Northern Ireland Authority for Utility Regulation

Review of Power NI BEQ

July 2013

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1 Executive summary

Background

1.1 Power NI has submitted its BEQ setting out its projected operating costs for the years ending 31 March 2015 and 2016. In accordance with our contract with the Northern Ireland Authority for Utility Regulation ("NIAUR" or "the Regulator") we have carried out a review of those projections and our findings and recommendations are set out in this report.

1.2 The background of this review is that Power NI and the Utility Regulator do not anticipate any material growth in the underlying demand for electricity or any significant additional demands on Power NI that would have a material impact on its cost base. Both Power NI and the Regulator expect that Power NI's customer base will continue to fall over the period of the next price control.

1.3 Notwithstanding the anticipated reduction in customer Power NI considers that its costs, in the short to medium term, are fixed. This position has been broadly accepted by the Regulator.

1.4 Our review has not included outsourced costs as these are the subject of a separate review.

Projected costs

1.5 Power NI's submitted cost projections, excluding outsourced costs, in 2012/13 prices are as follows:

Summary of Power NI BEQ		Actual		LBE		Forecast
Real 2012/13 Prices	2009/10	2010/11	2011/12	2012/13	2013/14	2014/15
	£m	£m	£m	£m	£m	£m
Salaries	4.256	4.913	4.929	5.888	6.163	6.215
MBIS	2.934	2.700	4.181	3.409	3.403	3.243
Agents	4.256	4.142	4.181	4.013	3.818	3.686
Corporate Charges	1.229	1.202	1.325	1.283	1.434	1.484
Bad Debt	3.131	2.828	2.653	3.228	3.265	3.263
BEQ total excluding outsourced costs	**15.806**	**15.785**	**17.269**	**17.822**	**18.082**	**17.891**

Source: Derived from Power NI BEQ

1.6 The costs for 2012/13 are the latest best estimate ("LBE") at the time that the BEQ was prepared. Actual costs for that year are not materially different to the LBE. We have therefore reviewed the projected costs in the context of the LBE 2012/13 costs.

1.7 After adjusting for a number of one off items we have arrived at underlying cost for 2012/13 (excluding outsourced costs) of £17.01m. A reconciliation of actual LBE costs for 2012/13 to our adjusted costs is as follows:

Analysis of BEQ One-off costs in FY13	**£m**
Power NI FY13 BEQ opex total	**19.96**
Less: Outsourced costs	(2.14)
Power NI FY13 BEQ opex total exc. Outsourced	**17.82**
Less: one-off costs	
MBIS Agency staff	(0.25)
MBIS Pension scheme administration	(0.15)
Bad debt	(0.30)
Agent Costs Postage	(0.11)
FY13 costs excluding non-recurring cost items	**17.01**

1.8 Given the trends in the business and the broad acceptance of the fixed cost nature of the business we consider that Power NI's costs for 2014/15 should be consistent with the above adjusted figure of £17.01m.

1.9 Power NI's projected costs for 2014/15 per the BEQ are £17.89m with the key movements set out in the table below:

Summary of Power NI BEQ Real 2012/13 Prices	**LBE 2012/13**	**One-offs 2012/13**	**Adjusted 2012/13**	**Forecast 2014/15**	**Key Movements 2014/15**
	£m	**£m**	**£m**	**£m**	**£m**
Salaries	5.89		5.89	6.21	0.33
MBIS	3.41	(0.40)	3.01	3.24	0.23
Agents	4.01	(0.11)	3.90	3.69	(0.22)
Corporate Charges	1.28		1.28	1.48	0.20
Bad Debt	3.23	(0.30)	2.93	3.26	0.33
BEQ total excluding outsourced costs	**17.82**	**(0.81)**	**17.01**	**17.89**	**0.88**

Source: BDO

Key findings and recommendations

1.10 We have reviewed the arguments put forward by Power NI to support the above projected increases in costs and are detailed comments are set out the following sections of our report. In summary we consider that, in the context of the expected trends in the business, the following adjustments should be made to Power NI's projected costs for 2014/15:

Summary of Power NI BEQ Real 2012/13 Prices	Forecast 2014/15	Recommendation 2014/15	Variance 2014/15
	£m	**£m**	**£m**
Salaries	6.215	5.964	(0.251)
MBIS	3.243	3.083	(0.160)
Agents	3.686	3.686	0.000
Corporate Charges	1.484	1.351	(0.133)
Bad Debt	3.263	2.960	(0.303)
BEQ total excluding outsourced costs	**17.891**	**17.044**	**(0.847)**

Source: BDO

1.11 The above adjusted figure of £17.044m is consistent with our estimate of Power NI's adjusted costs for 2012/13.

2 Introduction

2.1 BDO LLP ("BDO") has been instructed by the Regulator to review the BEQ Operating Costs submission prepared by Power NI for the Price Control Period beginning 1 April 2014. The BEQ includes Power NI's historical operating costs for the financial years 2009/10 to 2011/12, 10 months actuals plus 2 years forecast to arrive at Latest Best Estimate for the year 2011/12, and forecasts for the years 2013/14 and 2014/15. This report sets out the findings of our review and associated recommendations.

2.2 This report is one of a series of reports relating to the Northern Ireland Authority for Utility Regulations (NIAUR) price control review of Power NI for the Price Control Period commencing 1 April 2014.

Scope of work

2.3 The scope of our review as specified by NIAUR was to review the following BEQ categories:

- Salaries;
- Materials;
- Bad Debt;
- Agents Costs; and
- Corporate Charges.

2.4 Outsourced Service costs were substantially dealt with by NIAUR using a specialist associate. We have limited our scope to a description of key trends in this area, and have not commented on the reasonableness of the forecast operating costs for Outsourced Services.

2.5 The key deliverable from this assignment is a recommended Opex Baseline for 2014/15, to be consulted upon.

Approach

2.6 Our approach was based on a review of the BEQ submission prepared and submitted by Power NI. We reviewed the BEQ submission at a 'top down' level, focussing on areas which showed significant shifts in costs or one-off costs across each of the financial years provided. We also reviewed the operating costs for reasonableness in the context of Power NI having a shrinking customer base. We have not reviewed the efficiency of Power NI's operating cost base. Power NI's efficiency was previously reviewed in 2011 and we understand that NIAUR considers that Power NI has a reasonably efficient cost base.

2.7 We held an initial meeting with staff from Power NI on 23 April 2013 followed by meetings on 29 April 2013 and 9 May 2013 at which the BEQ submission was discussed.

2.8 Following these meetings we produced a document summarising the matters discussed. We shared this document with Power NI for comment. Power NI responded on 20 May 2013 to confirm their understanding of the discussions. The document issues to Power NI did not contain any opinions or conclusions in relation to the BEQ.

2.9 Following confirmation of factual matters, we conducted our analysis and developed a draft report to NIAUR. We discussed our draft findings with Power NI and their advisers at a workshop on 29 May 2013. Power NI provided further information and arguments in relation to our draft proposals, and we then finalised this report, which represents the key deliverable from this area of the Price Control review.

2.10 This report does not include any comment on the reasonableness of the apportionment of operating costs included in the BEQ submission between the regulated and unregulated areas of Power NI's business. A report on the apportionment of such costs has been prepared as a separate area of work within the overall Price Control review.

Structure of this report

2.11 To address the above requirements, the rest of this report is structured as follows:

(i) Section 3 summarises the BEQ data submitted by Power NI;

(ii) Section 4 considers the salary and payroll costs, Power NI's assumptions and HR plans in further detail;

(iii) Section 5 considers Materials and Bought in Services costs and their assumptions in further detail;

(iv) Section 6 considers bad debt charges;

(v) Section 7 covers agent costs;

(vi) Section 8 addresses Corporate charges levied by the Viridian Group; and

(vii) Section 9 is our overall assessment of the Power NI forecasts and our recommendations in relation to baseline opex for 2014/15.

The key sources of information for this report are the Power NI BEQ and the nominal and real excel forecasts. These records are held by NIAUR and have not been appended to this report.

Throughout this report the terms 'real' and 'nominal' are used. For this price control the year 2012/13 is the base year and when we state that figures are in real terms we refer to 2012/13 prices.

