REASONS BEHIND INCREASES IN PSO, DUoS, TUoS and SSS

Information Note

September 2009

1 – Introduction

New regulated retail tariffs are due to come into effect in Northern Ireland from 1 October 2009. A number of the elements that have been used to create these tariffs have substantially varied from the previous year and to increase transparency in relation to this issue the Utility Regulator has published this note providing information on these variations and the reasons that they have occurred.

	2008/09	2009/10
	£m	£m
NFFO / ROCs	-3.943	0.432
Landbank	0.095	0.093
CBO allocation	20.711	20.715
Kilroot Flue Gas Desulphurisation	22.760	23.960
Excess Legacy Generation costs	-37.540	-15.102
Market Costs	10.213	7.958
Energy Efficiency Prog. Funding	6.822	7.780
PSO Total Charges	**19.118**	**45.836**
Distribution Use of System (DUoS)	156.678	164.683
Transmission Use of System (TUoS)	35.372	35.757
SSS	20.550	24.180
Total	**£231.718**	**£270.456**

Table 1 PSO, UoS and SSS comparison to previous tariff year

Table 1 shows the comparison between individual elements within the Public Supply Obligation (PSO), Distribution Use of System (DUoS) and Transmission Use of System (TUoS) for both 2008/09 and 2009/10. An impact on all of these costs has been the reduction in electricity demand during 2009 below predicted levels leading to additional cost recovery required in the 2009/10 tariff year. These are revenue tariff requirements and the impact of these changes on individual tariffs will vary in relation to any projected demand in 2010. The PSO figure in table 1 does not reflect the PSO reduction in January 2009; it is comparing the position at start of October 2008 to the current position in October 2009.

NFFO contracts and ROCs are managed by NIE Energy Supply. Any costs associated with these processes are claimed through the PSO. The majority of NFFO contracts ended in March 2009 and the volumes of energy have significantly reduced. This has impacted on this value.

The Customer Buy Out (CBO) allocation costs relate to the customer buy out of Ballylumford contracts and these costs are due to end in March 2012. The Kilroot Flue Gas Desulphurisation costs end 1st November 2010.

Historically within the use of system tariff setting process increases have been applied as a percentage increase across the tariff groups however EU legal requirements require this to be revised and a more cost reflective approach to be adopted. It should be noted that the cost reflective pricing model has led to larger than average changes, both positive and negative, within individual tariffs. This change is part of a two stage approach by the Utility Regulator to meet its legal obligations. The change in DUoS to cost reflective pricing is the first stage with a planned change in TUoS to cost reflective pricing next year completing this approach. The Utility Regulator plans to hold a workshop this winter in relation to this issue. This will be aimed at increasing transparency in relation to cost reflective requirements and the impact of cost reflective tariffs.

2 - Reasons Behind Increases

Excess Legacy Generation costs

The reduction in excessive legacy generation costs from 2008/09 to 2009/10 reflects the expected reduced running of Kilroot Power Station due to gas prices. In December 2008 NIE's Power Procurement Business (PPB) was in a position to return a substantial amount of money to the customer. This was due to PPB selling contracts for electricity generation to suppliers in the summer without backing off these sales with fuel "hedges". This was done with regulatory approval. As fuel prices fell in the latter half of 2008 a surplus was built up, and by December it was around £100m. This allowed a one-off reduction in the PSO charge for the remainder of the tariff year, which was deemed the best method of returning this money to all customers. This led to a negative PSO value to customers. This is not reflected in the table as this relates to the January 2009 reduction.

Market Costs

Costs attributable to the approval of Further Residential Market Opening (Enduring Solution) are within market costs. These are costs both for the initial stage and for stage 2. These include the costs of NIE scoping various options and carrying out a full procurement exercise for a suitable implementation partner for a project that will entail exiting their moribund legacy system and installing a new set of market systems. These systems will facilitate a fully competitive domestic market. This will ensure compliance with EU Directives regarding full business unbundling and competitive electricity markets.

Other items included within these costs that have led to an overall reduction in market costs are the Fuel Security Code and an adjustment for under recovery from the previous year.

Distribution Use of System (DUoS)

The increase in DUoS is due to primarily due to under recovery in the previous tariff year. The overall required review regarding DUoS has led to changes within the DUoS charging groups. In the past Use of System costs were weighted towards greater revenue recovery from those customers with higher peak demand. The cost reflective pricing that has been applied to distribution costs has higher standing and availability charges. It also produces a more constant phasing of revenue recovery throughout the year for some customers.

Transmission Use of System (TUoS)

Transmission Use of System costs have not moved to a cost reflective model this year but as there are legal obligations on regulators from EU directives to be cost reflective it is intended to apply a cost reflective approach to Transmission costs next year.

System Support Services (SSS) Charges

Under recovery and demand reduction account for 8.5% of the increase in SSS tariff. Ancillary Services has also seen an increase due to change in allocation of grid code penalty payments, increase in Moyle low frequency reserve provision and an addition of high frequency response via Moyle.

The biggest driver in the increase in the SSS tariff is the ETSO (European Transmission System Operators) scheme. The purpose of the scheme is to compensate Transmission System Operators across Europe for use of their network for transit flows. In 2007 the Utility Regulator approved SONI’s signing up to the scheme. The cost was originally estimated to be relatively small, however the complex methodology proved to be impossible to predict and the out-turn is much higher. (A £200k provision was made in 2008/9 tariffs, but the outturn cost was £814k.) This methodology is currently being reviewed, with the new method due to be in place by 2011. The EU framework imposes this cost onto system operators, therefore at present it can only be collected via the SSS tariff (SONI’s source of income). This current charging framework is defined in SONI’s licence. There is an expectation that the SSS allowance will significantly reduce for the next tariff year.