Regulated Entitlement Values

2018/19 Tariff Year

September 2018



About the Utility Regulator

The Utility Regulator is the independent non-ministerial government department responsible for regulating Northern Ireland's electricity, gas, water and sewerage industries, to promote the short and long-term interests of consumers.

We are not a policy-making department of government, but we make sure that the energy and water utility industries in Northern Ireland are regulated and developed within ministerial policy as set out in our statutory duties.

We are governed by a Board of Directors and are accountable to the Northern Ireland Assembly through financial and annual reporting obligations.

We are based at Queens House in the centre of Belfast. The Chief Executive leads a management team of directors representing each of the key functional areas in the organisation: Corporate Affairs; Electricity; Gas; Retail and Social; and Water. The staff team includes economists, engineers, accountants, utility specialists, legal advisors and administration professionals.

Our Mission	Value and sustainability in energy and water.
Our Vision	We will make a difference for consumers by listening, innovating and leading.

Our Values

Be a best practice regulator: transparent, consistent, proportional, accountable, and targeted.

Be a united team.

Be collaborative and co-operative.

Be professional.

Listen and explain.

Make a difference.

Act with integrity.

Abstract

Electricity suppliers in Northern Ireland pay a number of regulated charges which they may in turn recover from their consumers. This information paper, which we produce each year, details each regulated charge that makes up a portion of electricity bills for both business and domestic consumers. The purpose of this information note is to communicate the changes to the regulated entitlement values for each charge which will take effect from 1 October 2018.

The paper covers the charges associated with electricity networks, electricity market operation, SEM and the PSO levy.

Audience

Electricity customers, businesses, suppliers and consumer groups.

Consumer impact

This paper provides information on each element of the regulated entitlements which make-up a portion of the cost of electricity paid by business and domestic consumers. The reasons for the changes are discussed within the paper.

Contents

1 Introduction

Electricity suppliers in Northern Ireland pay a number of regulated charges which they may in turn recover from their customers. The Utility Regulator approves Network charges and PSO charges whereas the Single Electricity Market Committee (SEMC) approves SEM charges. In this information note we refer to the regulated entitlement values for each charge which can be recovered over the next tariff year (1 October 2018 - 30 September 2019).

Network and PSO charges are collected by: NIE Networks (Northern Ireland Electricity Networks); and by SONI (System Operator Northern Ireland), whereas the SEM charges are collected by SEMO (Single Electricity Market Operator). The purpose of this information note is to communicate the changes to the regulated entitlement values for each charge which will take effect from 1 October 2018, together with explanations for these changes.

NIE Networks, SONI and the SEMO create tariffs to collect the entitlements over the forthcoming tariff year, based on cost/revenue allocation assumptions and consumption forecasts. The changes in regulated entitlement will affect individual customers in different ways. The relevant tariffs are published on the NIE Networks[1], SONI[2] and SEM website[3] which we have referenced in the footnotes below.

This paper has been authored and published before outturn costs have been collected or verified for the tariff year 2017/18 (1 October 2017 – 30 September 2018), therefore, the comparisons made below are between two forecasted revenue entitlements. For the sake of simplicity and transparency we have not updated the 2017/18 forecast from last year[4], however, we have accounted for the latest available information to us, in our forecasts for 2018/19.

In addition, we would add that electricity bills also include other costs, such as: wholesale energy costs; the climate change levy (for businesses only); the carbon reduction commitment; supplier charges; and VAT. The most significant of these other costs is the energy costs, and these will vary greatly between suppliers and customers, largely depending on the timing and extent of hedging contracts.

[1] http://www.nie.co.uk/About-NIE/Regulation/Regulatory-documents
[2] http://www.soni.ltd.uk/library/
[3] https://www.semcommittee.com/publications/topics/tariffs-8
[4] https://www.uregni.gov.uk/news-centre/information-note-published-regulated-electricity-entitlement-values-20172018

2 Charges regulated by the Utility Regulator

2.1 Northern Ireland network charges

Details of the movements in the maximum amount recoverable from network charges are set out in Table 1 below, but first we make some comments on the individual items which make up the network charges.

Transmission & Distribution Use of System (TUoS/DUoS) charges

The use of system charges are derived from the price controls put in place for NIE Networks with the RP6 being the most relevant for this tariff year. The tariffs reflect our best estimate for the 2018/19 tariff year by utilising the approach that the entitlement for any tariff year (October - September) should be 50% of the entitlement for the two financial years (April - March) which it spans.