3 Summary of Power NI BEQ submission

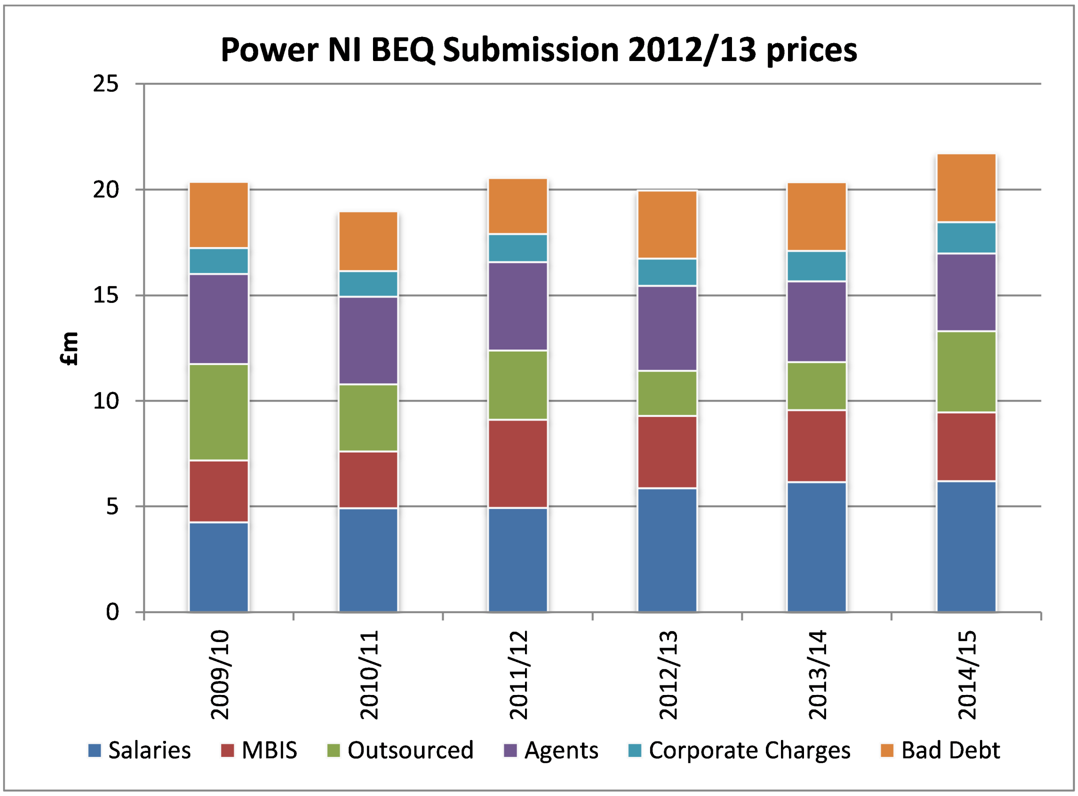
3.1 In this section of our report we set out a summary of Power NI's BEQ operating cost submission and consider the high level business trends impacting on Power NI's business over the forecast period.

Summary of Power NI's BEQ Submission

3.2 Power NI's BEQ submission is summarised below in tabular and graphical formats:

Summary of BEQ - Real 2012/13 Prices	Actual			LBE	Forecast	
	2009/10	2010/11	2011/12	2012/13	2013/14	2014/15
	£m	£m	£m	£m	£m	£m
Salaries	4.256	4.913	4.929	5.888	6.163	6.215
MBIS	2.934	2.700	4.181	3.409	3.403	3.243
Outsourced	4.556	3.182	3.280	2.141	2.274	3.826
Agents	4.256	4.142	4.181	4.013	3.818	3.686
Corporate Charges	1.229	1.202	1.325	1.283	1.434	1.484
Bad Debt	3.131	2.828	2.653	3.228	3.265	3.263
Total	**20.362**	**18.967**	**20.549**	**19.963**	**20.357**	**21.717**
ICT / AMS Expenditure						**-1.559**
Total excl ICT / AMS				**19.963**	**20.357**	**20.158**

Source: Power NI



Source: BDO, derived from Power NI BEQ Submission

3.3 Power NI's operating costs for the base year, FY13, are £19.963m. The biggest single element of these costs relates to staffing (29.5%).

Background

3.4 Power NI is an electricity supplier in Northern Ireland. Power NI's business is currently split between regulated energy supplied and unregulated energy supplies. Unregulated supplies are currently made to customers with annual levels of consumption greater than 150MWh per annum. All other supplies are regulated, and subject to the Price Control.

3.5 As part of the current Price Control Review, NIAUR is considering whether the current regulation threshold of 150MWh per annum should be revised. Power NI has proposed that all supplies of energy to non-domestic customers should be unregulated and has prepared its forecast information for the Price Control Review based on an assumption that all non-domestic supplies will be unregulated with effect from 1 April 2014.

3.6 Power NI's regulated operating cost base is historically a small proportion of its overall operating costs. In FY12, energy costs comprised around 95% of the overall operating cost base of Power NI. As energy costs are charged to regulated customers on a pass-through basis, Power NI's regulatory cost base has a small impact on consumers, relative to some other regulated businesses.

Base year position

3.7 For the purposes of this price control, the financial year ended 31 March 2013 has been taken as the base year.

3.8 Operating costs in 2012/13 were projected to be £19.963m, down in real terms from £20.318m in 2011/12.

3.9 2012/13 costs included a number of one-off items. Adjusting for these one-off costs, the total operating expenditure of Power NI (excluding Outsourced costs) was £17.01m in the base year:

Analysis of BEQ One-off costs in FY13	£m
Power NI FY13 BEQ opex total	**19.96**
Less: Outsourced costs	(2.14)
Power NI FY13 BEQ opex total exc. Outsourced	**17.82**
Less: one-off costs	
MBIS Agency staff	(0.25)
MBIS Pension scheme administration	(0.15)
Bad debt	(0.30)
Agent Costs Postage	(0.11)
FY13 costs excluding non-recurring cost items	**17.01**

Source: BDO

Comparison of Latest Best Estimate (LBE) to Actual

3.10 As the BEQ was prepared by Power NI prior to the commencement of our work on the review, the 2012/13 LBE figures have been superseded by unaudited actual figures. We requested that Power NI provide an analysis of base year actual opex to the LBE figures, and comments on the variances. Power NI's response is shown below:

Power NI analysis of actual outturn vs BEQ operating costs	FY13 Actual £'000	FY13 BEQ £'000	Var (Dec)/Inc £'000	Comments
Salaries (incl Agency Staff)	6,359	6,460	-101	Timing of new starts and earlier release of staff post enduring soluton
MBIS (excl Agency Staff & incl Agency Costs)	6,986	6,851	135	Higher consultancy and legal advice costs
Bad Debt	3,323	3,228	95	increase in the specific bad debt provision in respect of commercial customers and a higher provision rate applied to keypad customers with years to pay greater than 20 years
Outsourced services	1,987	2,141	-154	Lower IT seperation costs, lower Capita costs (primarily Licenses costs)
Outsourced services - AMS/ICT	1,325	0	1,325	BEQ assumed pass through of these costs through
Other interbusiness	1,283	1,283	0	In line with BEQ
	21,264	19,963	1,301	
Total Opex excl AMS/ICT	**19,939**	**19,963**	**-24**	

Source: Power NI

3.11 AMS / ICT costs are currently not included within the regulatory operating cost base under the St term, and have not been included in the Power NI BEQ analysis for FY13.

3.12 While noting variances within individual cost headings, the overall outturn is consistent with the BEQ projections for the year. We therefore consider the BEQ figures to be a reasonable basis for use as a base year comparator in reviewing Power NI's BEQ forecasts for the period to FY15.

FY13 LBE – analysis of actual and forecast expenditure

3.13 The split of actual and forecast expenditure is shown below:

Summary of BEQ - Real 2012/13 Prices	Actual FY13	2 months LBE f'cast FY13	Forecast pro-rata	Forecast pro-rata/actual
Salaries	4.853	1.035	5.174	106.6%
MBIS	2.702	0.708	3.539	131.0%
Outsourced	2.794	-0.653	-3.267	-116.9%
Agents	3.547	0.466	2.332	65.7%
Corporate Charges	0.965	0.318	1.590	164.7%
Bad Debt	2.485	0.743	3.716	149.5%
Total	**17.346**	**2.617**	**13.083**	

Source: Derived from Power NI BEQ information

3.14 The Forecast pro-rata figures are based on the 2 months LBE forecast multiplied by 5, to arrive at a figure with comparison with the 10 month actual figures.

3.15 We requested an explanation from Power NI in relation to the variations shown in profiling of costs. The explanations received are set out below:

3.15.1 Salaries: salaries are marginally higher in the forecast periods due to phasing, reflecting the fact that the actual figures would have had costs recharged to the Enduring Solution project and therefore the actual costs appear lower on a like for like basis. This is partly offset by the fact that from 1 Oct 12, HR staff moved from Power NI to Viridian Corporate

3.15.2 MBIS: costs are higher in the forecast period reflecting price control, legal and consultancy work being undertaken in the latter part of the year together with the timing of marketing spend.

3.15.3 Outsourced: the actual costs included post Enduring Solution go-live ICT/AMS costs. The forecast assumes that these are reclassified into pass-through, this is partly offset by the latter part of the year including uplifts in the Northgate contract in respect of RPI.

3.15.4 Agents: the lower forecast costs reflect lower transactions based on lower customer numbers due to competition, lower charges driven by lower monetary transactions as the forecast transactions are all at the lower tariff pricing and the forecast includes the release of surplus accruals.

3.15.5 Corporate charges: the higher forecast charges are driven by a more up to date allocation by Viridian Corporate part way through the year based on the Corporate cost LBE and higher HR costs being include from 1 Oct 12 (prior to this, these costs were incurred by the business).

