Regulated Entitlement Values

2019/20 Tariff Year

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, Markets and Networks. The staff team includes economists, engineers, accountants, utility specialists, legal advisors and administration professionals.

Our mission

To protect the short- and long-term interests of consumers of electricity, gas and water.

Our vision

To ensure value and sustainability in energy and water.

Our values

- Be a best practice regulator: transparent, consistent, proportionate, accountable and targeted.
- Be professional – listening, explaining and acting with integrity.
- Be a collaborative, co-operative and learning team.
- Be motivated and empowered to make a difference.

Abstract

Electricity suppliers in Northern Ireland pay a number of regulated charges which they may in turn recover from their consumers. This information paper 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 2019.

Audience

Electricity suppliers, customers, businesses 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

1.1 Electricity suppliers in Northern Ireland pay a number of regulated charges, known as regulated entitlement values, which they may in turn recover from their customers. The Utility Regulator approves network charges and public service obligation (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 2019 - 30 September 2020).

1.2 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).

1.3 The purpose of this paper is to communicate the changes to the regulated entitlement values for each charge which will take effect from 1 October 2019, together with explanations for these changes.

1.4 NIE Networks, SONI and the SEMO set tariffs to collect over the forthcoming tariff year, based on cost/revenue allocation assumptions and consumption forecasts. These costs are regulated through price controls to ensure the costs are necessary and efficiently incurred to help protect consumers. The changes in regulated entitlement will affect individual customers in different ways and **have already been incorporated into the recently announced Power NI tariff for domestic customers.** The relevant tariffs are published on the NIE Networks[1], SONI[2] and SEM website[3] which we have referenced in the footnotes below.

1.5 This paper has been authored and published before outturn costs have been collected or verified for the tariff year 2018/19 (1 October 2018 – 30 September 2019), therefore, the comparisons made below are between two forecasted revenue entitlements. For the sake of simplicity and transparency we have not updated the 2018/19 forecast from last year[4], however, we have accounted for the latest available information to us, in our forecasts for 2019/20.

1.6 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

[1] https://www.nienetworks.co.uk/about-us/regulation/network-charges
[2] http://www.soni.ltd.uk/library/
[3] https://www.semcommittee.com/publications
[4] https://www.uregni.gov.uk/news-centre/information-note-published-regulated-electricity-entitlement-values-20182019

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.

2. Network and system support charges

Transmission & Distribution (TUoS/DUoS) charges

2.1 The use of system charges are derived from the price controls put in place for NIE Networks, with the RP6 price control being the most relevant for this tariff year. The tariffs reflect our best estimate for the 2019/20 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.

TUoS

2.2 TUoS charges have increased by £1.3m from the 2018/19 charge of £44.0 million to £45.3 million.

2.3 The increase in TUoS charges is largely due to inflation although ongoing capital expenditure within the RP6 price control is also having an impact. The RP6 price control aims to set an efficient revenue cap to enable NIE Networks to deliver a quality network and services that customers need. The net effect of changes to capital allowance rates and headline corporation tax rates have also added to the entitlement.

2.4 K factor movements have a largely neutral impact for the 2019/20 tariff year although do include an under recovery of £1.5m, down from £1.7m in the 2018/19 tariff year. Excluding K, the underlying transmission revenue entitlement is £43.8 million for 2019/20.

2.5 The net effect of these factors is that the TUoS revenue entitlement increases by 3.0% for 2019/20.

2.6 NIE Networks pass on all TUoS charges to SONI. Revenue is then recovered via suppliers (STUoS) and generators (GTUoS) on the basis of a 75:25 split respectively.

2.7 STUoS has increased from the 2018/19 revenue requirement of £33.1 million to £34.1 million. This represents a rise of 3.2% for 2019/20. The £34.1m revenue is calculated based on 75% of overall TUoS plus a K-factor of c. £131k.

DUoS

2.8 DUoS charges have increased by £14.8m from the 2018/19 charge of £199.6 million to £214.4 million.

2.9 The increase is due to two main factors

a) Higher revenue entitlement of £9.7m driven by inflation and the ongoing capital programme within the RP6 price control. The RP6 price control aims to set an efficient revenue cap to enable NIE Networks to deliver a quality network and services that customers need. DUoS is also impacted by similar tax changes as noted in TUoS along with some opex changes driven by injurious affection and change of law.

b) Reduced demand in 2018/19 has led to a K factor under recovery of £3.5 million which needs to be included in 2019/20 tariffs. As 2018/19 benefited by inclusion of a £1.6 million over recovery this results in an overall impact of £5.1 million on tariffs.