Specific comments on DUoS charges

DUoS charges have increased from the 2017/18 charge of £194.0 million to £199.6 million.

The increase is due to higher revenue entitlement driven by the RP6 Final Determination compared to the Draft Determination on which 2017/18 tariffs were based. Higher inflation (RPI) than forecast has also pushed required revenues upwards.

However, this has been offset by K factor movements i.e. an over recovery has arisen which now has to be deducted from the underlying entitlement. Excluding K, the distribution revenue entitlement is £201.2 million.

The net effect of these factors is that the DUoS revenue entitlement decreases by 0.1% in real terms.

Specific comments on TUoS charges

TUoS charges have increased from the 2017/18 charge of £36.9 million to £44.0 million.

The increase in TUoS charges is also due to higher revenue entitlement driven by the RP6 Final Determination compared to the Draft Determination and higher inflation on which 2017/18 tariffs were based.

Unlike DUoS, K factor movements have increased TUoS revenues i.e. an under recovery has arisen which now has to be added to the underlying entitlement.

Excluding K, the transmission revenue entitlement is £42.3 million.

The net effect of these factors is that the TUoS revenue entitlement increases by 15.8% in real terms.

System Support Services (SSS) charges

These charges cover the cost of SONI and ancillary services required to operate the transmission system safely and reliably.

The SSS charge has increased quite substantially from the 2017/18 revenue of £48.2 million to £81.7 million in 2018/19. There are a number of reasons for this increase.

The largest element of the rise (£30.6 million) is related to ancillary services. These are payments made to generators or market participants for providing system services.

Costs are expected to increase due to:

a) The provision of more flexible services in order to facilitate increasing levels of renewable generation.

b) Costs associated with local reserve services agreements.

Offsetting savings are however expected in market charges as a result of these more flexible services.

Besides ancillary services, there are a number of other material influences on charge increases for 2018/19. Contributing factors include:

- Additional opex cost associated with the preparation for I-SEM.[5]
- Revenue uplifts for SONI resulting from CMA[6] decisions.
- Licence fee charges to cover the UR costs of the CMA referral.
- Capital returns provided as a result of the TSO undertaking network planning activities, which has not been previously remunerated.

Collection Agency Income Requirement (CAIR)

The Collection Agency Income Requirement (CAIRt) which SONI collect from suppliers and pay to Moyle Interconnector Limited is apportioned across the predicted units transmitted. The amount allocated depends upon the kWh consumption in each charging period.

[5] I-SEM refers to the Integrated Single Electricity Market.
[6] Competition and Markets Authority – SONI Final Determination.

Moyle provided a statement indicating that income required is £nil for the 2018/19 tariff year. This compares to a £12.5 million provision in 2017/18 and represents a 100% reduction from the previous year.

Overall network charges

To summarise: Table 1 below shows that the maximum amount recoverable for network charges will increase by 11.5% (nominal) and 8.3% (real) between 2017/18 and 2018/19.

Network charges are estimated to be 26% of the final electricity bill and therefore if we assume all else remains equal we estimate the combined effect on final bills to be an increase of 3.0% (nominal).

The precise impact on individual customers will depend on various factors including: the consumption profile; consumption quantity; and historical consumption. Customers should refer to company tariff tables. Links have been provided in section 1 of this paper.

Table 1: Northern Ireland network charges

	October 2017 - September 2018	**October 2018 - September 2019**	**% Change (nominal)**	**% Change (real)[7]**
Distribution charges (DUoS)	£ 194.0 m	£ 199.6 m	2.9%	-0.1%
Transmission charges (TUoS)	£ 36.9 m	£ 44.0 m	19.2%	15.8%
Support charges (SSS)	£48.2 m	£81.7 m	69.4%	64.4%
CAIR	£12.5 m	£0.0 m	-100%	-100%
Total Network Charges	**£291.6 m**	**£325.3 m**	**11.5%**	**8.3%**

[7] This ‘real’ change accounts for the forecast of inflation. This has been estimated by the Office of Budget responsibility at **3.0%** (See here: http://obr.uk/efo/economic-fiscal-outlook-march-2018/) (supplementary economy tables, RPI for 2019).