3.15.6 *Bad debt: the higher bad debt forecast charge reflects the fact that around the year end debts outstanding 2 years are written off coupled with the fact we look at our bad debt provisioning at year end in more detail prior to our year end accounts being finalised.*

Source: Power NI

Overview of Forecasts

3.16 Power NI's BEQ forecasts are summarised below:

Summary of BEQ - Real 2012/13 Prices	LBE	Forecast	
	2012/13	2013/14	2014/15
	£m	£m	£m
Salaries	5.888	6.163	6.215
MBIS	3.409	3.403	3.243
Outsourced	2.141	2.320	3.980
Agents	4.013	3.894	3.835
Corporate Charges	1.283	1.434	1.484
Bad Debt	3.228	3.265	3.263
Total	**19.963**	**20.479**	**22.020**
ICT / AMS Expenditure			**-1.559**
Total excl ICT / AMS	**19.963**	**20.479**	**20.461**

Source: BDO

3.17 We have excluded the impact of ICT / AMS expenditure to arrive at a like-for-like expenditure figure in FY13 and FY15, as ICT / AMS is currently provided for as a passthrough 'Et' cost.

3.18 Power NI's operating cost base, excluding ICT / AMS, is forecast to increase from £19.963m in FY13 to £20.461m in FY15, a real increase of 2.5%.

Business environment

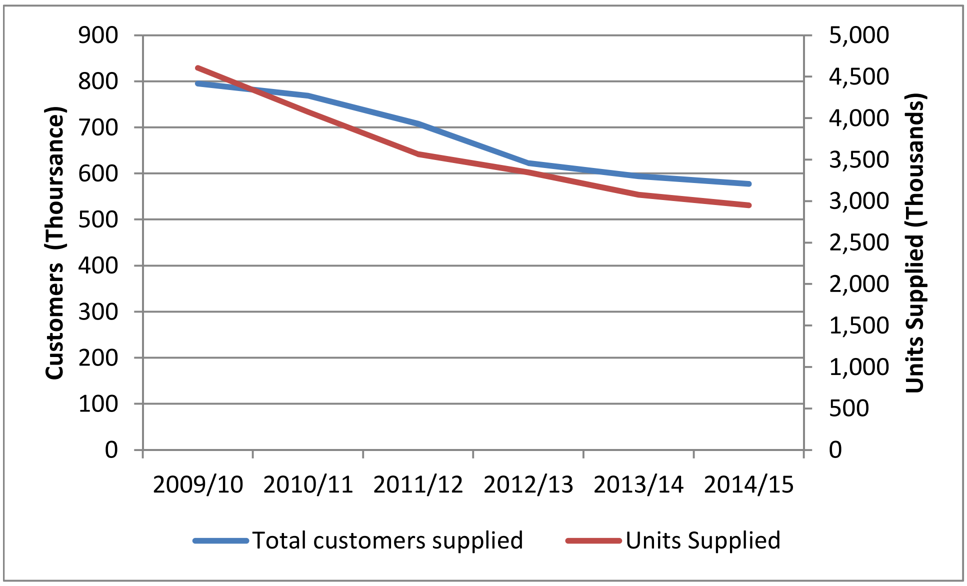
3.19 In this section we have described the high level issues which have impacted on Power NI's business during the BEQ period. These centre around overall business volumes and insourcing of previously outsourced services.

Customer numbers and units supplied

3.20 Since the introduction of competition in the NI energy supply market, customers have been able to choose their energy supplier. As Power NI was previously the only supplier in the market, an element of its market share has transferred to new entrants.

3.21 Power NI has provided actual and forecast information on customer numbers and volumes of electricity supply as part of its BEQ submission. This information is summarised below.

Customer numbers are based on figures at each year end. The information provided is for the whole business, including both regulated and unregulated customers / supplies.



Source: Power NI BEQ

3.22 Power NI's customer numbers reduced from 795,000 in March 2010 to 708,000 in March 2012. Since the introduction of measures to enable keypad customer to switch with effect from 20 May 2012, Power NI has experienced further increases in switching levels and has forecast customer levels at March 2013 to be 622,000, a loss of 85,000 in FY13.

3.23 Power NI envisages that switching rates will decline over time. Projected levels of decreases in net customer attrition in FY14 and FY15 are 28,800 and 16,200 respectively.

3.24 Power NI has provided us with a high level analysis of its customer switching assumptions, which show that over 96% of net customer changes in the period to FY15 are assumed to be domestic customers. Around 38% are domestic credit customers, with around 58% assumed to be domestic keypad customers.

Insourcing of Billing Services

3.25 Power NI's staffing costs increased in FY13 compared by FY12 by around £850,000 as result of the insourcing of the BPO and billing service from Northgate. Outsourced costs reduced by around £1.06m arising from the same change.

3.26 Power NI estimated that initial project costs associated with the insourcing would be £450,000, and that the project would deliver annual savings of £145,000 per annum.

4 Salary costs

4.1 In this section we have reviewed the Salary costs BEQ submission in detail.

Information Provided by Power NI

4.2 Breakdown of salary costs:

Breakdown of Salary Costs	Actual			LBE	Forecast	
	2009/10	2010/11	2011/12	2012/13	2013/14	2014/15
	£m	£m	£m	£m	£m	£m
Payroll costs re 100% employees						
Basic salaries and wages expense	3.365	3.448	3.642	4.468	4.628	4.659
Overtime & shift allowances	0.004	0.021	0.014	0.029	0.000	0.000
PSA	0.000	0.000	0.000	0.007	0.000	0.000
Payroll Service Charge	0.000	0.000	0.000	0.001	0.001	0.001
Employers National Insurance Contributions	0.321	0.349	0.389	0.459	0.465	0.472
Bonuses & profit related pay	0.090	0.457	0.434	0.299	0.325	0.317
Pension costs - defined benefit plan	0.296	0.480	0.308	0.436	0.495	0.495
Pension costs - defined contribution plan	0.175	0.206	0.186	0.185	0.205	0.227
Cash For Cars	0.032	0.032	0.034	0.030	0.022	0.022
Smart Pension Scheme Employer Offset	-0.108	-0.133	-0.140	-0.152	-0.079	-0.079
Deferred share awards	0.000	-0.031	0.000	0.000	0.000	0.000
Other allowances (please provide details)	0.082	0.084	0.063	0.126	0.101	0.101
Total	**4.256**	**4.913**	**4.929**	**5.888**	**6.163**	**6.215**

Source: Power NI

Analysis

4.3 Staff costs increased by £850k in FY13 following the insourcing of the BPO and billing team; this service was previously provided outsourced to Northgate.

4.4 We requested that Power NI provide an analysis of salary costs and FTEs by department. Their response is summarised below, for the period leading up to the base year, with staff numbers shown being the average number is each year.

FTEs - Permanent	Actual		LBE
	FY11	FY12	FY13
Call Centre	49.1	49.5	54.0
Billing	-	-	29.1
Business Development	19.8	15.8	16.0
Commercial/Trading	5.0	5.0	6.3
Communications	5.0	4.0	4.1
Customer Services	4.8	5.0	5.0
Debt	26.0	24.0	29.2
Energy Services	12.7	10.1	10.5
Finance	9.7	12.4	12.7
Marketing	5.0	4.0	5.5
Managing Director	1.0	1.0	1.0
Human Resources	2.0	2.0	1.0
Total	**140.1**	**132.7**	**174.2**

Source: Power NI

4.5 The above analysis differs from the initial FTE figures provided by Power NI in the BEQ submission to NIAUR. Power NI has indicated that the initial figures for FY11 and FY12 that were included in the BEQ were inaccurate.

4.6 The largest change in headcount in the historical analysis has arisen from the insourcing of the billing department in April 2013 from Northgate, which resulted in 29 FTE staff transferring to Power NI. This team previously delivered the same service as part of an outsourced service contract.

4.7 Other significant increases in the past year have resulted in 11.5 further FTE increases These have largely been made in the contact centre and debt teams, due to increased demands placed on these areas, as well as staff returning from the Enduring Solution project.

4.8 We requested that Power NI provide a commentary on the historical trends in staff numbers. Power NI's comments are below.

4.9 Power NI comments:

4.9.1 Contact Centres - The increase in FTEs between FY11 and FY13 reflects staff returning from the Enduring Solution project, together with the impact of longer call durations and the additional staffing requirements to meet exceptional call handling metrics in terms of % of calls answered and times to answer calls. A number of long-term agency staff were also made permanent, along with some natural attrition.

4.9.2 Billing - The department was insourced from Northgate on 1 April 2012

4.9.3 Business Development/IT Projects - The decrease in FTEs between FY11 & FY12 reflects the release of staff working on projects, in addition to the loss of core staff that have not yet been replaced.

4.9.4 Commercial/Trading - The increase in FTEs between FY12 & FY13 reflects additional business analysts, with one further staff member joining the team at the start of June 2013.

4.9.5 Debt - The fluctuations in FTEs between FY11 & FY13 reflects the mix of permanent and agency staff along with staff returning from the Enduring Solution project.