2.10 Excluding K, the underlying distribution revenue entitlement is £210.9 million for 2019/20.

2.11 Unfortunately, demand in GWh is also forecast to fall a further 2.8% in 2019/20 which means that the tariff increase based on entitlement alone of 7.4% is pushed up to 9.7% to recover the £214.4 million noted above.

System Support Services (SSS) charges

2.12 These regulated charges cover the cost of SONI and the ancillary services required to operate the transmission system safely and reliably. Revenue is apportioned across each kW of electricity consumed.

2.13 SSS revenue has reduced substantially (-31.5%) from the 2018/19 value of £81.7 million to £55.9million in 2019/20. There are a number of reasons for this decrease.

2.14 The largest element of the fall (-£26.0 million) is related to ancillary services. These are payments made to generators or market participants for providing system services. This year sees the removal of some rather substantial Local Reserve Service Agreements (LRSA) which are an element of ancillary services. These are NI specific security of supply contracts with generators which are no longer required to provide the necessary services to ensure the stability of the system.

2.15 Besides ancillary services, the other main contributor to revenue reduction is the K-factor over recovery (-£5.9 million) for 2017/18. SONI advised that the K-factor is primarily due to an under spend in ancillary services. In addition, specific project opex (Dt component of the licence formula) was lower than expected.

2.16 Alongside these decreases, the revenue includes some offsetting increases. Provision is made for £6.9m related to cost recovery of special projects (Zt component) such as implementation of the I-SEM and DS3 projects. These projects helped deliver the new market arrangements (I-SEM) and facilitate increased renewables on the system (DS3). The I-SEM Agreed Approach Document specified that these costs are recouped through the relevant TSO price controls and are therefore included in SSS revenue.

2.17 It is also worth noting that the SSS charge (in p/kWh) has not fallen by as large a percentage as the proportional fall in revenue. Revenue has fallen by -31.5% against a unit charge reduction of -28.7%. This is due to the fact that SONI demand forecasts have fallen by -3.8% since last year.

Collection Agency Income Requirement (CAIR)

2.18 Moyle's transmission licence permits them to raise revenues from sales of capacity on the Moyle interconnector and to recover the balance of its revenue requirements from payments received from SONI under the Collection Agency Agreement.

2.19 The Collection Agency Income Requirement ($CAIRt$) which SONI collect from suppliers and pay to Moyle Interconnector Limited is apportioned across the predicted units transmitted.

2.20 Moyle provided a statement indicating that income required is £nil for the 2019/20 tariff year. This represents the same provision as in 2018/19 and results in no charge for this asset.

Overall Network and system support charges

2.21 Table 1 below shows that the maximum amount recoverable for network and system support costs charged to suppliers between 2018/19 and 2019/20.

2.22 Network and system support charges are estimated to be 26% of the final electricity bill.

2.23 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.

Entitlement	2018/19 £m	2019/20 £m	Change %
Supplier Transmission charges (STUoS)	33.1	34.1	3.2
Distribution charges (DUoS)	199.6	214.4	7.4
Support charges (SSS)	81.7	55.9	-31.5
CAIR	0	0	0

Table 1 : Network Charges

3. Public Service Obligation (PSO) charge

Landbank

3.1 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.

3.2 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

3.3 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.

3.4 The PPB and the associated generation contracts are forecast to save customers £10.1 million in the 2019/20[5] tariff year. This compares to a net saving of £3.4 million forecast for the 2018/19 tariff year.

Sustainable Energy Programme (NISEP) costs

3.5 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 2019/20 have been updated to reflect the latest forecast expenditure but these remain at £8.5m, the same as 2018/19.

K factor

3.6 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.

[5] 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.

3.7 K factor reflects an over recovery for the 2019/20 year due mainly to differences between forecast and actual legacy generation income.

Overall PSO charges

3.8 To summarise: Table 2 below shows that the maximum amount recoverable for PSO charges will decrease from a £1.0m charge to a rebate of £10.2m for 2019/20.

