



Conclusion of the Utility Regulator's Review of the Power NI Ltd Maximum Average Price

Effective 1 April 2023



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

Protecting consumers is at the heart of the Utility Regulator's (UR) role and ensuring that domestic customers pay the correct price for electricity from the price regulated supplier Power NI Ltd is a core part of our work.

To this end the UR scrutinises Power NI submissions in relation to price changes and ensures that the maximum average charge per unit supplied is not more than the sum of the input costs allowed in the Power NI price control formula.

This ensures that customers pay no more than the efficient costs of purchasing and supplying the electricity plus an agreed profit margin set by the UR.

This review is the third that will occur alongside the implementation of the UK Government's Energy Price Guarantee Scheme (EPG) which applies a discount to the Power NI unit rate; and customers will pay the unit rate calculated after the discount has been applied. The discount is being funded by the UK Government and began on 1 November 2022. It applies across the UK to all electricity suppliers standard variable tariffs. However, the discount rate is lower for Northern Ireland.

Audience

Consumers and consumer groups; industry; and statutory bodies.

Consumer impact

The direct consumer impact of this review will be a change to the regulated electricity tariff. This change will affect domestic customers only. Domestic customers of Power NI will see a change to their tariff rates from 1 April 2023. The underlying Power NI standard tariff rates will decrease by 16.2%. However, the Energy Price Guarantee discount rate has also been reduced. This reduction off sets the reduction to the Power NI base tariff. The result is an increase of 14% to the actual price that Power NI customers will pay. The tariff and EPG rates will be reviewed again for Q3 2023 i.e. 1 July – 30 September.



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1. Approval by the Utility Regulator of the Power NI Ltd Maximum Average Charge per Unit Supplied

Summary

- 1.1 In January the Utility Regulator (UR), in consultation with Power NI, DfE and the Consumer Council, began a review of the Power NI maximum average charge for domestic customers. The current maximum average price has been effective from 1 January 2023. This review was triggered (as part of ongoing monthly monitoring) primarily due to a decrease in wholesale costs (this will be discussed in greater detail later in the paper). Therefore, a review was initiated to establish the new maximum average charge to become effective from 1 April 2023.
- 1.2 Since 1 January 2023, the price for customers on the Standard Home Energy tariff has been 38.81 pence per kWh (ex VAT).
- 1.3 Following a review, a decrease of 6.3 pence was deemed to be required to reflect falling wholesale costs, which would take the tariff to 32.51 pence per kWh (ex VAT).
- 1.4 However, the UK government have announced new discount rates for the Energy Price Guarantee¹ that will reduce the unit cost of electricity in NI by 3.77 pence per kWh (ex VAT) from 1 April 2023. The current Energy Price Guarantee discount is 13.61 pence per kWh (ex VAT) and is in place from 1 January 2023 to 31 March 2023. This means the current discounted rate that Power NI customers pay is 25.2 pence per kWh (ex VAT) i.e. 38.81 minus 13.61. The new discount rate of 3.77 pence per kWh will run from 1 April 2023 to 30 June 2023.
- 1.5 Therefore, this will mean that the new rate Power NI customers on the Standard Home Energy tariff will pay as of 1 April 2023 will be 28.74 pence per kWh (ex VAT). This equates to an increase of 14% to the existing rate.
- 1.6 Table 1 below shows the changes since January 2023 to unit rates (ex VAT) payable by Power NI customers.

¹ <https://www.gov.uk/government/publications/energy-bills-support/energy-bills-support-factsheet-8-september-2022>

Table 1 – Unit rate change

Rate (ex VAT)	p / kWh
Existing Rate (1 January)	38.81
Required decrease	-6.30
EPG discount	-3.7697
New rate (1 April)	28.74

- 1.7 Table 2 below shows the annual bill (including VAT) payable by Power NI customers.

Table 2 – Power NI domestic standard tariff (based on 3,200 kWh annual consumption)

	April 2023
Tariff Rate (p / kWh) without EPG Discount	34.1355
Supplier Annual Bill (£ / year) without EPG Discount	£1,092
EPG Discount (p / kWh)	3.9582
Effective Annual Bill (£ / year)	£966

- 1.8 The UR scrutinised Power NI's submission, ensuring that the maximum average charge per unit supplied is not more than the sum of the input costs allowed in the Power NI price control formula. Following agreement, the UR then wrote to Power NI stating that pursuant to Condition 55 and Annex 2 paragraph 2 of its licence the UR approved its submission reflecting the calculation of the "Mst" meaning the maximum average charge per unit. On 6 March 2023, the UR held a meeting with Power NI, the Consumer Council, and DfE. Here, the rationale behind the change was discussed and any questions addressed.
- 1.9 As is the usual practice, the tariff will be kept under constant review and adjusted if required. An adjustment would be necessary if changes in actual input costs (for example wholesale or network costs) created a significant difference between Power NI actual and forecast costs and revenues. The tariff would then need to be adjusted upwards or downwards to align costs and revenues.