4.9.6 Energy Services - The decrease in FTEs between FY11 & FY12 reflects the loss of student placements who were not replaced and the transfer of staff between departments

4.9.7 Finance - The increase in FTEs between FY11 & FY13 resulted from the additional resources required as a result of tasks now being performed by PNI as a result of the *disposal of NIE. This would include tasks such as Accounts Payable and Financial Forecasting*

4.9.8 Marketing - The slight increase in FTEs between FY11 & FY13 reflects additional business customer staffing requirements in line with our increased focus on business customers

Source: Power NI

4.10 Power NI's forecast headcount levels are shown below. Staff numbers are shown as averages in each year.

FTEs - Permanent	LBE	Forecast		Projected
	FY13	FY14	FY15	Change
Call Centre	54.0	56.1	56.1	2.14
Billing	29.1	29.0	29.0	- 0.08
Business Development / IT Projects	16.0	19.0	19.0	3.00
Commercial/Trading	6.3	7.0	7.0	0.75
Communications	4.1	4.2	4.2	0.08
Customer Services	5.0	5.0	5.0	-
Debt	29.2	31.2	31.2	2.00
Energy Services	10.5	10.5	10.5	-
Finance	12.7	13.6	13.6	0.90
Marketing	5.5	5.0	5.0	- 0.50
Managing Director	1.0	1.0	1.0	-
Human Resources	1.0	-	-	- 1.0
Total	**174.2**	**181.6**	**181.6**	**7.3**

Source: Power NI

4.11 Power NI had 172.9 FTEs in March 2013 (excluding agency staff).

4.12 In addition to the recent increases in headcount, Power NI is projecting further increased staffing requirements of 7.32 FTEs (4.2% of the current workforce) between 2012/13 and 2014/15).

4.13 Power NI have provided the following explanation for projected increases in staffing levels from 2013 levels:

4.13.1 FTEs: Increase between FY13 & FY14/15 is driven by:

4.13.2 Additional call centre FTEs increase reflects additional staff making outbound calls to customers as part of a customer retention strategy given competition levels.

4.13.3 Business Development/IT Staff FTEs increase reflects additional staffing requirements for more frequent changes to our systems as a result of market-driven changes; to support the development of improved management information and reporting within the business; general product development as a result of customer demand; and financial regulation and compliance changes and the knock-on impact on changes to our systems to comply *(e.g. changes to the DD arrangements within SEPA) encompassing design, analysis, project management and governance.*

4.13.4 *Debt FTEs increase reflects additional staffing requirements to combat additional debt chase requirements as a result of the down turn in the economic environment, compounded by the level of bad debt as a proportion of sales increasing. This necessitates enhanced management of the cashflows in the business in an effort to maximise debt recovery.*

Source: Power NI

Costs per FTE

4.14 We have analysed costs per FTE as follows:

Breakdown of Salary Costs	LBE	Forecast	
	2012/13	2013/14	2014/15
	£k	£k	£k
Total	33.792	33.941	34.227

Source; BDO, derived from data prepared by Power NI

4.15 Our analysis shows average costs per FTE increasing by £435 in real terms (i.e. above inflation) over the forecast period from £33,792 to £34,227.

4.16 We requested that Power NI provide an explanation as to why above inflation increases to staff costs were justified. Power NI's explanations for the increasing costs per FTE are as follows:

4.16.1 *Staff costs: Movements between FYs in very high level terms is driven by:*

- *Pension current service charges as advised by the Group pension scheme actuaries, Spence & Partners (previously Hewitt),*
- *a relatively small number of staff salary increments based on previously agreed progressions,*
- *staff turnover based on the requirements of the business over certain periods, and*
- *the mix between contracted staff and agency staff, with the latter generally being a lower cost that the former.*

4.16.2 *More detail on the movement in average FTE cost by department is outlined below:*

4.16.3 *Pensions auto enrolment - With regards to auto enrolment for next year, for defined contribution staff, they will be auto enrolled for pensions at a min 4% rate employee rate which means we will have to match as a min that rate. Staff can chose after the event to* *opt out but to be prudent we assumed a min of 4% for all staff, i.e. for those not contributing or contribution less than 4%, we increased their contributions to 4%*

4.16.4 *Contact centres - Whilst staffing numbers are assumed to increase as noted below, the average salary shows a slight increase between FY13 and FY14 reflecting the pensions auto enrolment reflecting the fact that on average prior to auto enrolment defined contribution staff were contributing less than 4% into the pension scheme*

4.16.5 *Billing/exceptions - Whilst staff numbers are assumed to remain flat, the average salary is also assumed to remain flat and not being impacted by pensions auto enrolment reflecting the fact that on average prior to auto enrolment defined benefit contribution staff were contribution on average at least 4% into the pension scheme*

4.16.6 *Business development - Whilst staffing numbers are assumed to increase as noted below, the average salary shows a reduction between FY13 and FY14 reflecting the assumed retirement of a member of staff on a higher than average salary on a defined benefit pension scheme. As there is no requirement for staff to retire at any specific age, the reduction in average salary cost however is by no means certain.*

4.16.7 *Debt - the average salary shows a slight increase between FY13 and FY14 reflecting the pensions auto enrolment reflecting the fact that on average prior to auto enrolment defined contribution staff were contributing less than 4% into the pension scheme*

4.16.8 *Energy Services - the average salary shows an increase between FY13 & FY14 reflecting a senior staff member returning on a full time basis, this member of staff was not backfilled in FY13*

4.16.9 *Finance - Staffing numbers are assumed to increase between FY13 & FY14, with the average salary increasing reflecting the pensions auto enrolment reflecting the fact that on average prior to auto enrolment defined contribution staff were contributing less than 4% into the pension scheme and salary progressions for a number of staff*

Source: Power NI

Our Comments

4.17 Power NI increased its staffing levels in existing business areas between FY12 and FY13 by 12 staff, in addition to the insourcing of 29 staff from the Northgate billing contract.

4.18 Whilst Power NI has experienced recent increases in workload in some areas of its business which have resulted in recent staffing increases, particularly the call centre and debt teams, it is not clear whether these trends will continue into FY15, or whether these will potentially reduce as a result of improved customer communication and customer awareness of the development of a competitive market. In addition, those functions where staff numbers are forecast to increase by the largest number in FY14 and FY15, i.e. call centre, business development and debt also increased staff numbers in FY13 compared to FY12.

4.19 In the overall business context of falling customer numbers, Power NI has not identified any significant areas for reductions in numbers of staff directly employed over the forecast period.

4.20 Power NI is projecting significant reductions in agency staff costs. Power NI is proposing a reduction in agency staff of £370k in real terms between FY13 and FY15. These reductions are considered to be associated with the completion of the Enduring Solution project in the first quarter of FY13.

4.21 In relation to the staffing costs per FTE, we consider that Power NI's explanations are reasonable, and that the impact of defined benefit pensions costs together with the impact of auto-enrolment is likely to have an effect on Power NI's staffing costs which are additional to inflationary increases.

Conclusion

4.22 In relation to staffing requirements, we consider that we have been provided with insufficient evidence that Power NI will require an additional 7.32 FTEs between the base year and 2014/15, given declining customer numbers, the increase in staff numbers in FY12 and what appears to be a mature / stable business model.

4.23 We therefore propose that, in the absence of more robust evidence of the requirements for further staff increases, Power NI's operating cost allowance for staffing costs in FY15 should be £5.964m, representing an increase of 1.3% on the FY13 base year operating costs above the rate of inflation.

4.24 This proposed allowance represents a reduction of £251k from the staff costs figure included in Power NI's BEQ. This figure represents 7.32 FTE multiplied by Power NI's forecast FY15 average cost per FTE of £34,227, in 2012/13 prices.

4.25 Subsequent to the Workshop with Power NI and its advisers on 29 May 2013, Power NI provided further information and explanations in relation to the proposed staffing levels in FY15. We have reviewed the information provided prior to confirming the above findings.