	2018/19 £m	**2019/20 £m**	**Change £m**
Landbank	0.1	0.1	0.1
Legacy generation	-3.4	-10.1	-6.7
NISEP	8.5	8.5	0.0
K factor	-4.1	-8.7	-4.5
Total	**1.0**	**-10.2**	**-11.2**

Table 2 : PSO charge

4. Charges regulated by the SEM Committee

4.1 The Single Electricity Market (SEM) is the wholesale electricity market for the island of Ireland and is regulated by the SEM Committee. The SEM consists of a number of electricity trading markets and is administered by the SEM operator (SEMO)

4.2 New market arrangements for the SEM were introduced on 1 October 2018 improving efficiency and facilitating effective competition in the market.

4.3 Since the new arrangements were introduced they have delivered significant benefits, including making more efficient use of the interconnectors that connect the SEM with the GB market; delivering a market that reflects the underlying cost of generation and delivering increased competition. The new capacity remuneration mechanism has delivered significant savings and allows new and existing generation to compete together. More detail on the trends and performance of the SEM is available on the SEM Committee website[6].

4.4 However, as with many major projects of this scale, this is a market in the early stages of its development. In the Balancing Market a number of issues have been raised by market participants. The SEM Committee has taken action to address some of these issues and will continue to work with SEMO, the TSOs and market participants to ensure the ongoing and continual improvement of the market.

4.5 In addition to regulating the SEM market design, the SEM Committee also oversees a number of all-island electricity market tariffs, including charges for generation capacity, the operation of the market (for SEMO) and market imperfections (for constraints). Details of the movements in the maximum amount recoverable for these SEM charges on an all-island basis are set out in Table 3 below.

Capacity charges

4.6 With the introduction of the new SEM market arrangements, a new Capacity Remuneration Mechanism (CRM) was also implemented. The new CRM is designed to secure sufficient generation capacity through a competitive auctions process to aid security of supply. The first auction secured c€200m annual reduction compared to the costs under the old SEM arrangements. The auction for 2019-20 cleared at a cost of €344.9m and this is the basis for

[6] https://www.semcommittee.com/news-centre/single-electricity-market-performance-1-april-2019-30-june-2019

supplier capacity charges in the upcoming tariff year.

Imperfection charges

4.7 Imperfections charges are mainly the costs associated with constraints on the all-island transmission network. Constraints are caused by network bottlenecks (such as the North-South interconnector, which is one of the most significant). These constraints result in the system operators (SONI and EirGrid) taking action to 'balance' the system in order to ensure stability of the electricity system. These actions are a normal and necessary part of electricity markets in other jurisdictions but are particularly important in the SEM, which is a small and highly constrained electricity system that has a high level of renewable generation.

4.8 The imperfection costs for 2019/20 have increased for two reasons. Firstly, the increase of renewables on the system e.g. wind, along with changes in the cost of generation has led to increased projected costs. Secondly, a substantial under recovery of imperfections revenue last year has added to the increase for this year's tariff. Further detail on the breakdown of imperfections costs available from the SEM Committee website[7].

4.9 For 2019/20, the imperfections charge is €355.8m compared to €183.8m for 2018/19. Given the significant impact of the under-recovery (the k-factor adjustment) we anticipate that this charge should reduce next year. The SEM Committee will also continue to scrutinise the core drivers of these costs. Going forward, the delivery of key network infrastructure such as the second North-South interconnector will help mitigate these costs further.

Market Operator charge

4.10 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).

4.11 The 2016-19 SEMO Price Control covers the period from 1 October 2016 to 31 March 2019[8]. There is a total entitlement under this Price Control of €1.2m for the upcoming tariff year, covering legacy costs associated with the

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[7] https://www.semcommittee.com/news-centre/imperfections-charge-201920-and-incentive-outturn-20172018-decision-paper

[8] 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

old market.

4.12 SEMO have submitted their Market Operator revenue requirement for tariff year 2019/20 which has been approved by the Regulatory Authorities. This revenue requirement of €11.3m matches the amount provided to SEMO within the new 2018-21 Price Control.

4.13 A K-factor for under recovery from the 2017/18 tariff year of €1.5m has been granted by the SEM Committee.

SEMO will therefore receive a revenue for 1st October 2019 until 30 September 2020 of €14.0m.

Overall SEM charges

4.14 Table 3 below shows the amount recoverable under the SEM charges in 2019/20. The amount has increased by 33.5%:

	2018/19 €m	**2019/20 €m**	**Change %**
Capacity	333.0	344.9	3.6
Imperfections charge	183.8	355.8	93.6
Market Operator charge	18.4	14.0	-24.2
Total	**535.2**	**714.6**	**33.5**

Table 3 : Charges regulated by the SEM Committee