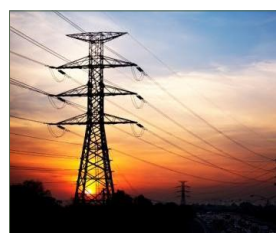


Power NI Supply Price Control 2017 (SPC 17)

UR Consultation

3 June 2016



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; Electricity; Gas; Retail and Social; and Water. The staff team includes economists, engineers, accountants, utility specialists, legal advisors and administration professionals.

Our Mission

Value and sustainability in energy and water.

Our Vision

We will make a difference for consumers by listening, innovating and leading.

Our Values

Be a best practice regulator: transparent, consistent, proportionate, accountable, and targeted.

Be a united team.

Be collaborative and co-operative.

Be professional.

Listen and explain.

Make a difference.

Act with integrity.

Abstract

This paper sets out for consultation the Utility Regulator's (UR) proposals for the next Power NI Supply Price Control (which begins 1st April 2017). It follows on from the UR's Approach paper published in October 2015. The paper outlines the analysis and rationale for the UR's proposed decisions in relation to the main issues within the control, those being its structure and form, an extension to the current Power NI control and the customer coverage (scope) of regulated tariffs.

Following responses to this consultation, final decisions will be taken in autumn/winter this year.

Audience

Consumers and consumer groups; industry; and statutory bodies.

Consumer impact

This paper sets out the UR's proposals for an extension to the current Power NI price control from April 2017 onwards. The price control establishes the permitted costs and profit margin for the duration of the control period. Subsequent regulated tariffs will have to operate within these limits. The price control decisions will therefore impact on the bills of price regulated customers. There are also proposals regarding whether non-domestic customers should continue to be covered by the control and thus able to avail of a regulated Power NI tariff.

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1. CONTEXT

Background

- 1.1 In Electricity, the primary statutory duty of the Utility Regulator (UR) is “to protect the interests of consumers of electricity supplied by authorised suppliers, wherever appropriate by promoting effective competition”¹.
- 1.2 As the former incumbent monopoly supplier, PowerNI has been price-controlled for many years. The electricity supply market in NI is now fully open to competition and there are now a number of competing suppliers in the market. Most of these suppliers supply to both domestic and Industrial and Commercial (I&C) customers.
- 1.3 However, Power NI continue to supply the majority share of the domestic market and, combined with their affiliated company Energia, some segments of the small I&C market also. The implications of this will be discussed further in the Scope and Coverage section of this paper. The current scope of Power NI price control covers all domestic customers and those I&C customers who consume 50MWh or less per annum. There are approximately 780,000 customers in the domestic electricity market and approximately 51,000 in the “less than 50MWh” annual consumption segment of the I&C market.

Approach consultation

- 1.4 The UR issued a consultation² in October 2015 on the approach we intended to adopt for the supply price control project (SPC17). The paper covered the intended approach, timeline and key issues relevant to the price control process for the three regulated energy suppliers in NI:
 - Power NI Ltd (Power NI) in the electricity supply market;
 - SSE Airtricity Gas Supply (NI) Ltd (SSE Airtricity) in the gas supply market in Greater Belfast; and

¹ Article 12 of the Energy (Northern Ireland) Order 2003.

² http://www.uregni.gov.uk/news/consultation_on_approach_to_supply_price_controls_for_energy_companies_laun

- firmus energy (supply) Ltd (firmus) in the gas supply market in the Ten Towns area.
- 1.5 This consultation paper consults on proposals for the Power NI control only. A separate UR paper is being published shortly to consult on proposals for the SSE Airtricity and firmus energy gas price controls.
- 1.6 The October 2015 approach consultation asked for respondents' views on the approach to the various elements of each of the controls. These covered:
- Structure and form;
 - Scope and customer coverage;
 - Duration;
 - Treatment of costs; and
 - Margin.
- 1.7 We received five responses to the approach consultation. However, only three of these referred to the Power NI control in their responses. These were from:
- Power NI;
 - Consumer Council (CCNI); and
 - SSE Airtricity.

A copy of each of response has been published alongside this decision paper and links to each of these responses can be found in Annex 1 to this paper.

- 1.8 Under the 'duration' section, the UR proposed an alternative approach in relation to the Power NI control. This was the option to put in place an extension to the current price control, rather than implement a completely new control on Power NI from April 2017. This is discussed in further detail in Section 2 of this paper. In this context this paper covers:
- Structure and form;
 - Extension of current Power NI control (covering duration, costs and margin); and

- Scope and Coverage.