5 MBIS

5.1 In this section we have reviewed the MBIS costs in the Power NI BEQ.

Information Provided by Power NI

5.2 The BEQ information on historic and forecast MBIS costs provided by Power NI is summarised below:

MBIS Costs - 2012/13 prices	Actual			LBE	Forecast	
	2009/10	2010/11	2011/12	2012/13	2013/14	2014/15
	£m	£m	£m	£m	£m	£m
Breakdown of costs						
Advice Centres	0.080	0.070	0.068	0.030	0.015	0.015
Consultancy, Audit & Legal	0.566	0.634	0.800	0.462	0.535	0.535
Agency Staff	0.331	0.493	0.534	0.572	0.262	0.201
Electricity Association	0.033	0.030	0.030	0.000	0.000	0.000
Insurance	0.041	-0.007	0.049	0.025	0.051	0.051
Light, Heat & Power	0.024	0.028	0.042	0.041	0.045	0.045
Marketing & Advertising	0.241	0.353	1.193	0.561	0.757	0.658
Journals & Subscriptions	0.050	0.080	0.070	0.071	0.108	0.108
Other Debt Management	0.099	0.133	0.174	0.180	0.182	0.182
Other Printing & Stationery	0.048	0.044	0.088	0.115	0.136	0.136
Pension scheme administration	0.000	0.000	0.204	0.382	0.228	0.228
Price Control Targets - Energy Efficiency etc	0.341	0.161	0.114	0.170	0.172	0.172
SAP Development	0.028	0.020	0.020	0.026	0.027	0.026
Goodwill payments	0.017	0.096	0.014	0.045	0.045	0.045
Rent & Rates	0.179	0.116	0.304	0.315	0.318	0.318
Telecomms	0.589	0.121	0.137	0.147	0.160	0.160
Training & Teambuilding	0.104	0.151	0.149	0.086	0.126	0.126
Transport & Travel	0.078	0.075	0.079	0.053	0.062	0.062
Cleaning	0.017	0.023	0.029	0.044	0.044	0.044
Office maintenance	0.007	0.033	0.026	0.045	0.049	0.049
Catering	0.013	0.010	0.012	0.015	0.015	0.015
Brokers fees	0.000	0.000	0.000	0.010	0.050	0.050
Childcare	0.003	0.003	0.002	0.006	0.005	0.005
Charitable donations	0.001	0.005	0.002	0.007	0.011	0.011
Other (please specify)	0.046	0.027	0.040	0.003	0.003	0.003
MBIS Total	**2.934**	**2.700**	**4.181**	**3.409**	**3.403**	**3.243**

Source: Power NI

5.3 MBIS costs increased significantly from £2.7m in FY11 to £4.181m in FY12. The FY12 expenditure included significant one-off costs, largely as a result of marketing and advertising costs arising from the rebranding of NIE Supply as Power NI following the disposal of NIE T&D by the Viridian Group, together with costs of insourcing relating to the Antrim contact centre.

5.4 MBIS costs in FY13 show around a £770k reduction from FY12 levels. MBIS costs are forecast to further reduce by £166,000 per annum (4.9%) in real terms between FY13 and FY15.

5.5 Actual costs for FY13 exceeded LBE by £135k. Power NI's explanation for this was that consultancy and legal costs in the year exceeded forecast. Power NI has not indicated that this should result in any change to the FY15 forecast expenditure.

Analysis

5.6 We conducted a 'top down' analysis of the BEQ information, consistent with our overall approach to the review of Power NI's operating expenditure.

5.7 Our analysis of these costs is set out below and focuses on the areas of significant movement in expenditure, and/or significant spend.

5.8 The areas highlighted for further analysis are summarised below. The remaining cost categories which did not show substantial changes are aggregated and shown as "Other cost categories".

MBIS Costs - 2012/13 prices	LBE 2012/13	Forecast 2014/15	Change	Change
	£m	£m	£m	%
Breakdown of costs				
Consultancy, Audit & Legal	0.462	0.535	0.073	16%
Agency Staff	0.572	0.201	(0.370)	-65%
Insurance	0.025	0.051	0.025	100%
Marketing & Advertising	0.561	0.658	0.096	17%
Journals & Subscriptions	0.071	0.108	0.037	52%
Other Printing & Stationery	0.115	0.136	0.021	18%
Pension scheme administration	0.382	0.228	(0.154)	-40%
Training & Teambuilding	0.086	0.126	0.039	45%
Brokers fees	0.010	0.050	0.040	395%
Other cost categories	1.125	1.152	0.027	2%
MBIS Total	**3.409**	**3.243**	**(0.166)**	**-5%**

Source: BDO

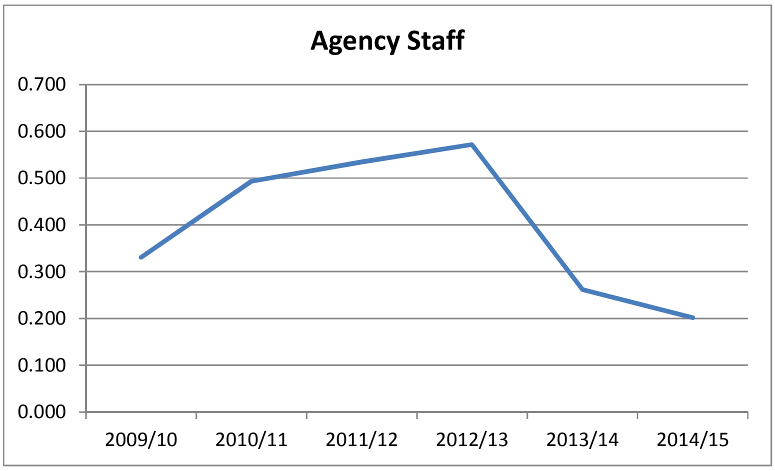
Consultancy and legal costs

5.9 Consultancy and legal costs saw a significant increase in FY12, relating to the insourcing of the BPO and billing team from Northgate. FY13 and future periods are more in line with the historic average level of costs in this area, as shown in the diagram below:

Source: BDO

Agency staff costs

5.10 The overall trend is agency staff costs is shown in the diagram below.

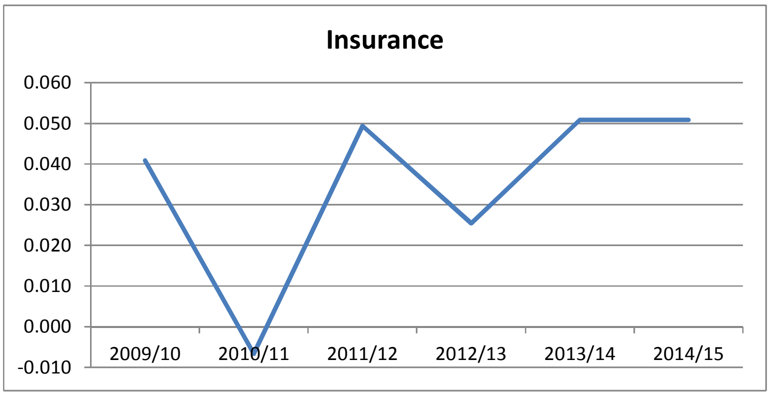


Source: BDO

5.11 Power NI have explained that increased agency staff costs in FY13 reflected the additional staffing requirement associated with the implementation of the Enduring Solution Project, in particular during a three month training period from March to May 2012. Power NI have advised that agency staff costs in the forecast periods largely reflect contact centre and debt team non-permanent staff. Power NI has stated an intention to use permanent staff where possible and to minimise the use of agency staff in the business in future.

Insurance

5.12 The trend in insurance costs levels between FY10 and FY15 is shown below.

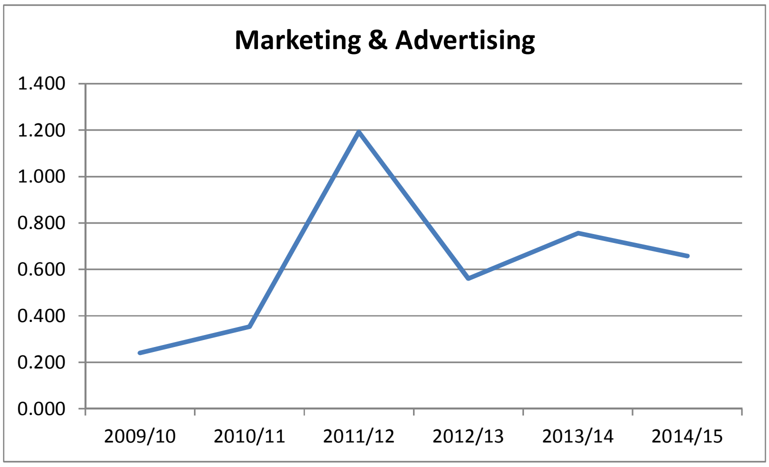


Source: BDO

5.13 Insurance costs have fluctuated in recent years. Power NI noted that prepayment / accruals adjustments have meant that the costs in individual years between 2009/10 and 2011/12 were not completely accurate. Power NI have forecast costs in FY14 and FY15 at £50k per annum.

Marketing and Advertising, other stationery and printing

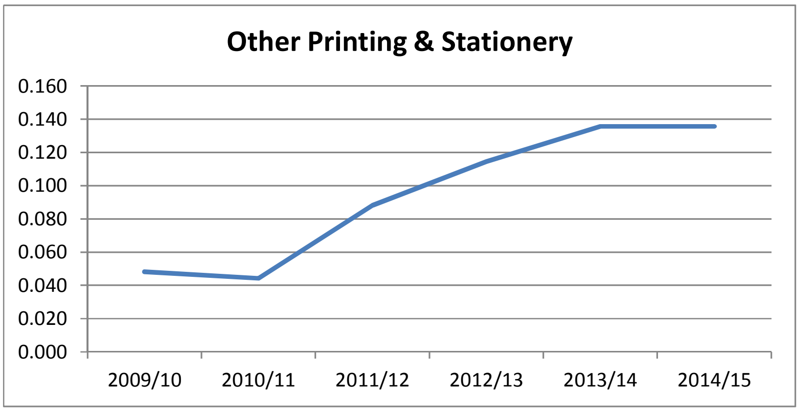
5.14 Marketing and advertising costs reflect the cost of customer communications, which Power NI states are focussed on customer awareness, rather than customer acquisition. The overall trend in marketing and advertising costs is shown below.



