



# **Consultation on Electricity Licence Fee Methodology**

**1 October 2010**

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## 2 INTRODUCTION

All electricity licence holders are required to pay an annual licence fee. This fee is calculated in accordance with a published methodology laid out in a determination document by the Authority. A permanent arrangement is required to replace the current temporary one. This consultation considers options for a permanent methodology.

The Electricity (Northern Ireland) Order 1992 (the Order) gives powers to issue licences and provision for the payment of a fee<sup>1</sup> for inclusion in those licences. All licences granted under Article 10(1) of the Order contain a condition which specifies that the holder of the licence is required to pay a fee. That fee shall be a proportion, determined by the Utility Regulator (in “the determination”). Prior to issuing the determination a methodology is disclosed in writing to the licensee. This estimates costs for the year in question in the exercise of its functions under the Order, the Energy Order, the SEM Order (Single Electricity Market) and the Directive Regulations. To date this apportionment has been made on the basis of an equal split across all licence categories (i.e. 1/3 Transmission and Distribution, 1/3 Supply and 1/3 Generation).

In the event that a licensee does not use their licence (i.e. they do not engage in market activity associated with the licence held and remain ‘dormant’<sup>2</sup>), the annual licence fee is charged at the ‘de-minimis rate’. This is currently £250 for supply and £1000 for generation.

Electricity Licence fees are collected once a year and historically invoices are issued during September. In addition to collecting fees in respect of licences issued by it,

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<sup>1</sup> A copy of the licence condition is included at Annex 1

<sup>2</sup> Of the 15 supply licences in force, 8 are ‘dormant’

the Utility Regulator also collects fees in respect of licences originally issued by the Department of Economic Development (now the Department of Enterprise Trade and Investment (DETI)).

Electricity Licence fees for 2009/10 were calculated in accordance with an interim methodology encapsulated in a determination that was put in place for the 2009/10 year. The methodology was originally intended to apply for 1 year only (1 April 2009 to 31 March 2010). It updated the methodology that had been in place since the industry was privatised and was first subject to regulation in the early 1990s. The update was introduced to ensure generators without a contracted capacity were charged appropriate licence fees. However, in order to give sufficient time for consideration of the options set out in this paper and for consultation with licensees, it is intended to calculate the 2010/11 licences on the basis of the terms of the interim determination.

### 3 CONSIDERATIONS

In reviewing the licence fee methodology we have identified a number of considerations:

- Cost reflectivity - licence fee charges should reflect the full costs incurred by the Utility Regulator as set out in the “payment of fees” condition in each licence and individual licensees should bear an appropriate proportion of those costs;
- To encourage the active use of licences and reflect the principle that obtaining a licence indicates an intention to use, accept and adhere to responsibilities that come with holding a licence;

- Current industry structure - we will want to consider the impact of recent changes to the structure of the industry e.g. we now have more small licence holders with the increasing focus on renewables, changes in company structure and ownership, licencable activity created for the SEM (e.g. SEMO);
- Transparent and understandable - the licence fee methodology should be straightforward to apply and easily understood by stakeholders; and
- Harmonisation: given SEM we will want to, where possible, avoid any unnecessary inconsistencies with CER's licence fee methodology.

## 4 CURRENT PRACTICE CONSIDERED

This section sets out the current practice in licence fee methodology for electricity, gas and water in the Utility Regulator for comparison between the industries. The practice in RoI and GB in relation to electricity licence fee charging and methodology is then described.

### 4.1.1 UTILITY REGULATOR ELECTRICITY LICENCES

The Utility Regulator, in accordance with the licence fee condition included in all licences, calculates electricity licence fees so as to recover the allowable cost of regulation each year. The practice since the inception of the organisation has been that, of the total costs to be recovered, 1/3 is payable by transmission and distribution licensees, 1/3 by supply licensees and 1/3 by generation licensees. It should be noted that regulated businesses can recover licence fees as part of their regulated entitlement. There are minimum fixed charges for all licensees whether they are active or not. A copy of the current determination detailing this is attached at Annex 2. Generation costs were historically based on contracted capacity however,

the 2009/10 determination changed this to Declared Net Capacity (DNC) for 2 reasons:

- 1) “contracted capacity” is a term peculiar to generators who were a party to generating unit agreements since 1992. The term is not applicable to any new entry since then; and
- 2) This terminology is recognised by the industry.

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#### 4.1.2 UTILITY REGULATOR GAS LICENCES

Gas directorate recovers its costs of regulation each year via licence fees also. The current practice is 80% of the fee liability falls to conveyance licence holders, with 20% to supply licensees. There is a fixed charge of £50,000 on conveyance licensees that participate in distribution, which is deducted from the total costs recoverable. A de-minimis amount of £1000 has been charged to suppliers and ‘dormant’ licence holders.