Background

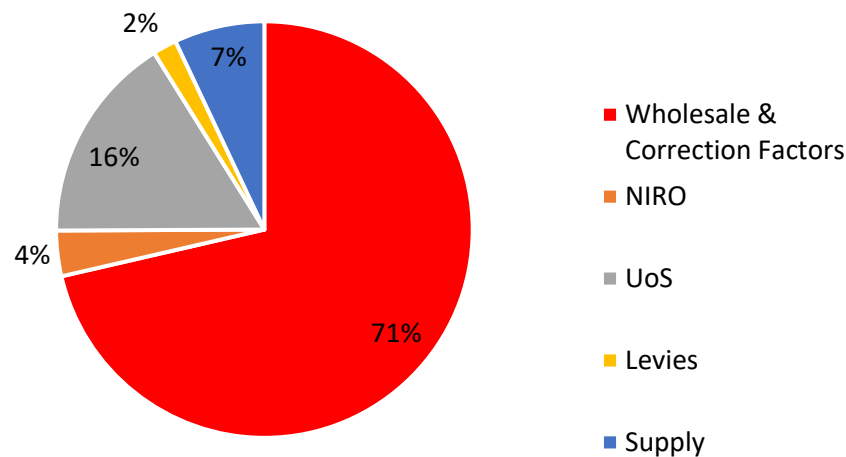
- 1.10 The domestic electricity supply market has been fully open to competition since 1 November 2007, and since June 2010 a number of suppliers have entered the domestic market. There are now five active suppliers in the domestic market (including Power NI). However, whilst facing competition from other suppliers, Power NI is still dominant in this sector of the market.
- 1.11 Under the terms of Power NI's licence to supply electricity, the Utility Regulator ("the Authority" or "UR") can ensure the maximum amount that Power NI can charge for electricity to domestic customers is not more than the price control allows.
- 1.12 The details of the operation of Power NI's supply price control are set out in its Licence. At present, Power NI's maximum allowed unit price of electricity (MS_t) for customers subject to and within the scope of price control is made up of a number of components:

$$MS_t = G_t + U_t + S_t + KS_t + (J_t - D_t) + E_t$$

2. Elements of the Maximum Average Charge

- 2.1 The UR takes an active role in scrutinising Power NI's proposed domestic regulated tariffs. The UR continues to set a price control that sets allowances for Power NI's operating costs and profit margin. In addition to this, any other Power NI operating costs that are passed through the tariff (which are not allowed for in the price control, e.g., licence fees) must be approved by the UR. The aggregate of the price control allowances and pass through costs are termed the supplier charge (see Figure 1 below).
- 2.2 Power NI retail tariffs (derived from the maximum average charge) for this upcoming year are made up of a number of components (including the supplier charge discussed above):

Figure 1 - Makeup of the maximum average tariff – 1 April 2023



These elements are further discussed in the sections below.

Levies and Use of System Charges

2.3 Several of the final tariff components are common across all suppliers and the final customer will usually pay these regardless of who their supplier is. These components are all subject to regulatory review and approval:

- Levies – System Support Services (SSS), Public Service Obligation (PSO); and
- Use of System charges (UoS) – these are the costs of transmission and distribution of electricity through the NIE Ltd network to homes and business.

2.4 These costs are regulated because they are levied to recover the costs of those parts of the electricity industry which are natural monopolies. Independent suppliers are free to enter the market and purchase power. They will usually add on the charges outlined above to their energy costs before setting the final price to sell to customers. This is because they are required to pay these charges in order to safely and securely transport the power to the customer.

2.5 For the purpose of setting an April 2023 tariff, the published Levy and UoS rates have been used where available and, where they haven't yet been published, forecast estimates for these network components have been used to derive the Power NI revenue requirement for them over the next 24 months. Generally speaking, an increase for RPI will be assumed for these elements in the absence of having the actual published tariff rates that will apply from April 2023 onwards. In addition to this RPI uplift, if other

information is available, e.g., from consultation papers or other sources, this will also be used to inform a best estimate of the rates if they have yet to be finalised. It is important to note that Power NI's tariffs will be adjusted in future depending on the actual cost out-turns that materialise, the forecasts used at this time are simply for initial tariff setting purposes.

- 2.6 The remaining components of Power NI's tariffs are subject to regulatory scrutiny and are detailed in the following paragraphs.