5.15 Marketing and advertising costs in FY12 saw a large increase relating to the rebranding of NIE Supply as Power NI.

5.16 Marketing is projected to increase by 17.2% between FY13 and FY15. Power NI have stated that customer engagement costs were reduced during the period of implementation of Enduring Solution and that further competition in the sector will place increased demands on customer communications.

5.17 Other printing and statements costs are related to the marketing and advertising costs, and are associated with mailouts etc. These costs are projected to increase by £21k between FY13 and FY15.

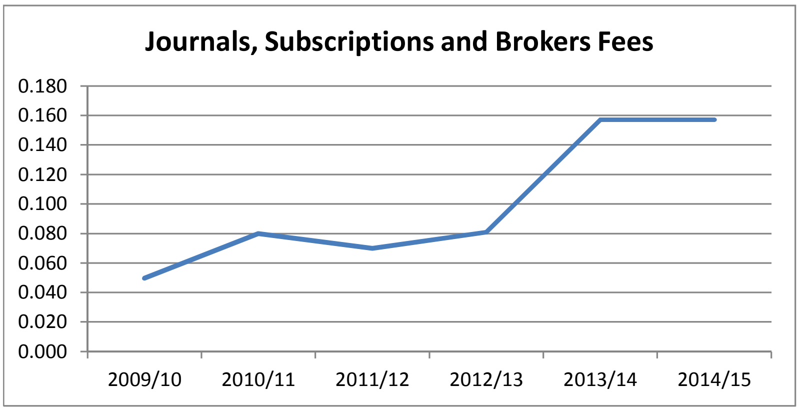


Source: BDO

5.18 We consider that we have been presented with insufficient evidence to justify and increase in Marketing and Other Printing & Stationery costs from FY13 levels. We further note that FY13 levels are above-trend in both of these cost categories, adjusting for the impact of the FY12 rebranding exercise on marketing costs. Restricting these costs to FY13 levels would result in a £120,000 reduction in opex.

Journals and Subscriptions, Brokers Fees

5.19 Journals and subscriptions are forecast to increase by £37k per annum between FY13 and FY15. In addition, Broker's Fees are projected to increase by £40k per annum. These projected increases relate to an assumption by Power NI that trading on the interconnector will commence in FY14 and drive increased costs in these areas.

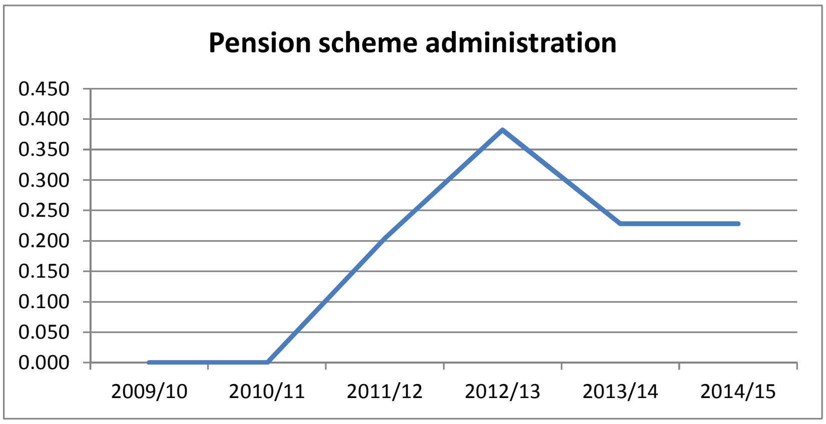


Source: BDO

5.20 Power NI has accepted that the disallowance of broking costs is reasonable, however they have argued for the retention of the Journals increase on the basis that trading on the interconnector will reduce their wholesale energy costs, resulting in savings to the consumer.

Pension Scheme Administration

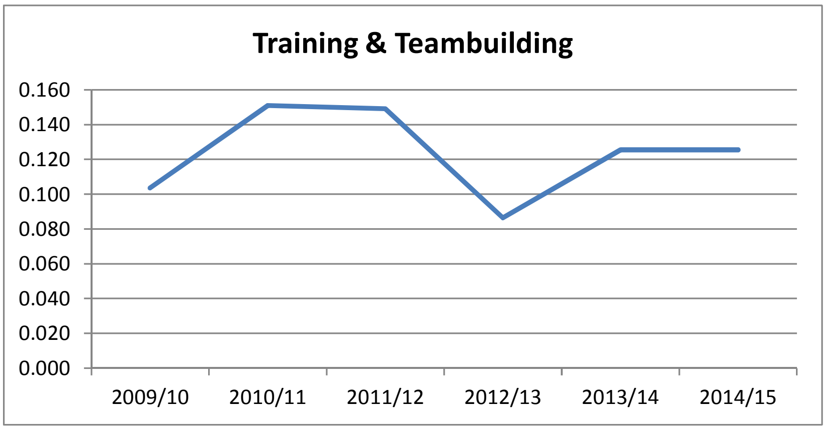
5.21 Pension scheme administration costs are charges associated with the administration of the Viridian Group pension scheme and are not within Power NI's direct control. These are notified to Power NI by the group and were first charged to the company in FY12. The costs are forecast to fall by £154k between FY13 and FY15. These costs were higher in FY13 than in FY12 or future years due to the impact of the group's triennial scheme valuation costs. The triennial scheme valuation will be repeated in FY16. These costs relate to the administration of the scheme and do not include deficit related scheme contributions.



Source: BDO

Training and Teambuilding

5.22 Training and teambuilding costs were suppressed in FY13 compared to previous periods, and are projected consistently with costs incurred in FY10 through FY12.



Source: BDO

Conclusion

5.23 Based on our 'top down' review of Power NI's MBIS costs, in our view the overall allowance for MBIS costs should be reduced by £160,000 from the levels shown in the Power NI BEQ submission. This represents reductions in the following areas:

MBIS Proposed reductions	**£m**
FY15 Power NI BEQ Total	3.243
Proposed reductions:	
Other Printing & Stationery	0.020
Marketing	0.100
Journals / Broking fees	0.040
Total Proposed reductions	0.160
Adjusted MBIS FY15	3.083

Source: BDO

5.24 We note that our findings take into account further information provided by Power NI in response to our drafting findings.

6 Bad debt

6.1 In this section we have reviewed the Bad debt costs included in the Power NI BEQ submission.

Information provided by Power NI

6.2 Power NI has projected bad debt levels based on percentages of overall turnover. Power NI accepts that it is difficult to project bad debt levels with accuracy due to the impact of external factors such as the economic environment on the level of bad debt within its business.

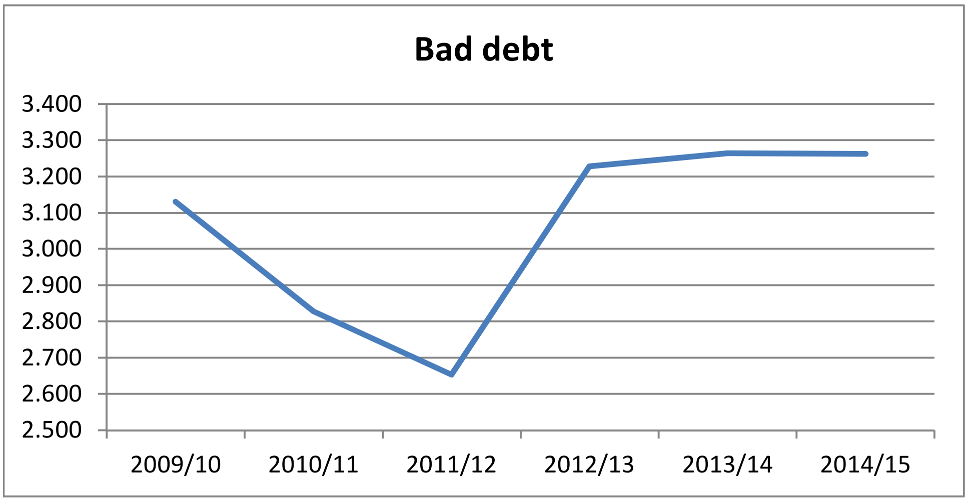
Analysis

6.3 NIE's forecast bad debt levels are based on the following assumptions:

Analysis of Bad Debt	Actuals			LBE	Forecast	
	2009/10	2010/11	2011/12	2012/13	2013/14	2014/15
	£m	£m	£m	£m	£m	£m
Turnover	678.548	586.684	537.477	488.913	459.113	440.712
Bad Debt	3.131	2.828	2.653	3.228	3.265	3.263
Bad Debt Percentage	0.46%	0.48%	0.49%	0.66%	0.71%	0.74%

6.4 Source: BDO, Derived from Power NI BEQ

6.5 An historical analysis of Power NI's bad debt charges show a substantial increase in bad debt levels of £576,000 in FY13, (21.7%) compared with FY12. It is clear that the bad debt charge has shown a significant degree of variability in recent years.