2.2 Northern Ireland Public Service Obligation (PSO) charge

Details of the movements in the maximum amount recoverable from PSO charges are set out Table 2 below, but first we make some comments on the individual items which make up the PSO charges.

Landbank

NIE Land Bank business was established to protect the land surrounding existing power stations for future electricity generation development. The Land Bank sites were vested and the NIE Land Bank business currently manages these sites in accordance with Condition 23 of NIE Network's Licence and directions issued by the Utility Regulator.

Landbank costs benefitted from the sale proceeds of land in previous years and this has resulted in a return to a small positive revenue requirement.

Legacy generation costs

The Power Procurement Business (PPB) has power purchase agreements with the power station owners in Northern Ireland. These contracts were put in place with privatisation of the industry back in 1992. PPB purchase power under the terms of these contracts and then sells this power in the SEM. Any profit or loss forms part of the levy on all customers in Northern Ireland via the PSO.

The PPB and the associated generation contracts are forecast to save customers £3.4 million in the 2018/19[8] tariff year. This compares to a net saving of £5.4 million forecast for the 2017/18 tariff year.

Northern Ireland Sustainable Energy Programme (NISEP) costs

A levy is imposed on all demand to fund the Northern Ireland Sustainable Energy Programme (NISEP). The objective of this programme is to promote energy efficiency with particular regard to vulnerable electricity customers. Costs for 2018/19 have been updated to reflect the latest forecast expenditure.

K factor

If the amount of revenue recovered in any one year exceeds or falls short of the amount allowed, the correction factor operates in the following year to give back any surplus with interest, or to recover any deficit with interest, as appropriate.

K factor reflects an over recovery for the 2018/19 year due mainly to the timing of

[8] Please note that, similar to DUoS and TUoS charges, we have changed our approach to calculating the entitlement for the tariff year, such that, the entitlement for any tariff year (October - September) is 50% of the entitlement for the two financial years (April - March) which it spans.

revenue income from legacy generation.

Overall PSO charges

To summarise: Table 2 below shows that the maximum amount recoverable for PSO charges will decrease from £5.3m to £1.0m for 2018/19.

Table 2: Northern Ireland PSO charges

	October 2017 - September 2018	**October 2018 - September 2019**	**£ Change (nominal)**
Landbank	£ -0.2 m	£ 0.1 m	£ 0.3 m
Legacy generation costs/income	£ -5.4 m	£ -3.4 m	£2.0 m
NISEP + incentive	£ 8.4m	£ 8.5m	£ 0.1 m
K factor (negative = over recovery)	£ 2.5m	£ -4.1 m	£ -6.6 m
Total PSO charges	**£ 5.3 m**	**£ 1.0 m**	**£ -4.2 m**

3 Charges regulated by the SEM Committee

The SEM Committee regulates certain charges in the all-island electricity market including charges for generation capacity, the operation of the market and market imperfections (or constraints).

Details of the movements in the maximum amount recoverable for SEM charges on an all-island basis are set out Table 3 below, but first we make some comments on the individual items which make up the SEM charges.

Capacity charges

In the SEM, generators receive a capacity payment as a contribution to fixed investment and operating costs. The total amount is revised annually to reflect the cost of new peaking capacity and the amount of capacity required to meet security standards. Suppliers in turn pay a capacity charge which is profiled monthly.

The Capacity pot for the current Capacity Payments Mechanism (CPM) is funded through Supplier Capacity Charges. The CPM will cease in September 2018 when I-SEM goes live. The October 2017 – September 2018 pot was valued at €524m.

The new Capacity Remuneration Mechanism (CRM), within I-SEM, replaces the CPM and is a volume based mechanism which will only procure the required volume of capacity that is needed to deliver Security of Supply. The volume of capacity is procured via competitive auctions that trade volumes of Capacity for financial hedging products. The first auction cleared at a cost to consumers of €333m which is a reduction compared to the last CPM amount above.

Imperfection charges

Actual dispatch on the all-island transmission network differs from the optimal dispatch derived for the market schedule. This is because constraints are introduced due to network bottlenecks (including the North-South interconnector) and due to the need for the system operators to maintain reserve for operational security.

The imperfections charge is mainly to cover the cost of the variance between actual dispatch and the unconstrained economic dispatch reflected in the market schedule.

