO ROQUE BONINI

Until the government communicates a clear position on concessions, utilities will be very cautious about new projects.

CLEVELAND PRATES

Investments

The lack of clarity about what happens when the concession contracts expire in four years "directly affects day-to-day operations of the companies," as well as inhibiting investment, says Landau. "Nothing is known, starting with the rules for compensation if companies' assets [not yet paid back] revert to the government," she emphasizes. The compensation that would be required is estimated at several billion dollars.

Prates thinks that until the government communicates a clear position on the concessions, utilities will be very cautious about new projects. "Investments in the energy sector take many years to mature and require long-term planning, so you must have some idea of what will happen," he says.