Source: BDO

6.6 Bad debts levels have fluctuated significantly over the period between around £2.6m and around £3.2m. Bad debt levels have historically been low within Power NI's business: bad debt as a proportion of turnover was below 0.4% in FY2008 and FY2009, and below 0.5% in FY 2010.

6.7 Forecast levels of bad debt in FY14 and FY15 represent peaks of bad debt cost over the review period covering 2009/10 to 2014/15.

6.8 Restrictions on customer switching act to prevent customers with debt from switching to Power NI's competitors. This has resulted in Power NI being left with an increasing proportion of its overall customers who are in arrears.

6.9 Power NI has argued that the business is experiencing increasing levels of bad debt as a result of the ongoing economic difficulties being experienced by business and domestic customers in Northern Ireland, and that competition has led to cherry-picking of debt free customers by its rivals.

6.10 While we do not disagree with the information provided by Power NI, we note that it relates to macro-environmental trends which Power NI has not attempted to relate to recent trends and fluctuations in its bad debt charges, or to its specific forecast levels of bad debt.

6.11 Power NI has also identified that NIE's introduction in May 2012 of more stringent RPU practices has resulted in increased debt risks to Power NI. We have not requested nor were we provided with data to support this claim. Power NI has also pointed to the impact of recent tariff increases on projected bad debt levels.

Conclusion

6.12 We consider that it is reasonable to assume that the cost of bad debt as a percentage of overall turnover will rise as more regulated customers switch to other providers. However insufficient evidence has been provided by Power NI to justify an increase to the overall cost of bad debt from the 2012/13 levels which represent the peak cost over the period 2009 – 2013 and an increase of £576,000 from 2011/12 levels.

6.13 We therefore recommend that the allowance for bad debt be restricted to £2.96m in 2012/13 prices, representing the average historical actual bad debt costs incurred from FY2010 to FY2013, during a period when Power NI had significantly more customers than projected for FY15.

6.14 This represents reduction of £303k from the level in the Power NI BEQ. The adjusted allowance equates to 0.672% of turnover in FY15, which is higher than the bad debt to turnover ratio in any year from 2009 to 2013.

6.15 We note that the level of operating costs for bad debt in the BEQ is based on both regulated and unregulated customers. In recent price controls, Power NI has only received a specific operating costs allowance for forecast bad debts to regulated customers.

6.16 An allowance of £2.96m for Power NI would correspond to £2.53m for the regulated business, assuming a regulatory threshold of 50MWh. This is based on regulated turnover for 2014-15 of £376.15m in 2012/13 prices.

7 Agent costs

7.1 In this section we have reviewed the Agent Costs element of the Power NI BEQ submission.

Information provided by Power NI

7.2 Power NI's historic and forecast agent costs are shown below.

	Actual			LBE	Forecast	
	2009/10	2010/11	2011/12	2012/13	2013/14	2014/15
	£m	£m	£m	£m	£m	£m
Bank charges	0.409	0.457	0.118	0.254	0.261	0.261
Postage	0.923	0.818	0.823	0.902	0.720	0.701
Transaction Charges	2.925	2.866	3.240	2.857	2.837	2.723
	4.256	**4.142**	**4.181**	**4.013**	**3.818**	**3.686**

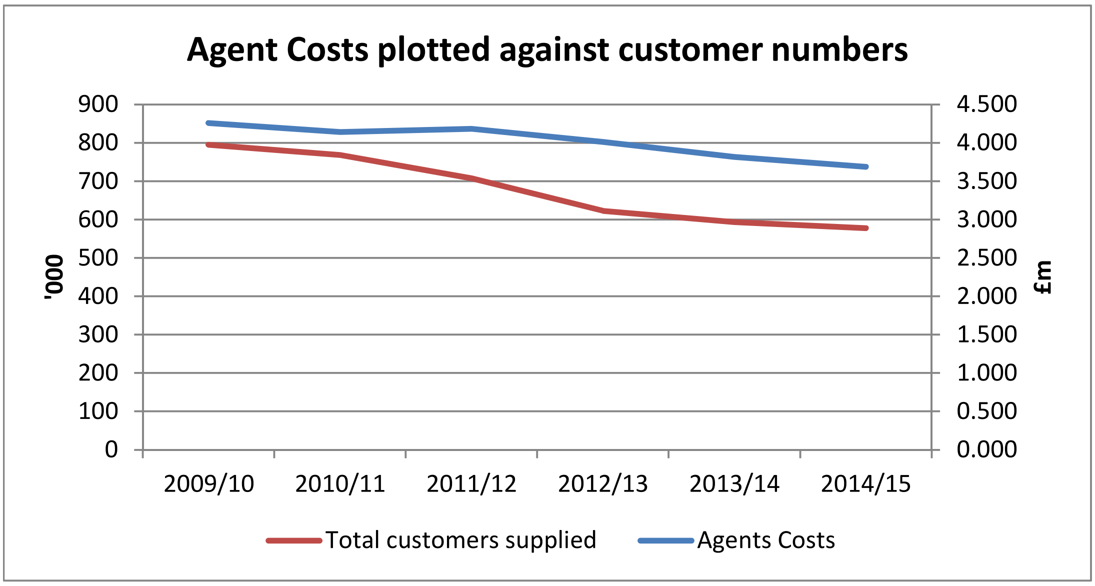
Source: Power NI BEQ

Agent costs are projected to fall by £327k per annum in real terms between FY13 and FY15. The reduction is due to the assumed reduction in customer numbers within Power NI's business over the period.

We requested that Power NI provided us with a bottom up analysis to support its forecast costs in this area.

Analysis

7.3 Agent costs are substantially driven by customer payments and customer interactions, and should therefore be expected to fall in line with overall customer numbers. However, increased take up of bill payments using payment cards, online payments and telephone payments has meant that historical costs in this area have not fallen as quickly as overall customer numbers.

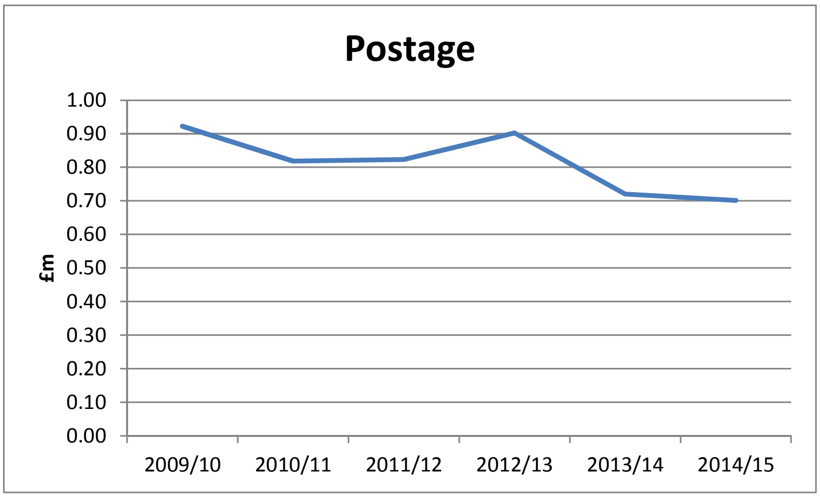


Source: BDO

7.4 Agent costs may be grouped into 3 areas for the purposes of analysis – postage costs, bank charges and transaction charges. Transaction costs include over the counter, card payment, and telephone payment costs.

Postage

7.5 The trend in postage charges between FY10 to FY15 is shown below:



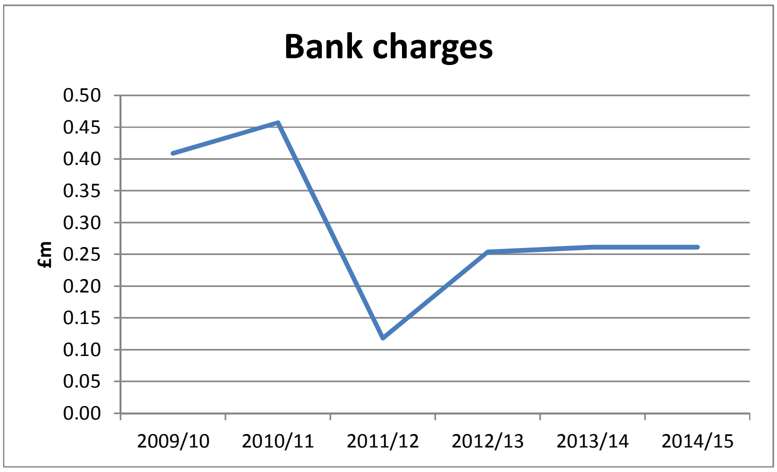
Source: BDO

7.6 Power NI explained that the increase in costs in FY13 was the result of lower discounts following a change in the company's contract with Royal Mail. Power NI changed supplier from Royal Mail to TNT mid-way through FY13. Projected reductions in costs in FY14 and FY15 relate to reductions in customer numbers and mail volumes plus the full year effect of the switch to TNT.