The imperfections entitlement has increased by 6.21% in nominal terms from the current tariff year. Main reasons for the higher forecast entitlement are the increase in forecasted fuel costs and also a provision included for I-SEM related costs. Further information is available from the SEM committee website[9].

Market Operator charge

SEMO incurs operational costs while carrying out its functions and recovers these costs, together with capital related costs including a rate of return, through Market Operator tariffs and fees, which are levied on market participants. To facilitate this recovery of costs, the Market Operator submits proposals on its allowed revenue and the charges required to recover this revenue to the Regulatory Authorities (RAs). The 2016-19 SEMO Price Control was published on 3 August 2016 and covers the period from 1 October 2016 to 31 March 2019[10].

SEMO have submitted their Market Operator revenue requirement for tariff year 2018/19 which has been approved by the Regulatory Authorities. This revenue requirement matches the amount provided to SEMO within the 2016-19 Price Control, with an adjustment to reflect the K factor over recovery from the 2017/18 tariff year. SEMO will also be recovering a full year of active I-SEM which is itself higher than last year's tariff. SEMO are also recovering revenue associated with 12 months of SEM resettlement under the 2016-19 Price Control along with pre Go-Live Opex. This means in effect SEMO are recovering 12 months of revenues for two separate Price Controls and an amount for Pre-Go-Live activities. The market operator tariff has increased by 77.3% in nominal terms.

Overall SEM charges

Table 3 below shows the amount recoverable under the SEM charges in 2018/19. The amount has decreased by 24.3% (nominal) or 26.5% (real) compared to 2017/18:

Table 3: Charges regulated by the SEM Committee

	October 2017 - September 2018	October 2018 - September 2019	% Change (nominal)	% Change (real)

[9] https://www.semcommittee.com/publications

[10] https://www.semcommittee.com/sites/semcommittee.com/files/media-files/SEM-16-043%20SEMO%20Price%20Control%20Decision%20Paper%20for%20period%20commencing%201%20October%202016.pdf

Capacity charge	€ 524.0 m	€ 333.0 m	-36.5%	-38.3%
Imperfections charge	€ 173.0 m	€ 183.8m	6.2%	3.1%
Market operator charge	€ 10.39 m	€ 18.4m	77.3%	72.1%
Total charges	**€ 707.4m**	**€ 535.2**	**-24.3%**	**-26.5%**

The first CRM auction took place in December 2017 and procured capacity for the period from I-SEM Go-Live to 30 September 2019.

Transitional year-ahead auctions will procure 100% of the capacity required for the Capacity Years 2019/20, 2020/21, and 2021/22.

The enduring auction arrangements will apply to capacity year 2022/23 onwards. For each capacity year from 2022/23 onwards, approximately 95% of capacity will be procured via separate auctions held approximately four years in advance of the start of the corresponding capacity year. The remaining 5% for each capacity year will be procured via separate auctions approximately one year in advance of the capacity year commencing.

The capacity procured under the CRM will be funded through Suppliers paying capacity charges into the Capacity Market, in similar fashion to the arrangements under SEM. These charges are derived from the expected annual value of capacity reliability options sold in the auction, and a forecast of total demand.

4 Other costs

Energy

The largest component of electricity bills is the cost of purchasing energy from the wholesale electricity market (the SEM / I-SEM). In order to offer fixed energy prices, suppliers often enter into forward hedges. End-user prices between suppliers will vary depending on the extent, timing and duration of hedging contracts and other differing commercial aspects of the businesses.

Whilst the SEM Committee does regulate bidding behaviour in some areas of the energy market by generators, the wholesale energy component of bills is not regulated, except in Northern Ireland for customers (mainly domestic) of the incumbent supplier, Power NI.

Climate Change Levy (for business customers only)

The Climate Change Levy (CCL) was introduced on 1 April 2001. Non-domestic electricity customers pay the levy at a rate of 0.583 p/kWh from 1 April 2018 and 0.847 p/kWh from 1 April 2019[11].

Supplier costs and margin

Electricity bills will also include a component to cover supplier costs and margin.

VAT

Value added tax (VAT) is applied to electricity at a rate of 5% for average consumption (fewer than 33kWh per day). Above that level of consumption, the standard rate of 20% is applied[12].

[11] https://www.gov.uk/government/publications/rates-and-allowances-climate-change-levy/climate-change-levy-rates
[12] https://www.gov.uk/guidance/vat-on-fuel-and-power-notice-70119#electricity