However a review has recently been carried out, with a new methodology being subsequently proposed. It is suggested that all supply licence holders would pay a fixed fee of £1500 (to increase annually based upon the Retail Price Index (RPI)). The remaining licence fee net of the fixed annual supply charges would be apportioned between the conveyance licence holders who participate in transmission activities on the basis of the total forecast volumes transmitted in that year.

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#### 4.1.3 UTILITY REGULATOR WATER LICENCES

This is a somewhat more straight forward affair, as apportionment is not required due to having only the one company, NI Water, who pay the total fee associated with the cost of regulation.

#### 4.1.4 CONSUMER COUNCIL NORTHERN IRELAND

The Utility Regulator is also required to recover the Consumer Council's Northern Ireland (CCNI) electricity, gas and water related costs each year. DETI approves and then notifies the Utility Regulator of the amount of CCNI related costs which need to be recovered each year and this amount is factored into the licence fee calculations before we issue the invoices. In electricity, CCNI costs were historically paid by NIE supply business. However, now that there is no longer a Public Electricity Supply company, CCNI costs are apportioned across all electricity supply licence holders on the same basis as our licence fee calculation i.e. using supply volumes. Gas directorate are proposing a change to CCNI cost recovery for gas matters; in that they are recovered from distribution licence holders, with apportionment based on forecast gas volumes distributed in the year to which the fees relate. For CCNI water related costs charges are applied to NI Water within their licence fee.

#### 4.2 COMMISSION FOR ENERGY REGULATION (CER), ROI CURRENT PRACTICE

Most fees are received as part of a levy collected under an annual statutory instrument. These are collected in quarterly stages. The levy relates to each activity of generation, transmission, distribution or supply.

Fixed quarterly levy amounts (specified in the statutory instrument) are payable for each of the following types of undertaking.

- Transmission system operator
- Transmission system owner
- Distribution system operator
- Distribution system owner

For generators connected to the transmission or distribution system (and registered under the SEM trading and settlement code (the Code)), 5.2 cent per megawatt hour (MWh), rounded to the nearest euro, is payable at the trading boundary on the forecast quantity of electricity in MWhs which it is estimated to be generated and/or supplied at the trading boundary in the billing quarter and the difference between the relevant quantity and actual quantity in the previous quarter.

In the case of generators with generating units below the de minimis threshold of 10MW (which are not required to be registered and are not registered under the Code), 5.2 cent per MWh, rounded to the nearest euro, is payable at the trading boundary on the forecast quantity of electricity in MWhs which it is estimated will be generated and/or supplied at the trading boundary in the billing quarter and the difference between the relevant quantity and actual quantity in the previous quarter.

The term “actual quantity” is defined as the quantity of electricity in MWhs which has been generated at the trading boundary which, in turn, is defined as the boundary between the transmission and distribution systems.

For suppliers, 5.2 cent per MWh of aggregated demand at the trading boundary, rounded to the nearest euro, is payable on the forecast quantity of electricity in MWhs which it is estimated will be generated and/or supplied at the trading boundary in the billing quarter and the difference between the relevant quantity and actual quantity in the previous quarter.

Generators and suppliers are required, under the terms of this system, to supply to CER;

- A statement of the forecast quantity of electricity in MWhs which it is estimated will be generated and/or supplied at the trading boundary in the



billing quarter no later than on the first day of each quarter; and thereafter within 25 working days of the end of each quarter;

- In the case of generators, a statement certified by SEM Operator or the Meter Registration System Operator as appropriate of the actual quantity for the relevant undertaking in the previous quarter; and
- In the case of suppliers, a statement certified by the SEM Operator of the actual quantity for the previous quarter.

Penalties apply where the provisions set out above are not complied with and interest is payable where payments due are not made.

In any quarter, where the actual payment is more or less than required, it is to be adjusted in the following quarter by the payee or CER as appropriate.

The Generation & Supply aspects of the levy present some difficulty for CER in their current format, particularly with the new Trading arrangements. It can sometimes take up to 4 months after the end of the quarter to receive actual trading data from industry participants leaving anomalies in expected income levels for the year. Adjustments for over/under recovery of levy income are made annually.

#### 4.3 OFGEM, GB CURRENT PRACTICE

Costs to be recovered by Ofgem, in respect of its electricity functions are recovered from network businesses that hold electricity transmission and distribution licences. The power to recover these costs arises from Standard Licence Conditions (SLCs) based on formulae set out below. These comprise an annual estimate of Ofgem's costs calculated in accordance with its cost control regime less income (other than that collected through SLCs) and a number of costs for other bodies. Where

exceptional costs arise, a methodology will be disclosed in the corporate plan or by means of another statement for dealing with these.

The basis of recovering costs from the relevant licence holders is based on the proportion of the total of electricity customers to the total of gas and electricity customers.