7.7 Power NI also pointed to the impact of legislative changes in increasing the volume of customer communications in recent years, despite reducing customer numbers.

Bank charges

7.8 The trend in bank charges is shown below:



Source: BDO

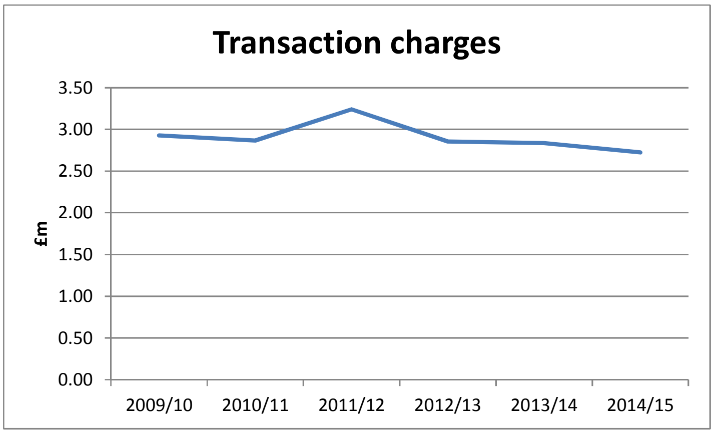
7.9 Power NI explained the increases in bank charges since FY12 as being associated with a new contract entered into with Bank of Ireland.

7.10 Power NI have informed us that FY10 and FY11 costs are distorted by the inclusion of some transaction charges relating to card payments within the Bank Charges category.

7.11 Bank charges are forecast to remain increase marginally over the forecast period.

Transaction charges

7.12 The trend in transaction charges is shown below:



Source: BDO

7.13 Transaction costs increased between FY10 and FY12 despite falling customer numbers.

7.14 We have reviewed Power NI's bottom up forecast for consistency with Power NI's customer number projections. The projected agent costs are in line with Power NI's customer forecast customer numbers.

Conclusion

7.15 Based on our analysis we have not proposed any reduction in Power NI's forecast agent costs.

8 Corporate charges

8.1 In this section we have reviewed the Corporate charges in the Power NI BEQ submission.

Information provided by Power NI

	Actual		LBE	Forecast	
	2010/11	2011/12	2012/13	2013/14	2014/15
	£m	£m	£m	£m	£m
Breakdown of Corporate Charges					
Call Centre Rental	0.044	0.000	0.000	0.000	0.000
Overheads recharge	0.067	0.000	0.000	0.000	0.000
Depreciation recharge	0.035	0.000	0.000	0.000	0.000
Overheads recharge	1.054	1.322	1.281	1.409	1.437
Depreciation recharge	0.002	0.002	0.002	0.025	0.047
Total	**1.202**	**1.325**	**1.283**	**1.434**	**1.484**

Source: Power NI

Analysis

8.2 Power NI has forecast a 15.7% real terms increase in group charges between FY13 and FY15.

8.3 Corporate charges are generally allocated to Power NI based on the company's share of group revenues, with HR costs allocated based on headcount. The projected share of group charges is 33.6% in FY15. We would highlight that the information presented to NIAUR in the BEQ is inaccurate in this respect, as a figure of 28.3% was initially provided.

8.4 Power NI has advised that it has no control over the level of charges which are levied by the Viridian Group, which cover a range of activities delivered by the Viridian Group such as group finance, risk management, insurance, treasury, legal IT and SAP.

8.5 Power NI's Group charge costs have risen since Viridian's disposal of NIE T&D to ESB, as Power NI now represents a larger proportion of the overall Viridian groups revenues and therefore attracts a higher proportion of group charges.

8.6 Power NI has provided the following commentary on the projected increases in Viridian Group charges:

8.6.1 Corporate charges have historically been incurred as a function of activities carried out on behalf of Power NI at a Viridian Group level. As with all group owned businesses certain activities will be conducted on their behalf bringing to bear some economies of scale and general oversight. As of 01 October 2012 all Group Technology and HR staff have been absorbed into the Viridian Group Corporate function. As a result, Corporate *charges are forecast to increase (compared to March 2011) with cost reductions in reflected IT and HR staff within Power NI.*

8.6.2 *The total corporate cost budget for 2013/14 is £4,420k of which Power NI assumes £1,436k - 32%. In terms of metrics for Power NI relative to the rest of the Group, Power NI represents:*

- *22% of budget Viridian Group operating profit for 2013/14;*
- *43% of staff headcount at 31 December 2012; and*
- *30% of budget Viridian Group turnover for 2013/14.*

8.6.3 *The breakdown of Power NI's share of Viridian Group corporate costs for 2013/14 is as follows [BDO note - this shows the movement in overheads recharged from 2011/12 in nominal prices inflated by RPI for 2012/13 and 2013/14, compared to the forecast costs for 2013/14 in nominal prices. The figures shown below do not reconcile to the Table at 8.1, which is stated in 2012/13 prices]:*

Corporate Cost Breakdown	2011/12 £'000	Inflated 12/13 - 3.2% £'000	Inflated 13/14 - 3% £'000	2013/14 £'000	Variance £'000
Group Board & Chief Executive	334	344	355	404	-49
Group Finance, Risk Mgt & Insurance	256	264	272	234	38
Group Technology	204	211	217	277	-61
Treasury & Accounts payable	196	202	208	94	114
Company Services & Legal	114	118	122	93	28
HR & Payroll	60	62	64	202	-139
Taxation	50	52	53	42	11
Premises	39	40	41	48	-7
SAP	29	30	31	41	-11
Total	**1,281**	**1,322**	**1,362**	**1,436**	**-74**

Source: Power NI

8.7 We requested that Power NI provide specific information on the analysis of the FY15 corporate charges, which are forecast to increase from the FY14 levels. Power NI provided the following follow up response:

8.8 *The paper outlined the basis of our intercompany costs for 2013/14. The only difference (after removing RPI) in 14/15 is that there is an additional c. £22k in depreciation relating to a full year's depreciation of a SAP upgrade which is to happen later this year, plus a £26k increase in corporate overheads. Although the total values of the overhead in the BEQ are correct, the figure of 28.3% quoted out to the side in the BEQ is erroneous. The percentage allocated to Power NI for 13/14 is 32%. The percentage allocation for*

14/15 is largely unchanged at 32.5%[1]. The corporate recharge is primarily based on a general allocation basis, with all costs incurred by Viridian Corporate being allocated based on share of turnover with the exception of Human Resources costs which are allocated on a headcount basis.

Source: Power NI

8.9 We also requested that Power NI provide an analysis of the gross corporate charge over the period of the BEQ, as shown below:

Corporate Charges	Actual			LBE	Forecast	
	2009/10	2010/11	2011/12	2012/13	2013/14	2014/15
	£m	£m	£m	£m	£m	£m
Gross Corporate Charges (2012/13 prices)	6.859	5.695	4.124	4.000	4.335	4.421
Power NI share (2012/13 prices)	1.229	1.202	1.325	1.283	1.434	1.484
Power NI share (proportion of Gross charge)	17.9%	21.1%	32.1%	32.1%	33.1%	33.6%

Source: BDO, Derived from information provided by Power NI

8.10 The gross charges show a large reduction in FY12, resulting from the disposal of NIE T&D by the Viridian Group. Power NI's share of the corporate charges has increased by £64,000 between FY10 and FY13, during a period when the gross corporate charges have reduced by £2.859m. This reflects the reduction in size of the overall group following the disposal of NIE T&D.

8.11 Power NI's share of corporate charges is forecast to increase by £200,000 between FY13 and FY15. Of this increase £135,000 is due to increases in the gross corporate charges, with the remaining £65,000 attributable to a proposed increased share being borne by Power NI.

8.12 Power NI has attributed the proposed increase in gross corporate charges as arising from additional activities undertaken at group level, including:

(i) Upgrade of SAP;

(ii) Implementation of Cognos required due to increased financial reporting complexity;

(iii) Unavoidable IT refresh;

(iv) Greater focus on IT security;

(v) Telephony support project; and

(vi) HR support moving from subsidiary to group level.

[1] This appears to be 33.6% i.e. £1.484m charge as a proportion of £4.421m

8.13 The projected movements in Power NI FTEs set out in section 4 show a reduction in HR staff of 2 over the period 2011/12 to 2014/15 as a result of staff transferring to Group. We therefore accept that an increase in group HR costs is justified. However, the level of projected increase appears high, particularly as Power NI would only bear a proportion of the cost.

Conclusion

8.14 The forecast corporate charges include proposed increases both in the overall level of charges and in Power NI's share of the overall costs.

8.15 In the context of a falling customer base and turnover, we do not see a justification for Power NI taking an increased share of group charges. Similarly, other than the increase attributable to the shift of HR from Power NI to Group we do not consider that the increase in underlying corporate costs over and above RPI is justifiable.

8.16 We therefore recommend that £133,000 (being the whole of the increase associated with the increase in allocation plus 50% of the increase in underlying costs) should be disallowed.