Wholesale Energy Cost and Over / Under recovery

- 2.7 The all-island Integrated Single Electricity Market (I-SEM) is both a competitive and regulated wholesale energy market on the island of Ireland. It is an all-island market encompassing the generation plants of both Northern Ireland and Ireland (RoI). Whilst in the previous SEM market there was one "pool" and timeframe which all suppliers would have to purchase from on a half hourly basis, as well as the potential to enter into "hedges" with generators to help limit exposure to price fluctuations, the new market has different markets and timeframes which the supplier can purchase energy from. These include:
- Day Ahead Market;
 - Intra Day Market;
 - Balancing Market (difference between the suppliers demand and what they have already purchased); and
 - Forwards Market (same principle as a hedge in the previous SEM).
- 2.8 Hedges effectively mean that the supplier is purchasing power on a forward basis at a fixed price based on forecast market prices (plus a premium). The approval of the Power NI hedging methodology is given by the UR, as well as the approval of the forecast of the total of Power NI wholesale costs for their estimated demand for the tariff period. Due to the fact that the wholesale energy component of final tariffs is both large and volatile, over or under recoveries of revenues in any tariff period are generally caused by wholesale energy costs out turning lower or higher respectively, than was forecast at the time of tariff setting. Over recoveries that occur in any given tariff period are handed back to customers in the subsequent tariff period and under recoveries are added to the total cost forecast of the subsequent tariff period.

2.9 Wholesale costs also include:

- Capacity Costs – these are the costs suppliers pay to help ensure there is sufficient generation available within the system in order to meet peak demand. Generators receive capacity payments even when they don't generate (for instance when wind generation is covering most of the electricity demand) but are incentivised to be available to do so should they be needed.
- Imperfection charges - these 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.

Supplier charge

- 2.10 The supplier charge is made up of the efficient costs of Power NI's own supply business and are approved by the UR. These costs are assessed and collected through the application of the Power NI Supply Price Control and any other costs approved on a pass through basis (after thorough regulatory scrutiny). The allowance set in the price control is for Power NI own operating costs (e.g. salaries, IT systems, rent and rates, legal fees, bad debt costs, keypad meter transaction costs and a target profit margin of 2.2% of forecast turnover). Other costs which are unknown, but treated as "passthrough" as they are unavoidable (e.g., licence fees, certain IT project costs), are allowed and these also go into the overall supplier charge.

NIRO costs

- 2.11 These costs are audited on behalf of the UR by Ofgem as part of its UK-wide audit. NIRO is the Northern Ireland Renewables Obligation and the costs of it go towards the subsidisation of investment in renewable energy, e.g., windfarms in Northern Ireland.

Why are Power NI's Tariffs decreasing?

- 2.12 The maximum average charge as calculated by the tariff formula will decrease by c.16.2% (as shown by the p/kWh required decrease in section 1.5), but the actual tariff charged to domestic customers will increase by 14% from 1 April 2023. This is due to the reduction of the Energy Price Guarantee discount that is being funded by the UK Government. Table 2 below shows the movement in the final price customers will pay after the EPG discount has been applied to the tariff. The final price fell by 0% on 1 January 2023 but will increase by 14% on 1 April 2023 despite the fall in Power NI's own tariff as this reduction is being offset by the reduction in the EPG discount from 13.61 p/kWh (ex VAT) to 3.77 p/kWh (ex VAT).

Table 2 - Historic Final Price (after EPG discount applied to tariff) (ex. VAT)

Effective from date	1 January 2023	1 April 2023
Approved Tariff (pence per kWh)	25.20	28.74
% Change	+0%	14%

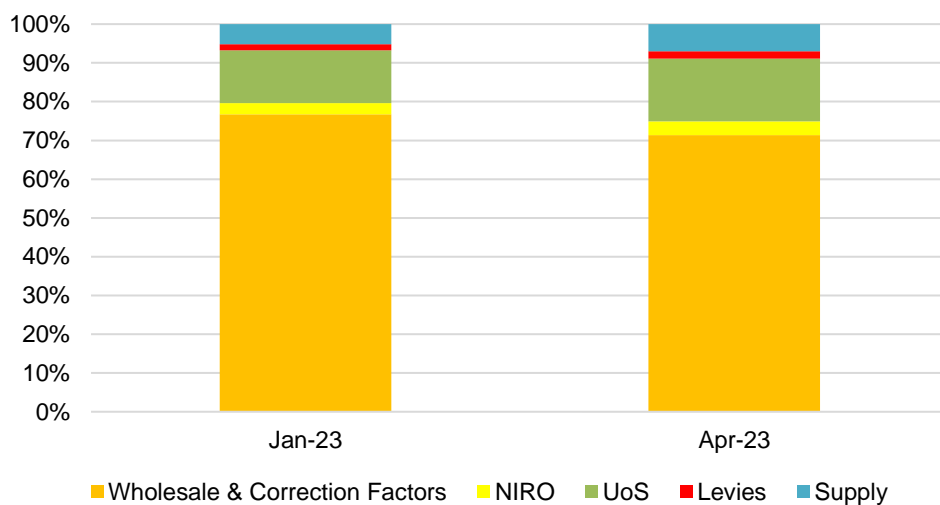
Wholesale Energy Cost and Power NI Under recovery element

- 2.13 Power NI have seen a reduction in energy costs since last setting the tariff in January 2023.
- 2.14 Until recently, there has been strong upward price pressure in the international fuel markets with both gas and carbon in particular, increasing significantly. This has had the result of increasing the cost of purchasing electricity generated in the SEM wholesale market. Energy costs have however softened in the past few months but are still trading at multiples of the prices experienced in 2020.
- 2.15 This upward price pressure in both the spot and forward markets continued throughout 2022.
- 2.16 However, as mentioned above the high wholesale costs have been offset by the UK government introducing the Energy Price Guarantee since 1 November 2022 that has reduced the unit cost of electricity in NI.

Breakdown of Tariff

- 2.17 The graph shown in Figure 2 below compares the breakdown of the April 2023 tariff with the breakdown of the previous tariff set at January 2023. This demonstrates that the wholesale energy element makes up a large proportion of the tariff costs and is similar to the January 2023 tariff in this regard.

Figure 2 – Breakdown of April 2023 tariff costs compared with a breakdown of the previous tariff costs



- 2.18 The annual bill² from 1 April 2023 will be £966 inclusive of VAT (and including the Energy Price Guarantee discount). This compares with a previous annual bill (based on the tariff set at January 2023) of £847. On this basis, a typical customer will pay £119 (14%) more than the effective (after EPG discount) January 2023 tariff.

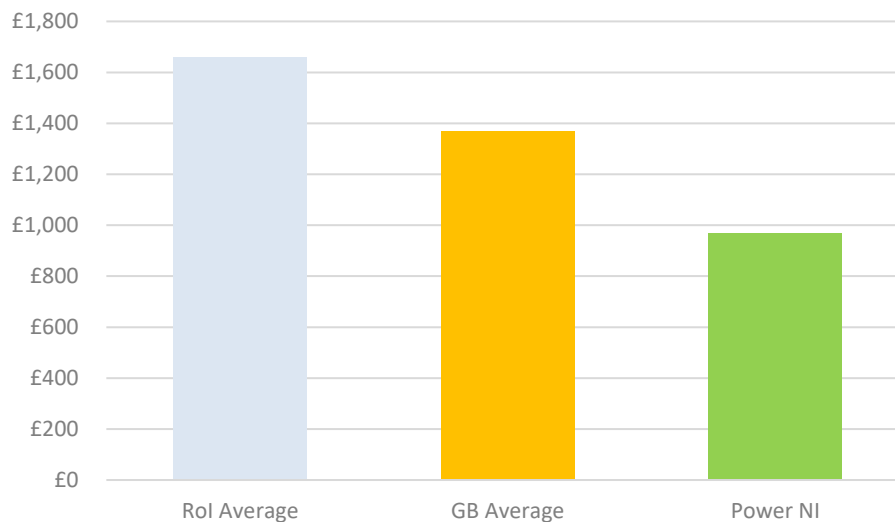
Comparison with GB

- 2.19 Figure 3 below shows the average annual bill for a Power NI domestic credit customer compared to the Republic of Ireland average annual bill and the GB Electricity Price Cap (including the UK Energy Price Guarantee discount). This comparison is based on the latest available information.

Figure 3 illustrates that the Power NI tariff for an average domestic credit customer will be circa 29% cheaper than the GB Electricity Price Cap which equates to £400 (after Energy Price Guarantee discounts have been applied). The Power NI tariff will also be 42% cheaper than the current annual bill in RoI which equates to a difference of £694.

² The average annual bill amounts have been calculated based on the standard domestic tariff set at each tariff review (including VAT) and are based on an average annual consumption of 3,200 kWh as has been used in previous years.

2.20 **Figure 3 - Comparison of average annual bill in GB and RoI with Power NI (based on estimated usage 3,200 kWh p/a including VAT and EPG related discounts) as of 1 April 2023**



NB 3,200 kWh represents typical average consumption which has been used in previous years for tariff comparison

Both Power NI and GB prices include Energy Price Guarantee (EPG) discounts. No discount applies to the RoI average annual bill figure.

Outcome

- 2.21 The Utility Regulator has reviewed the Maximum Average Price submission provided by Power NI and the calculated final price customers should pay after the Energy Price Guarantee discount has been applied. The Utility Regulator is satisfied that the calculated price decrease is appropriate and therefore agrees the new standard domestic tariff of 28.74 pence per kWh (ex VAT) from 1 April 2023.