



EA Response to Utility Regulator Information Paper on Electricity Prices in Northern Ireland

Electricity Association of Ireland
Energy and Environment Policy Committee



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The Electricity Association of Ireland (EAI) is the trade association for the electricity industry on the island of Ireland, including generation, supply and distribution system operators. It is the local member of Eurelectric, the sector association representing the electricity industry at European level.

EAI aims to contribute to the development of a sustainable and competitive electricity market on the island of Ireland. We believe this will be achieved through cost-reflective pricing and a stable investment environment within a framework of best-practice regulatory governance.



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Introduction and Summary

The EAI notes the publication of this information paper on Electricity Prices in Northern Ireland by the Utility Regulator in support of transparency within the Single Electricity Market (SEM).

The objective of the information paper is to provide data to enable comparison of retail prices in NI with the UK, ROI and other member states within the EU. EAI supports this objective. Reliable data on electricity pricing improves transparency and enables an informed debate on issues of regulation and energy policy.

Within the paper, the regulator highlights further work that remains to be done to aid this comparison. At the same time, the paper makes certain statements and conclusions that EAI believes should have awaited completion of this work and that are not fully substantiated by the data presented in the paper. This is regrettable. In order to ensure that the paper would not work against its own objective of transparency, EAI wish to make some clarifying points.

About Electricity Prices

The Wholesale Market

The Single Electricity Market (SEM) is the wholesale market in the island of Ireland. Suppliers buy electricity in the SEM in order to supply their customers. Effectively a single price for the entire market is set for each half hour, according to rules which are approved by the two regulators, including NIAUR. Data shows that the prices in SEM closely follow the cost trend of international fuel prices, primarily gas, given its dominance in the fuel mix. (Note that, since most gas used on the island of Ireland must be transported from Great Britain, the gas price will always be somewhat higher than the GB price.) The Market Monitoring Unit established by the regulators has consistently reported in its analysis that **SEM prices are cost-reflective.**

This is because, in bidding into this market, generators on the island are required by licence to follow strict rules. Generators are required to bid based on their short run marginal cost of production. This means that energy, the greater component of the price of electricity, is determined by input prices.

In GB, studies indicate that wholesale prices are set below the long-run marginal cost of production, ultimately leading to a significant shortfall in generation capacity compared to that needed, as identified in Project Discovery¹. Issues such as this must be factored into a comparison of prices.

Market Redesign

As explained above, the Single Electricity Market has worked well and is accepted as being cost-reflective. Wholesale markets around Europe are being amended in order to facilitate an integrated electricity market. The regulatory authorities have established a project to decide on the necessary changes to SEM and to implement them. The pending redesign of the wholesale market may change the mechanism by which prices are formed on the island. It is crucial that the right design is delivered vis a vis our European neighbours if industry on the island is to remain competitive. We would suggest that any future initiative on prices in Northern Ireland and any comparison with our European neighbours is presented in the context of the ongoing integration of SEM and the wholesale markets of Great Britain and the rest of Europe.

Network Charges and Public Service Obligation

The remaining components of the retail price of electricity consist of charges for using the networks, the public service obligation (PSO) set by regulators according to government policy and suppliers' own costs. The level of networks and PSO charges and their

¹ “Our findings suggest that the British wholesale market might be underpricing electricity. With substantial excess generating capacity over the last decade, the market has seen firms “sweating their assets” so that the price has fallen below LRMC. Unless the wholesale price increases to at least LRMC in the near future, the GB market could have difficulties securing replacement investment for the generating capacity to be retired over the coming decade”(Helm, 2009 and CER, 2009, ESRI 2013 p.10))

distribution across the market is a matter of regulation and government policy and varies widely across the EU.

Due to differences between policy objectives, markets and regulatory structures across Europe, such a comparison is by no means straightforward. Regrettably, this information paper presents a crude comparison and makes no attempt to account for these country-specific factors. As a result, the inferences made in the paper could, we believe, seriously mislead and, for that reason are, ill advised. We propose that the paper would benefit from revision based on a more detailed analysis of the factors influencing price development across member states.