One half of the amount recoverable from electricity licence holders is allocated to holders of electricity transmission licences that have a “system operator standard condition” direction in effect on the licence (there is only one of these at present – if more than one emerges then further work on an apportionment would be necessary) and half allocated between electricity distribution licence holders. This is apportioned according to the proportion of electricity customers that are directly connected to any licensed electricity distribution network of that electricity distribution licence holder to the total number of electricity customers. Licence fees are treated as pass through costs for price control purposes.

Under BETTA (British Electricity Trading and Transmission Arrangements), Ofgem amended the special conditions of each of the transmission licensees to allow recovery of the licence fee from the system operator rather than all transmission licensees. The full Ofgem principles document sets this out more fully.

A reconciliation between the final version of the corporate plan for the relevant year, the funding voted by Parliament for the relevant year and the total sum being recovered for the relevant year through the ‘Payments by Licensee to the Authority’ SLCs will accompany invoices for licence fees.

The minimum licence fee payable will be £500 a year. Where the amount due under the formula set out above is less than this it will be rounded up to £500.

An electricity customer is:

Any energised or de-energised entry or exit point to the licensed electricity distribution system, where metering equipment is used for the purpose of calculating charges for electricity consumption. Customers should be identified from Metering Point Administration Numbers (MPANs), such that individual customers are identified at each connection point.

The total number of electricity customers is defined as the total number of customers directly connected to the licence holder's licensed electricity distribution network as at 30 September each year.

Only one individual customer should be identified at each connection point. This means aggregating multiple MPANs which arise due to the type of "tariff" (or equivalent) and/or metering arrangements but are associated with a single connection point (i.e. MPANs in respect of additional concurrent meters should be ignored).

In some cases (e.g. flats) the connection point may be from the licensed electricity distribution system to wiring owned by a landlord or a facilities manager. In such cases, individual customers supplied by such wiring are classed as customers of the licensed distribution system where they are identifiable from MPANs.

Any proposed changes to the licence fee methodology will be reflected in a new licence fee determination and would be subject to public consultation.

## 5 ELECTRICITY LICENCE FEE METHODOLOGY

The options that this paper presents for further consideration are the following;

- 1) Make a determination which applies the methodology used in the current interim determination. This would be adjusted to account for the inclusion of fees for all licences issued and for increasing costs on 'dormant' licences to an appropriate level to meet objectives. This is based upon the fact that the DNC for generation is a recognised one in the industry.
- 2) Charge all licence fees to T&D along the lines of the OFGEM model;
- 3) Adopt a form of the CER methodology for the purposes of aligning the methodologies used. However, aspects of the detail of the CER system maybe administratively burdensome and adoption of the principles behind this methodology would require careful thought to ensure that the practical arrangements were workable.

In addition to the consideration of various methodologies, there is an opportunity to consider revising the timing of fee collection so as to collect licence fees at the start of the Utility Regulator financial year. This will align with other directorates within the Utility Regulator and will lead to more efficient financial processes within the organisation. As is the case for the Water licence, a provision for the recovery of any additional costs in the current year could be included in addition to the facility to adjust for over-recovery or under-recovery in the following financial year.

Currently the Utility Regulator does not apply licence fees for the holder of the SEMO (SEM Operator) licence and the holder of the Transmission System Operator Licence, SONI Ltd. It is intend to apply licences fees to the organisations at the same level as dormant licences going forward.

## 5.1 OPTIONS

1. Make a determination to apply from 2011/12, applying the methodology used in the current interim determination which includes:
  - allowing for the issue of licence fee invoices at the start of the financial year and subsequent adjustment later in year and in the following financial year.
  - setting the de-minimis annual fee amount for “dormant” licences at £1500, (to increase annual based upon the Retail Price Index (RPI)) thus aligning this fee across directorates within the Utility Regulator.
2. Apply CER’s methodology.
3. Apply Ofgem’s methodology.
4. Continue the interim arrangements without any change.

## 6 RESPONSES TO THIS CONSULTATION

This consultation welcomes stakeholders views in relation to the options identified. Responses should be sent to the Utility Regulator by 5pm on Friday 26<sup>th</sup> November 2010 either by post or by email using the contact details below:

Simon Scott  
Utility Regulator  
Queen’s House  
14 Queen Street  
BELFAST  
BT1 6ED

[Simon.Scott@uregni.gov.uk](mailto:Simon.Scott@uregni.gov.uk)

**Condition 12: Payment of Fees**

- 1 The Licensee shall, at the times stated hereunder, pay to the Authority fees of the amount specified in or determined under the following paragraphs of this Condition.
- 2 Within 30 days after the grant of this Licence but in any event before <<INSERT DATE>>, the Licensee shall pay to the Authority an initial fee of £<<INSERT AMOUNT>>.
- 3 In respect of the year beginning on 1 April in the year following the grant of the licence and in each subsequent year, the Licensee shall pay to the Authority a fee which is the aggregate of the following amounts:
  - (a) an amount which is a proportion, as determined by the Authority, of the amount estimated by the Authority, according to a method which has previously been disclosed in writing to the Licensee, as likely to be its costs during the year in question in the exercise of its functions under the Order, the Energy Order, the SEM Order and the Directive Regulations in relation to the holders of licences granted under Article 10(1) of the Order;
  - (b) an amount which is a proportion as determined by the Authority of the amount estimated by the Authority (in consultation with the Competition Commission) as having been incurred in the calendar year immediately preceding the 1 April in question by the Competition Commission in connection with references made to it under Article 15 of the Order with respect to the Licence or any other licence issued under Article 10(1)(a)

of the Order; and

- (c) the difference (being a positive or a negative amount), if any, between:
- (i) the amount of the fee paid by the Licensee in respect of the year immediately preceding the 1 April in question less any refund paid to the Licensee in respect of that year under paragraph 4; and
  - (ii) the amount which that fee would have been in respect of that year had the amount comprised therein under sub-paragraph (a) been calculated by reference to the total costs of the Authority in connection with the functions referred to in sub-paragraph (a) and the proportion thereof actually attributable to the Licensee,

(such total costs being apportioned as determined by the Authority according to a method previously disclosed in writing to the Licensee),

and the fee shall be paid by the Licensee to the Authority within one month of the Authority giving notice to the Licensee of its amount, provided that notice is given within six months of the beginning of the year in respect of which the fee is payable.

- 4 In respect of the year beginning on 1 April of year subsequent to the grant of the licence and for each subsequent year, the Authority may pay the Licensee an amount (**the refund**) calculated in accordance with the method previously disclosed in writing to the Licensee and by reference to the difference between:

- (a) the proportion of the licence fee for that year paid by the Licensee which is attributable to the Authority's estimate of its costs in accordance with paragraph 3(a); and
- (b) the Authority's reasonable revised estimate of those costs provided that

any such refund shall be paid to the Licensee on or before 31 March in the year to which the fee relates.



### LICENCE FEES

Under the Condition on Payment of fees in your licence the Northern Ireland Authority for Utility Regulation (the Utility Regulator) is required to disclose to licensees in writing the method by which it has determined the proportion of the licence fee to be paid by each licensee.

As a result of previous correspondence with electricity licence holders the Utility Regulator has decided that, one-third of its electricity regulatory costs will be charged to the holders of generation licences, one-third to transmission and distribution licensees, and one-third to supply licensees. The total of electricity regulatory costs to be recovered is defined as the amount of the Utility Regulator's estimate of those costs associated with the regulation of the electricity industry (including relevant costs associated with the Single Electricity Market) in the forthcoming year plus or minus any deficit or surplus in respect of the current financial year.

Generation licence holders will pay a minimum fee each year of £1000 plus an apportionment of the balance of the 1/3 costs which will be charged to those licensees based on the Declared Net Capacity of each generating station or stations as agreed with Land and Property Services, a copy of which agreement shall be forwarded to the Utility Regulator before 31 May 09 and thereafter each and every time such agreement is amended.

Transmission licensees will pay a minimum fee each year of £1000. In addition the main transmission licence holder will pay the balance of the 1/3 costs to be charged to those licensees.

The 1/3 costs to be charged to supply licensees will be apportioned on the basis of supply measured in terms of megawatt hours and based on business activity in the previous year. Supply licensees will be required to provide actual end year (1 April – 31 March) megawatt

hour figures by the end of June each year so that licence fees can be set and invoices raised.

The General Consumer Council's costs will be met by all supply licence holders apportioned on the basis described above.

The Utility Regulator has further decided that there will be a minimum fee each year of £250.00.

Certain costs will be excluded from the above calculations and will be identified separately in the fee to be paid. These costs are referred to in the Payment of Fees Condition in the licences and include costs incurred by the Competition Commission in connection with references made to it.

In relation to references to the Competition Commission, or any successor body, identifiable external costs incurred by or on behalf of the Utility Regulator of references made under Article 15 of the Electricity (Northern Ireland) Order 1992 will be charged to any licence holder or group of licence holders, who are the subject of or connected with such references, in proportions which the Utility Regulator shall in its discretion determine.

In relation to future activities, other than Competition Commission references, undertaken by the Utility Regulator in the performance of its duties and functions under Articles 4 and 6 of the Order, where the costs of such activities exceed £5,000 and where the performance of those duties and functions is intended by the Utility Regulator only to affect a particular licence holder or group of licence holders, the Utility Regulator may charge to any such licence holder or group of licence holders the costs of such activities in proportions which the Utility Regulator shall in its discretion determine.

If any other situations occur, the Utility Regulator will decide how they are to be dealt with in the context of the licence fee setting method outlined above.