About this document

- 1.9 The purpose of this document is to consult on the proposals for the extension to the Power NI price control, and on its scope/customer coverage.
- 1.10 This paper is the second in a series of papers following on from the publication of the approach consultation in October 2015. It is anticipated that the work will be completed by the end of 2016, with a final decision paper in the autumn, with a view to having the extension to the Power NI control in place for 1 April 2017.
- 1.11 The UR set out to ensure that the process to set the various price controls (the two gas supply controls of SSE Airtricity and firmus energy are being dealt with in a separate UR paper) would be transparent and timely. To that end, this paper consults on the main proposals for the extension to the current Power NI price control which expires on 31 March 2017. The timetable was presented in the October approach consultation. Given the need for timely delivery to meet licence modification requirements, we intend to stick closely to that timetable and the milestones which were set out therein.
- 1.12 The document is structured as follows:
- Section 2 outlines the proposed structure and form of the control;
 - Section 3 discusses the proposal for the extension to the current Power NI control in relation to costs and margin;
 - Section 4 provides detail on scope/coverage for those sectors of the electricity market we consider should fall within the scope of the control;

Equality considerations

- 1.13 As a public authority, the UR has a number of obligations arising from Section 75 of the Northern Ireland Act 1998. These obligations concern the promotion of equality of opportunity between:
- i. persons of different religious belief, political opinion, racial group, age, marital status or sexual orientation;

- ii. men and women generally;
- iii. persons with disability and persons without; and
- iv. persons with dependants and persons without.

1.14 The UR must also have regard to the promotion of good relations between persons of different religious belief, political opinion or racial groups.

1.15 In the development of its policies the UR also has a statutory duty to have due regard to the needs of vulnerable customers i.e. individuals who are disabled or chronically sick, individuals of pensionable age, individuals with low incomes and individuals residing in rural areas. Some of the above equality categories will therefore overlap with these vulnerable groupings.

1.16 In order to assist with equality screening of the proposals contained within this consultation paper, the UR requests that respondents provide any information or evidence in relation to the needs, experiences, issues and priorities for different groups which they feel is relevant to the implementation of any of the proposals. Furthermore, the UR welcomes any comments which respondents might have in relation to the overall equality impact of the proposals.

Q1. Do respondents agree that where this consultation has an impact on the groups listed, those impacts are likely to be positive in relation to equality of opportunity for energy consumers?

Q2. Do respondents consider that the proposals for the Power NI price control need to be refined in any way to meet the equality provisions? If so, why and how? Please provide supporting information and evidence.

Responding to this consultation

1.17 The UR is keen to hear all stakeholder views on the proposals set out in this consultation paper for the Supply Price Control for Power NI.

- 1.18 We would like to advise respondents that, in keeping with Section 65 of the [Fresh Start Stormont Agreement](#), the maximum time period required for consultations is normally now 8 weeks.
- 1.19 It is our intention to comply with this requirement. We will consult for the normal 8 weeks, but allow an additional two working days to compensate for the public holidays on 12th and 13th July, in keeping with good practice guidelines.

Responses to this consultation should be forwarded to reach the UR on or before 4pm on Tuesday 2nd August 2016 to:

Nicola Sweeney
The Utility Regulator
Queens House
14 Queen Street
Belfast
BT1 6ED
Email: Nicola.Sweeney@uregni.gov.uk

- 1.20 Your response to this consultation may be made public by the UR. If you do not wish your response or name made public, please state this clearly by marking the response as confidential. Any confidentiality disclaimer that is automatically produced by an organisation's IT system or is included as a general statement in your fax or coversheet will be taken to apply only to information in your response for which confidentiality has been specifically requested.
- 1.21 Information provided in response to this consultation, including personal information may be subject to publication or disclosure in accordance with the access to information regimes; these are primarily the Freedom of Information Act 2000 (FOIA) and the Data Protection Act 1998 (DPA). If you want the information that you provide to be treated as confidential, please be aware that, under the FOIA, there is a statutory Code of Practice with which public authorities must comply and which deals, amongst other things with obligations of confidence.

- 1.22 In view of this, it would be helpful if you could explain to us why you regard the information you have provided as confidential. If we receive a request for disclosure of the information we will take full account of your explanation, but we cannot give an assurance that confidentiality can be maintained in all circumstances. An automatic confidentiality disclaimer generated by your IT system will not, of itself, be regarded as binding on the Authority.
- 1.23 This document is available in accessible formats. Please contact: Nicola Sweeney on 028 9031 6622 or nicola.sweeney@uregni.gov.uk

2. STRUCTURE AND FORM

2.1 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 (M_t) for customers subject to and within the scope of price control is made up of a number of components:

$$M_t = G_t + U_t + S_t + K_t + (J_t - D_t) + E_t$$

In any given year t ,

2.2 G_t refers to the cost of the "wholesale" electricity which Power NI purchases and so long as Power NI complies with its Economic Purchasing Obligation, this will be passed directly through to customers via the regulated tariff.

2.3 U_t covers the costs of using the electricity network; these costs are regulated for all Suppliers through the NIE Transmission and Distribution (T&D) price controls.

2.4 K_t is a correction facility whereby under or over-recoveries in the previous year can be collected by the business (under-recovery) or given back to consumers (over-recovery).

2.5 J_t encompasses costs associated with buy-out from the Northern Ireland Renewables Obligation with the D_t term representing any savings on the buy-out Power NI achieves.

2.6 E_t is associated with costs which are uncontrollable and are passed through to customers via the regulated tariff on a 100% basis. These costs include licence fees; approved IT projects spend required in order to put in place the systems and processes to comply with licence obligations and pension deficit costs incurred before 31 March 2015.

