

# Regulated Entitlement Values

2017/18 Tariff Year

September 2017



## 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 2017.

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.

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# 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 2017 -30 September 2018).

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 2017, 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<sup>1</sup>, SONI<sup>2</sup> and SEM website<sup>3</sup> 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 2016/17 (1 October 2016 – 30 September 2017), therefore, the comparisons made below are between two forecasted revenue entitlements. For the sake of simplicity and transparency we have not updated the 2016/17 forecast from last year<sup>4</sup>, however, we have accounted for the latest available information to us, in our forecasts for 2017/18.

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.

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<sup>1</sup> <http://www.nie.co.uk/About-NIE/Regulation/Regulatory-documents>

<sup>2</sup> <http://www.soni.ltd.uk/InformationCentre/Publications/>

<sup>3</sup> <https://www.semcommittee.com/publications/topics/tariffs-8>

<sup>4</sup> <https://www.uregni.gov.uk/news-centre/information-note-published-regulated-electricity-entitlement-values-20162017-0>

## 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 2017/18 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 2016/17 charge of £190.2 million to £194.0 million.

The increase is mainly related to K factor movements i.e. an underrecovery has arisen in the previous year which now has to be added to the underlying entitlement. Excluding K, the distribution entitlement is approximately the same at £190m.

The net effect of these factors is that the DUoS entitlement decreases by 1.5% in real terms.

#### **Specific comments on TUoS charges**

TUoS charges have increased from the 2016/17 charge of £30.1 million to £36.9 million.

The increase in TUoS charges are also impacted materially by K factor movements. The 2016/17 charge was lower than the underlying entitlement by £7.8m and while 2017/18 charges also benefit by inclusion of previous over recoveries of £2.6m the result is an increase in charges. Underlying entitlement has also increased in line with the RP6 determination which allocated a higher proportion of rates and pensions to transmission.

The net effect of these factors is that the TUoS entitlement increases by 18.3%

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 slightly decreased from the 2016/17 charge of £48.8 million to £48.2 million.

Future Network Charges will also consider the implementation of I-SEM costs, future DS3 decisions and the CMA consideration of the current SONI Price control that are currently on-going.

### **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.

The income for Moyle is £12.5m for the 2017/18 tariff year which is the same as last year.

## Overall network charges

To summarise: Table 1 below shows that the maximum amount recoverable for network charges will increase by 3.6% (nominal) with no increase in real terms between 2016/17 and 2017/18.

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 0.9% (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**

	<b>October 2016 - September 2017</b>	<b>October 2017 - September 2018</b>	<b>% Change (nominal)</b>	<b>% Change (real)<sup>5</sup></b>
Distribution charges (DUoS)	£ 190.2 m	£ 194.0 m	2.0%	-1.5%
Transmission charges (TUoS)	£ 30.1 m	£ 36.9 m	22.6%	18.3%
Support charges (SSS)	£ 48.8 m	£ 48.2	-1.1%	-4.5%
CAIR	£ 12.5 m	£ 12.5 m	0.0%	-3.5%
<b>Total Network Charges</b>	<b>£ 281.6 m</b>	<b>£ 291.6 m</b>	<b>3.6%</b>	<b>0.0%</b>

<sup>5</sup> This 'real' change accounts for the forecast of inflation. This has been estimated by the Office of Budget responsibility at **3.6%** (See here: <http://budgetresponsibility.org.uk/efo/economic-fiscal-outlook-march-2017/>) (supplementary economy tables, RPI for 2018).



## **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 have remained similar to previous years and the sale of land has resulted in a forecast refund to customers via the PSO in 17/18.

### **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 £5.4 million in the 2017/18<sup>6</sup> tariff year. This compares to a net saving of £2.0 million forecast for the 2016/17 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. Cost for 2017/18 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 under recovery for the 2017/18 year due to increased expenditure versus forecast on NISEP schemes and delays in the sale of land

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<sup>6</sup> 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.

within Landbank.

### Overall PSO charges

To summarise: Table 2 below shows that the maximum amount recoverable for PSO charges will increase from £3.0m to £5.3m for 2017/18.

**Table 2: Northern Ireland PSO charges**

	<b>October 2016 - September 2017</b>	<b>October 2017 - September 2018</b>	<b>£ Change (nominal)</b>	<b>% Change (real)</b>
Landbank	£ -0.2 m	£ -0.2m	£ 0.0 m	
Legacy generation costs/income	£ -2.0 m	£ -5.4m	£ -3.4 m	
NISEP + incentive	£ 9.2 m	£ 8.4m	£ -0.8 m	
K factor (negative = over recovery)	£ -4.0m	£ 2.5m	£ 6.5 m	
<b>Total PSO charges</b>	<b>£ 3.0 m</b>	<b>£ 5.3 m</b>	<b>£ 2.3 m</b>	<b>71.3%</b>

## 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 total capacity charge for 2017/18 has increased by 3.6%. The main driving influence in this increase is the 1.4% increase in Capacity Requirement. It is worth noting here that the Annual Capacity Payment Sum will cease on 23 May 2018 as the new I-SEM goes live, the total Capacity charge taking the first five months of each entitlement year results in both a 5.1% nominal and 1.4% real increase.

### 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 149.9% in nominal terms from the current tariff year. A major reason for the higher forecast entitlement is the low k-factor value (90% decrease from previous year) and also a provision included for I-SEM related costs accounting for 9% of the Imperfections revenue

requirement. Further information is available from the SEM committee website<sup>7</sup>.

### 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<sup>8</sup>.

SEMO have submitted their market operator revenue requirement for tariff year 2017/18 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 2015/16 tariff year. The market operator tariff has increased by 3.9% in nominal terms. The increase in tariffs reflects a change in k-factor from over to under recovery.

### Overall SEM charges

To summarise: Table 3 below shows the maximum amount recoverable, under the SEM charges in 2016/17, has increased by 20.8% (nominal) or 16.6% (real).

**Table 3: Charges regulated by the SEM Committee**

	<b>October 2016 - September 2017</b>	<b>October 2017 - September 2018</b>	<b>% Change (nominal)</b>	<b>% Change (real)</b>
Capacity charge <sup>9</sup>	€519.0 m	€539.0 m	3.9%	0.2%
Imperfections charge	€69.2 m	€173.0m	149.9%	141.2%
Market operator charge	€10.0 m	€10.34m	3.9%	0.3%
<b>Total charges</b>	<b>€598.2</b>	<b>€722.4 m</b>	<b>20.8%</b>	<b>16.6%</b>

<sup>7</sup> <https://www.semcommittee.com/publications>

<sup>8</sup> <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>

<sup>9</sup> The capacity charge is calculated and published on a calendar basis, these numbers have been adjusted to tariff year values for comparison with the other SEM charges.

## 4 Other costs

### **Energy**

The largest component of electricity bills is the cost of purchasing energy from the wholesale electricity market (the SEM). In order to offer fixed energy prices supplier often enter into forward hedges and final prices between suppliers will vary between suppliers and customers, depending on the extent, timing and duration of hedging contracts.

Whilst the SEM Committee does regulate bidding behaviour in the spot market, the wholesale energy component of bills is not regulated for most customers. In Northern Ireland this component remains regulated 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 0.568 p/kWh from 1 April 2017 and 0.583 p/kWh from 1 April 2018.

### **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.