The most appropriate comparison to make is with RoI, with whom Northern Ireland shares a common wholesale market and a number of other similarities in terms of government and regulatory policy. We argue strongly that the differential in electricity prices between ROI and NI can be explained with reference to the allocation of network charges between small to medium and large users and related government policy.

Comments on the Information Paper

Against this background, we have a number of comments on the Information paper:

Methodology

- The paper presents insufficient evidence in order to draw any inferences or conclusions. Comparison with other countries without a disaggregation of LEU Prices or any allusion to wide-ranging and highly significant country-specific idiosyncrasies mitigates against a like-for-like comparison despite the paper's best intentions². In Germany for example, LEUs have an exemption from costs associated with the Energiewende (Energy Transition to renewable energy) which account for half the domestic consumers' bill.

² Throughout the process, we also had to ensure we were always comparing like with like and therefore had to ensure our methodology was consistent with DECC”(p.13)

Comparison with the Republic of Ireland (ROI)

- A comparison with the Republic of Ireland offers the best prospect for a like for like comparison. Indeed such a comparison can offer important insights into the true driver of price differentials.

- A number of important aspects of the markets, system and government policy are common across the two jurisdictions
 - NI & ROI share a common wholesale market (i.e. the SEM). Prices are cost reflective and there is no wholesale price differential between the two. The SEM design has been openly and strongly endorsed by the regulatory authorities from the respective jurisdictions who were closely involved in its development. Both regulators are represented on the SEM Committee which oversees the overall functioning of the market, market power mitigation strategy and governance arrangements in the SEM. The SEM is unusual, if not unique, in terms of the constraints it imposes upon generators. The key parameters of a mandatory Pool and binding Code of Practice for Bidding, capacity payment mechanism design and operation and payment for other services, are wholly determined by the RAs..

 - Both jurisdictions, geographically peripheral to Europe, are at the wrong end of the supply line, but both have a valuable natural resource in wind. In relation to renewables, the policy of both Governments is the same i.e. 40% RES by 2020 and the RES generation mix across the two is comparable.

 - NI & ROI share a common connection charging policy (i.e. shallow connection policy which is a feature of the SEM High Level Design, this is referenced in the paper as a driver of NI prices)

 - Population density and economies of scale are comparable, although LEU customers in ROI are larger and have flatter loads

- In light of shared competitive forces, market liquidity and wholesale prices, we can see no reason why retail companies operating in both markets would price differentiate between the two.

The differential in electricity prices between ROI and NI can in large part be explained with reference to the allocation of regulated network charges between small to medium and large users and related government policy.

It is important to appreciate that any differences are not due to the wholesale or retail market in electricity or government policy towards renewables, which is broadly similar in both jurisdictions.

- We note that other Members States have rebalanced tariffs to favour industrial consumers in the interests of competitiveness.
 - In 2009, the CER re-balanced UoS charges in ROI to reflect the government decision to rebalance network tariffs in favour of Large Energy Users (LEUs)³. As a result, per annum savings of €50m attributed to large energy users funded by a rebalancing of domestic tariffs (CER/10/102 & CER/10/206)

Conclusion

- In conclusion, whilst EAI welcomes increased transparency, the value of this information paper is questionable given the significant potential for misinterpretation as outlined above
- The price of electricity on the island of Ireland is largely determined by fuel prices as a result of cost-reflective production in the wholesale market
- There is vigorous competition in the retail market containing suppliers' margins
- Variation in costs for specific categories of customers reflect regulatory decisions and government policy.
- Informed debate on energy and energy prices is an important aim
- It is clear that the regulator has put significant work into research. The present report requires more work for it to fulfil its aims.

³ <http://debates.oireachtas.ie/dail/2009/10/13/00055.asp>