2.7 The E_t element of the control is reviewed and amended in the licence as part of each price control setting process. This will be particularly relevant regarding the pension deficit recovery (which is currently a pass-through item in E_t). The Competition Commission ruled during the RP5 referral that the treatment of the pension deficit of NIE should be consistent with Ofgem's treatment of pension deficits of the distribution businesses in GB. The UR decided that it was appropriate to adopt these principles for the other NI regulated energy businesses that seek to pass through pension deficit costs through their

regulated tariffs. This is directly relevant to Power NI and their recovery of historic pension deficit. A formal notification of the new arrangements and the cut-off date for the recovery of historical pension deficit was issued December 2014 in the paper "*Pension Deficit Recovery – A Utility Regulator Position Paper*³".

2.8 This paper stated that the cut-off date would be 31 March 2015 and that the historical deficit determined at this time would be recovered over no longer than 10 years. The paper stated that "The companies affected by this decision will need to submit calculations of historical and incremental deficits and illustrate compliance with the RIGS methodology for the purposes of setting regulated tariffs." The UR's intention to apply consistently this policy in relation to pension deficit recovery was previously consulted on as part of the 2012-14 Power NI price control.

2.9 As demonstrated above, the majority of Power NI's costs that go into regulated end tariffs are straight 'pass-through' costs which are subject to other price controls or regulations; and thus this price control review deals principally with the S_t term of the tariff formula (along with the aforementioned E_t), which is in effect Power NI's own operating costs and net profit margin allowed by the regulator. This amount must be sufficient to finance an efficient business of the licensee and should comprise the following elements:

- Operating costs;
- Allowed Margin.

2.10 The Allowed Revenue of S_t is currently collected on a ratio of a 70% fixed amount plus a 30% variable amount collected on a per customer basis. This was reviewed as part of the last control and as a result it was determined that the split should be adjusted slightly (moving to 70:30 from 67:33).

2.11 The approach consultation proposed that the structure and form of the control would remain the same and respondents were asked to provide their view on this.

³ http://www.uregni.gov.uk/news/view/regulator_publishes_a_pension_deficit_position_paper/

Consultation response in relation to the structure and form of the Power NI control

2.12 CCNI highlighted the need to ensure that all costs which are ‘passthrough’ are appropriate. They stated:

“Uncontrollable costs that are passed through to consumers on a 100% basis, need to be carefully considered by the UR. If there is any influence Power NI can exercise in reducing these costs it must be incentivised to so.”

2.13 The UR does support this view and would highlight that the costs which are allowed to be ‘passthrough’ are strictly defined in the Power NI licence and that there is a rigorous process in terms of ensuring that these costs are appropriate, efficiently incurred, required and actually incurred. No pass through costs are approved unless the UR is satisfied that all these criteria have been met.

2.14 Power NI, in their response, stated that the structure and form of the control remained appropriate.

2.15 Therefore, as stated in our approach paper, we are of the view that the structure and form of the Power NI control should remain the same.

Q3. Do respondents agree with the proposal that the structure and form of the control remain the same?

3. EXTENSION OF THE CURRENT POWER NI PRICE CONTROL

3.1 The October approach paper stated that the duration of the next price control could be one, three or five years in duration. However, the UR indicated that there was also a potential alternative option to extend the current Power NI price control and noted the reasons for considering this alternative.

3.2 The development of the new I-SEM wholesale electricity market may materially impact upon the level of operating costs of Power NI in the future. The market arrangements will be very different and much more complex and Power NI will most likely see an increase in costs as a result of changing many businesses processes, e.g. to become a 24 hour trading operation. The changes to the wholesale arrangements will also ripple through to many other cost lines not directly associated with wholesale operation but nevertheless linked. However, this impact of I-Sem on the Power NI business is difficult to forecast and assess with the necessary accuracy in advance. We therefore stated in the approach that we were considering the option of continuing the existing Power NI control parameters until such time as we can make a more informed forecast of the I-SEM impacts on their business and the efficient cost and margin levels which we should allow.

3.3 It is anticipated that the new I-SEM market will 'go-live' in the latter stages of 2017. The market design is still in development and as such makes it more difficult to determine with a degree of certainty what the likely cost impacts on Power NI could be. In this context, the UR considered the option of an extension to the current control until there is more clarity in terms of the likely cost impacts.

3.4 The approach paper proposed that the current control could potentially be extended for:

- One year – thereby ending March 2018; or
- Two years – thereby ending in March 2019.

Consultation response in relation to the extension of the Power NI control

3.5 The UR received a number of responses to the approach consultation and those which referred to the extension were positive. CCNI stated:

“Consumer Council is open to considering a potential roll-over of the current Power NI price control to help address the uncertainty in relation to the development of the new I-SEM”

3.6 Power NI were in favour of an extension to their current control given the uncertainty surrounding I-SEM:

“ISEM represents a fundamental redesign of the wholesale electricity market with a targeted implementation date part way through the first year of any potential new price control term...Full clarity is unlikely to be forthcoming until post ISEM go-live. This introduces a substantial degree of subjectivity into the forecast costs and renders an objective assessment impracticable. To progress a conventional new price control determination would require significant business model and cost estimation, exposing Power NI to risk and undermining the evidence based decision making regulatory principle”

3.7 In this context UR is minded to extend the current Power NI price control, rather than develop and implement a completely new control at this time. There have been a number of iterations with Power NI since the issue of the approach paper to help formulate how the extension would work.

3.8 Through this iteration the UR and Power NI have agreed the following principles to establish how the extension will operate:

- The current control will be extended for two years - until 31 March 2019;
- One-off non-recurring expenditure items that were included as allowable costs in the current control have been removed from the operating expenditure allowance and will not be included in the extension-related allowed costs;
- Estimated efficiencies earned in the current control will be shared 50:50 with customers during the extension period, with the assumption that the remaining efficiency gain will address the move to the new I-SEM model during the extension period and cover any increased cost;
- Cost allocations between the regulated and unregulated businesses of Power NI will be refreshed for each year of the extension to reflect the actual customer numbers and volume splits between the two businesses

- Margin level will remain the same during the extension period.

Q4. Do respondents agree with the UR minded to proposals in relation to the extension of the Power NI price control?

4. SCOPE AND COVERAGE

- 4.1 This section of the paper discusses the scope and coverage of the Power NI price control. The UR has price controlled Power NI in the domestic and I&C sectors where they are dominant and competition from other suppliers has not been sufficient to adequately protect customers. As competition grows and becomes more effective, the argument grows for removal of the price control on Power NI; and instead more of a reliance on the competition from other suppliers as the primary means to protect consumers in terms of price.
- 4.2 Power NI are currently subject to price control regulation for (i) the whole of the Domestic market; and (ii) I&C customers up to 50MWh per annum consumption. Power NI has repeatedly argued in recent years that it is no longer uniquely dominant in the I&C electricity market where it is price controlled, and that the market is sufficiently competitive that the price control should be removed from the remaining I&C market (leaving then only domestic customers within the scope of the price control). The UR has been actively considering these issues, as noted in our October Approach paper.
- 4.3 Market share is deemed to be an important factor in the assessment of dominance, as well as a range of other factors and indicators that are also assessed by the UR.

Overview of Market Dominance

- 4.4 Establishing whether a supplier is in a uniquely dominant position in a market is important in identifying whether there is a justification for treating that supplier differently from other suppliers, by applying to it a price control to restrain its potential ability to take advantage of its significant market power. Indicative of a supplier's market position is the market share that the supplier enjoys in that market. The prevention of the potential ability of Power NI to abuse their dominant position, to the detriment of consumers and competition, is the overriding and clearly articulated reason why the UR price controls Power NI in the markets where they remain dominant.
- 4.5 With a market share of 50% or more, there is a legal presumption of dominance. Clearly any presumption is capable of being rebutted. However, the higher the

market share, the less likely it is that the presumption will be rebutted. Within a market share range of 40-50%, there is no legal presumption of dominance either way. The analysis of other factors, such as the relative market share of their competitors, market entry barriers, etc, will require even more scrutiny to help determine whether dominance exists in the market. Clearly the lower the market share, the less likely that dominance will be established. There have rarely been findings of dominance below a 40% market share.

4.6 It is in this context that the trigger for a consultation on the retention of the control on Power NI was set at a market share level of 50% in the decision paper for the 2014 – 2017 price control.

4.7 Power NI remains dominant in the domestic market with a market share of circa 66% by customer number and circa 64% by consumption. Though they have lost market share in recent years, they remain significantly dominant in the domestic market. The UR envisages that price control regulation i.e. the setting of regulated tariffs offered by Power NI will continue to apply to the whole Domestic market whilst Power NI remain in such a dominant position. The UR has previously committed to, and will continue to, monitor the situation as further competition emerges and in light of our statutory duties.

4.8 The situation for the non-domestic market in Northern Ireland for the supply of electricity is less clear. Power NI is no longer price controlled in the larger I&C market. This control scope was removed many years ago as competition emerged and became established for those larger customers. The previous price control review also examined the scope of the control; and as a result the threshold for price regulation in the non-domestic market was lowered at that time from 150MWh to the current 50MWh.

4.9 To date, Power NI (when taken with their affiliate company, Energia) has been the dominant supplier in the 0-50MWh I&C market, and is currently still subject to price control and associated regulated tariffs. However, the market shares have been changing since the last price review and now require further consideration.

4.10 As stated in our previous review of scope, the UR considers that undertakings within the same corporate group are in effect one undertaking when considering market power. This is consistent with precedent elsewhere in Europe. Therefore,

we are following established practice by aggregating the market shares of Power NI and its sister company affiliate Energia for the purposes of the analysis.

4.11 The approach paper stated that the UR would review the scope of the price control as part of the current price control setting process. It is important to reference the 2014 Power NI Supply Price Control decision paper⁴. This paper stated that there would continue to be a price control on the non-domestic sector of 0-50MWh. The decision paper also set out what the criteria would be that would trigger a consultation on further end-user price control de-regulation of the I&C sector.

4.12 The criteria included:

- 1. Power NI/Energia must have a combined market share (by consumed units) of less than 50% for two consecutive quarters; and*
- 2. There is a minimum of 3 independent suppliers, each of which has at least 10% share of consumed units in the relevant market. For clarity, what this means in practice is Power NI/Energia plus two other independent suppliers.*

4.13 As it currently stands, this second criteria has been met. Power NI and Energia combined have a market share in the 0-50 MWh sector of around 53% and there are two other suppliers with more than 10% of consumed units in the 0-50MWh market.

4.14 With regard to the second criteria and following internal discussion and consideration, and given the criteria has been met for a substantial period of time the UR is of the view that criteria 2 is no longer required. However it has been met nonetheless. We are also removing the need for a consultation at the trigger point. This current consultation in effect fulfills that purpose. In considering the scope of the control it could be argued that given the first criteria has not been met the current control needs to remain in place until the 50% market share threshold has been in place for two consecutive quarters. Meeting this requirement in the context of dominance and the observed market activity in the 0-50MWh market will be discussed later in this section.

⁴ http://www.uregni.gov.uk/news/ur_publishes_power_ni_supply_price_control_2014-2017

4.15 The approach consultation also stated that a number of indicators/measures of the degree of competition would be considered in our assessment of the need for the remainder of the non-domestic sector of the market i.e.0-50MWh to remain under the price control or not.

4.16 As well as market share by consumption, these include:

- Number of suppliers;
- Substitutability of the product; and
- Market share trends over time;
- Customer switching rates.

Approach Consultation responses in relation to the review of Scope

4.17 Respondents were asked in the Approach paper published in October 2015 to give their views on the UR reviewing the scope of the Power NI control.

4.18 In their response to the approach consultation CCNI were supportive of reviewing the scope of the current price control on the 0-50MWh sector. However they did urge caution. They stated:

“The Consumer Council recognises that given the greater level of competition in the Industrial & Commercial (I&C) market, there may be merit in the UR proposal to review price regulation in the 0-50MWh sector of the market. However, the Consumer Council urges caution and highlights that, without adequate protection, small business consumers are, along with vulnerable domestic consumers, the group most likely to lose out in an unregulated energy market.”

4.19 SSE Airtricity, in their response, also urged caution. They stated the view that deregulation in the 0-50MWh sector was premature. As highlighted above, they also gave the opinion that the current measure of market shares which is carried out by consumption should be on the basis of customer numbers not consumption.

“SSE believes that market share for Power NI should be looked at in conjunction with that of its other brand Energia. In addition, as set out above, SSE believes that the driver of deregulation should be customer numbers and not consumption

to more appropriately reflect competition developing. As such, SSE's view is that deregulation in this sector is premature."

4.20 However, the UR would point out that the issue of dominance in the market as defined was measured by consumption to date and to change this now would be inconsistent with previous tranches of deregulation.

4.21 Power NI argued strongly that there should be a review and that in fact the control should be removed immediately from the 0-50MWh sector of the market.

4.22 Power NI also argue that they do not believe that the 0-50MWh sector of the market is a 'market':

"Power NI considers this decision was fundamentally flawed. Price regulation is not in place for the entirety of this sector but rather a sub-section of a sub-section of the market share figure described above i.e. it is not in place for the entire 50% of the combined Power NI/Energia share but rather a percentage of Power NI's share only."

4.23 The UR would refute this, given that we were clear about defining the market as being 0-50MWh and not the entire I&C market as a whole in terms of determining dominance at the last price control and outlined the reasons for this.

4.24 Power NI also reference EU policy and the fact that the retention of a price control on the I&C market is not consistent with this policy.

4.25 The UR is unaware with any specific EU directive requirement which precludes end-user price regulation in the small business market. However we do see some merit in Power NI's argument and the EU direction of travel they are pointing to. At present however the UR's current policy response to dominance is to continue with price regulation on the dominant player. This is currently the case in both electricity and gas.

4.26 They also stated that they believe they are no longer dominant in this market and by retaining a price control the UR is distorting the market:

"It seems clear to us that the current market conditions necessitate a consultation on the removal of price regulation in the non-domestic sector as there is a clear lack of dominance. Further, the retention of price regulation in the non-domestic sector is ineffective, distortive and has disproportionate effects on the development of competition and the wider electricity supply market."

4.27 As highlighted in the analysis above, competition has developed well in the 0-50MWh market whilst the price control has existed. Therefore, the UR would disagree with this statement.

Number of Suppliers

4.28 There are currently 8 active electricity suppliers in the entire Non-Domestic market (or 7 if you combine companies that are members of the same corporate group) though several operate on a very small basis. This situation can be deemed as producing six competing suppliers to Power NI/Energia. They are:

- Budget Energy;
- Click Energy (*recent entry to the market*);
- Electric Ireland;
- Go Power (*recent entry to the market*);
- SSE Airtricity;
- Vayu

4.29 The UR monitors the market shares in the 0-50MWh sector on a quarterly basis. We receive supplier market share data, which provides details of supplier market shares, by both customer and consumption, split into 10MWh usage bands.

Substitutability of the product

4.30 Electricity (electric energy) is a homogeneous commodity and, in principle, the nature of the good consumed by a large industry is the same product that is used by small consumers in other parts of the system, since in all cases it is electromagnetic energy guided by the networks. In that sense, the substitutability of product between electricity suppliers is very high with little product differentiation. As regards electricity per se, and the substitutability of it as a product, the product is the electric energy and there is extremely limited (if any) ability to substitute the product for something else, certainly in the short term time horizon. This reinforces the potential for dominance and market power issues to be of material concern where there is a single supplier or inter-supplier competition is ineffective.

Market Shares Trends

4.31 In assessing market share, the UR has always assessed a supplier's share based on consumption data (rather than on customer numbers). Furthermore the combined share of Power NI and its affiliate Energia have been taken together for the assessment of dominance, as they have common shareholders/ultimate controllers. Currently the combined share of Power N/Energia in the 0-50 MWh sector of the market is 53% by consumption.

4.32 In terms of market share trends, at January 2014 (just before the beginning of the current control) the Power NI/Energia market share was 58% by consumption. At that time we anticipated that the market share might deplete more rapidly to below 50% over the course of the coming years. Whilst it has reduced, it still remains above 50%.

4.33 Table 1 below shows market shares by consumption in January 2014 and compares these to the latest information submitted in February 2016⁵ across the 4 main suppliers in the relevant 0-50 MWh category.

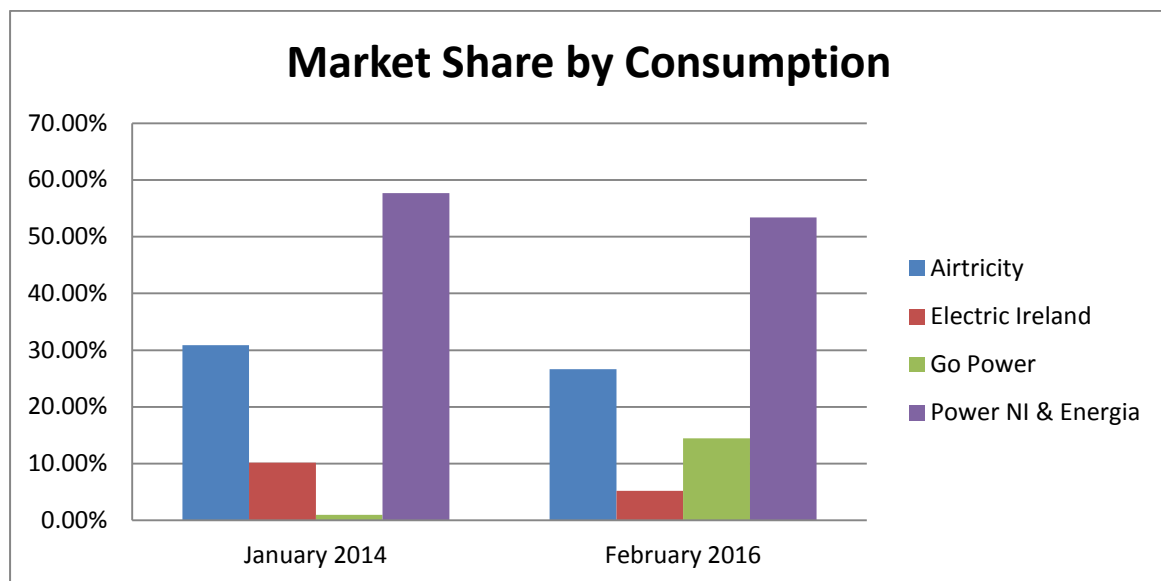
Table 1: 0-50 MWh Market Shares by Consumption January 2014 and February 2016

	Airtricity	Electric Ireland	Go Power	Power NI & Energia
January 2014	31%	10%	1%	58%
February 2016	27%	5%	14%	53%

4.34 Graph 1 below shows the same information as contained in Table 1 in a graphical format.

⁵ Market share information provided by NIE up to February 2016

Graph 1: 0-50 MWh Market Shares by Consumption January 2014 and February 2016



4.35 The table and graph above highlight the significant shift in market shares when measured by consumption. As previously stated, whilst Power NI is still presumptively dominant, (i.e. market share above 50%) we have seen significant recent competitor activity in this sector and a fall in Power NI/Energia share. A slowly falling market share for Viridian has always been the trend since the market was first opened to competition. Previous to this Power NI had a monopoly position in the small business market. We also can observe market expansion following market entry from Go Power and this is another indicator of a healthy market i.e. when a new entrant can expand rapidly following market entry. This expansion has been at the expense of all the three other major suppliers in the market.

Customer switching rates

4.36 Customer switching is another metric that can be examined to determine how active a market is. As previously mentioned NIE provide the UR with market share information in the 0-50MWh market and the sub-sectors within this market. However, they do not provide specific switching information for this market. In this context we have looked at the customer switching rates for the <70kVA market to estimate the customer churn rate in the small business market. Table

2 below shows the switching rate for the years 2014 and 2015. This was calculated by taking the total switches for the year in the <70kVA market as a percentage of the whole <70kVA market.

Table 2: Customer switching rates in the <70kVA market for 2014 & 2015

	2014	2015
Customer Switching %	10%	9%

4.37 The annual customer switching rates were circa 10% for 2014 and circa 9 % for 2015. These rates would be considered as a reasonable rate in terms of an active market. They are also comparable with switching rates in the small business sector in Rol.

Conclusions on retaining the control on the overall 0-50 MWh I&C market

4.38 Taking the above analysis into consideration it could be argued that the 0-50MWh I&C market shows signs of active supplier competition, with market shares shifting in terms of distribution amongst the suppliers and switching rates at a reasonably high level. There are a number of active suppliers and Power NI/Energia market share continues to decline slowly but steadily. They are now very close to falling below the 50% market share level where presumptive dominance ends. Therefore, there is a strong argument to remove the price control on the remaining 0-50 MWh I&C sector at this point as opposed to waiting until the 50% market share trigger is actually breached. The UR proposes to consult on this question now.

4.39 The UR notes that, if we make a final decision in the autumn to remove the remaining I&C sector from the coverage of the price control, this will be the first time that smaller businesses in NI will not have the price protection of regulated tariffs. In effect, the growing level of competition, new supplier entry and competition to Power NI will be the means by which customers will be protected in relation to price. Several key follow on points emerge then:

- I. It is vital that I&C customers, and their representative bodies, actively consider and weigh up their electricity supply choices to make sure they are getting the best possible deal and price;
- II. They must continue to do this over time, not just as a one-off, and be “active” shoppers-around;
- III. The UR will continue to monitor the I&C markets and supplier prices and profits to make sure that customers are benefitting from competition and that market power and dominance issues do not re-emerge and threaten consumer protection.

Potential for retention of a price control within the smallest customer (0-10 MWh) sub-sector of the 0-50MWh sector

4.40 Given the discussion above, and the proposal to remove the price control for the remaining 0-50 MWh I&C market, the UR considered if there was any merit or argument in carving out the smallest I&C customers and retaining the price control arrangements for this I&C sector alone. We therefore carried out some analysis to inform a decision regarding the possible retention of the price control not on the 0-50MWh market as a whole, but rather a price control on a sub-sector of customers. We looked at the smallest I&C customer sector which are those using 0-10 MWh per annum. As opposed to looking at dominance within the subsection, we examined if there are potential differences in the market and in the customers in the lower end of the 0-50MWh market as opposed to those in the upper end. This analysis examined the customer losses which Power NI has experienced over the last two years, the number of suppliers in the sub-sections of the 0-50MWh sector, net movement in their customer numbers and the potential characteristics of those customers in the lower subsector of the 0-50MWh market. The findings are laid out below.

Power NI Customer Losses

4.41 We requested information from Power NI in relation to the number of customer losses per thousand they experienced in 2014 and in 2015 in each 10MWh subsector of the 0-50MWh market. This gives an indication of whether

the 0-10MWh subsector has greater customer retention to the former incumbent than the other subsectors within the market.

Table 3 – Power NI losses per '000 in 2014 and 2015

Customer Size	2014 Losses per '000	2015 Losses per '000
0-10MWh	35	59
10-20MWh	45	73
20-30MWh	61	105
30-40MWh	78	100
40-50MWh	78	131

4.42 The information in Table 3 can be interpreted in a number of ways. It demonstrates that Power NI do experience a higher number of losses per thousand in the larger subsectors. For example, in the 40-50MWh subsector they had 131 losses per thousand in 2015 versus 59 per thousand in the 0-10MWh subsector. The trend displayed is essentially that Power NI experiences higher customer losses the larger the sector considered. This is to be expected as rival suppliers will seek to capture the higher consumption customers and will market to those more vigorously. As a result of this Power NI face less competitive pressure in the smallest customer segment than in the larger customer end of the 0-50MWh market.

4.43 However, it can also be demonstrated that the losses per thousand in the 0-10MWh in 2015 were significantly higher than they were in 2014 (almost double). The same is true for the other sectors and this indicates that competitive activity in all subsectors of the 0-50MWh market is increasing strongly.

Number of Suppliers

4.44 Another metric which can be used to determine how active a market is, is the number of active suppliers. In addition to Power NI and Energia there are six other competing suppliers in the 0-50MWh market. These suppliers also operate in all subsectors of the 0-50MWh market. Therefore, from this perspective

customers in each subsector have as much choice in terms of suppliers as in this market as a whole i.e. a customer in the 0-10MWh subsector has access to the same suppliers as those in the rest of the market.

4.45 The market share information for the main suppliers (three of the six competing suppliers are small new entrants and not included in the table) is shown in Table 4 below. It is shown for the 0-10MWh and the 10-50MWh subsectors of the market.

Table 4 – Market shares 0-10MWh and 10-50MWh Feb 2016

Customer Size	Power NI	Energia	PNI/Energia	Airtricity	Go Power	Electric Ireland
0-10MWh	51%	9%	60%	23%	13%	4%
10-50MWh	36%	16%	52%	27%	15%	5%

4.46 The table demonstrates as expected that Power NI/Energia do have a higher market share in the smallest size band. However, it also shows that the range of suppliers are equally active in the market sectors shown and compete in all sectors, as can be seen in the similar distribution of market shares in each sub-sector shown.

Power NI Net Movement in Customer

4.47 Another market view can be taken by examining the net movement in customers of Power NI in each of the subsectors. NIE reports show that Power NI obtain circa 70% of the new connections in the 0-50MWh market. This is not a systemic occurrence in that Power NI is not the default or commissioning supplier. A newly connected customer must choose a supplier and Power NI clearly take a large proportion of the new connections. It would appear that many of the newly connected customers in smaller end of the I&C market choose to go with Power NI.

4.48 Table 5 below demonstrates that Power NI net movement in customer numbers in each of the sub-sectors is a net loss, except for the 0-10MWh sector in which they have a net increase. It can only be speculated if the potential

reasons for this, in conjunction with having fewer losses per thousand in the 0-10MWh sub-sector, are:

- that most new connections are in the 0-10MWh sector;
- other suppliers are reluctant to take new I&C connections as they are a credit risk; or
- newly connected customers flock to Power NI for reasons of brand loyalty and perception.

Table 5 – Power NI net movement in customers 2014-16

Customer Size	Jan 2014 Customer Numbers	Jan 2016 Customer Numbers	% Movement
0-10MWh	19,530	20,359	4%
10-20MWh	7,446	5,969	-20%
20-30MWh	2,903	2,720	-6%
30-40MWh	1,650	1,610	-3%
40-50MWh	1,029	943	-8%

Customer characteristics

4.49 In determining if there are unique features within the subsectors of the the 0-50MWh market, we also considered the customer characteristics within it. It could be argued that the smallest I&C customers in the market have certain characteristics which may be part of the reason that the analysis in the previous sections shows that in the 0-10MWh subsector Power NI has less customer losses per thousand and their customer numbers have also seen a net increase as opposed to a decrease in each of the other subsectors.

4.50 The average usage in the 0-10MWh sub-sector is 4MWh (determined from the data provided in the reports provided to the UR by NIE) which is around the same as an average domestic customer. The Federation of Small Businesses (FSB) have highlighted to us, in their response to the recent Review of Effectiveness Phase II consultation, that their members often find it difficult to engage in the energy market. They cited reasons such as:

- difficult to compare offers – confusing;
- focus on their core business allows less time to research into the different options, they don't have specific resource to do it; and

- lack of buying power.

4.51 Reasons such as those above are similar to the reasons why some domestic customers don't switch (and most domestic switches require a doorstep visit) and likely contribute to making these customers more 'sticky' and less able or willing to switch than larger I&C customers.

Conclusions on data and UR Proposal

4.52 On balance, the UR does not believe that there is enough evidence to support sub-dividing the 0-50MWh market and creating a subsector of 0-10MWh, with the retention of a price control on it. The analysis above gives conflicting signals with some potential indications of raised market power, and fewer losses per 1000, in the 0-10MWh sub-sector. However, the data also indicates that competition is increasing in all the I&C subsectors over time. Power NI losses per 1000 have almost doubled in the 0-10MWh subsector in the period examined. Whilst they are lower in this sub-sector than the others, they still show an increase in competition and market activity. The data also indicates that there is the same number of active suppliers in all 0-50MWh market sub-sectors.

4.53 In terms of the legal position on the issue of price controls for the non domestic sector, Power NI have pointed out to the UR that they feel the continued retention of a price control in the I&C market is inconsistent with EU law. This has been put forward by Power NI many times. Whilst Power NI's views can be challenged, it tends to lend weight to the need for the removal of the control in the I&C market alongside the market metrics discussed above.

4.54 Given all the above, and the UR duty to promote competition if appropriate to do so, the UR is now consulting on the removal of the price control on the entire remaining electricity I&C sector of 0-50MWh at the end of the current control period (31 March 2017). On balance there is a clear direction of travel with Power NI continuing to lose market share and material competitive activity in the entire 0-50 MWh market. The UR is consulting on this proposal in this paper. In terms of timing for a removal of the control we take the view that it would be prudent to set 31 March 2017 as the date to dovetail with the beginning of the extension period. This allows certainty and clarity around such things as the allocation of costs between the regulated and unregulated parts of the business.

Logistical considerations for a scope change

- 4.55 The UR consider it extremely important that we identify and put in place whatever measures are necessary to ensure that all I&C customers, especially those in the 0-50 MWh category which could be newly de-price controlled, benefit fully from competition amongst suppliers. We want to use this consultation to seek feedback on what those measures might be, and how best we can ensure that I&C customers gain the benefits of competition.
- 4.56 If the UR were to reduce the scope of the Power NI price control we are of the view that other things may need to be put in place along with any change in scope. The UR would like to create as much as we can a 'level playing field' in this market between Power NI and the other competing suppliers. In this context, we would be keen to implement measures which could help this.
- 4.57 During the consultation and in advance of a final scope decision in the autumn, the UR will continue to work with Power NI to clarify any actions which will need to be taken in advance of the removal of the price control on the 0-50MWh sector.
- 4.58 These could include, but may not be limited to:
- Requirement for Power NI to write to all the affected I&C customers, with text approved by the UR, informing them of the ending of the control scope for I&C customers and informing/reminding them of the existence of competing suppliers and their ability to switch as a condition of price control removal and the furtherance of the UR statutory duty to promote competition;
 - