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15 July 2011

NIE Energy Supply Price Control 2011-2013 – Proposals for Consultation

Dear Nicola,

Viridian Power and Energy (VPE) welcomes the opportunity to comment on the above consultation. Without more detailed information or analysis we necessarily restrict our comments in this response to important points of principle and general observations based on the very limited information provided in the consultation paper. VPE is a strong advocate of best regulatory practice as recently re-iterated and reflected in the 3rd Directive and the Department for Business Innovation and Skills Principles for Economic Regulation[1] and we respond to this consultation in that spirit with the following key observations:

1. The retrospective application of the price control as proposed and its short duration of only two years (part of which is applied retrospectively) does not appear to provide a stable and predictable regulatory framework for the institution being regulated, its (potential) competitors, and consumers.

2. On numerous occasions throughout the consultation paper it is stated that the Utility Regulator "believes" there are reasons to support its views or arguments (reference pages 5, 6, 7, 8, 10, 15, 16 and 17) but there is often little or no evidence provided in the consultation paper to support and substantiate these beliefs. This would appear contrary to the principle that regulatory decisions should be fully reasoned and

[1] The 3rd Directive is available online @ http://ec.europa.eu/energy/gas_electricity/legislation/legislation_en.htm Principles for Economic Regulation is available online @ http://www.bis.gov.uk/assets/biscore/better-regulation/docs/p/11-795-principles-for-economic-regulation.pdf

justified based on robust evidence and we would suggest this is damaging to investor and market confidence as a whole.

3. Page 11 of the consultation paper proposes to disallow an increase in corporate charges and justifies this as follows: ‘We [the Utility Regulator] believe that corporate charges have increased as a result of the divestment of NIE plc, and as such should be borne by the shareholder’. We do not consider the divestment of NIE plc as relevant in this context. The entity subject to price control is NIE Energy Supply and its parent company activities should be considered out of scope for the purposes of determining whether corporate charges have been efficiently incurred. The only relevant question in our view is whether the services in question could be more efficiently procured in the current environment, either from the parent company or elsewhere – not in the context of a corporate structure which no longer exists.

4. Page 17 of the consultation paper discounts the possibility of disallowing power procurement costs retrospectively after the hedging policy statement has been approved and providing the economic purchasing obligation is adhered to. If the Utility Regulator was to be inconsistent in this regard, it is stated, ‘then the licensee has recourse to appeal’. Although we understand there are provisions for an appeals mechanism in the 3rd Directive we were not aware that licensees in Northern Ireland or the SEM yet have recourse to appeal against regulatory decisions and would request more clarity on this and the process of appeal.

5. There are a number of ambiguities and inconsistencies in the consultation paper which create confusion. For example the GB experience of high switching rates is referred to on page 6 as an indicator of higher switching rates in Northern Ireland going forward but yet the GB experience is discounted on page 15 of the consultation paper in the context of NIEES being arguably less exposed to market risks because of customer stickiness ‘which to date appears higher in NI than in the rest of GB [and] …is likely to remain so over the price control period’. It is not clear why the GB experience is a relevant comparator in one context (switching rates going forward) but not relevant in a very similar and related context (customer stickiness) and we would suggest further explanation is required.

6. It is not clear from the consultation paper how and to what extent NIEES is more comparable to other regulated (network) businesses than a supply company operating in a competitive market and we suggest this needs further explanation.

7. What is the basis for choosing a net margin of 1.7% for NIEES? We would suggest this needs further explanation and supporting evidence.

8. In principle we are very uncomfortable with the proposed approach for fixing the net margin because on the one hand it is justified on the basis of being consistent with gas and previous supply price controls in other jurisdictions but on the other hand it is deemed necessary to modify this approach given the quantum of NIEES turnover and to do so in an arbitrary manner given the lack of regulatory precedent. One could argue that precisely because of the quantum of NIEES turnover an experimental approach, as proposed, should be clearly avoided. It also throws into question the relevance of following the gas precedent and increases the perception of regulatory risk in the market as a whole.

Please do not hesitate to contact me if you would like to discuss any aspect of this response.

Yours sincerely

K Hannafin

Kevin Hannafin
Regulation Manager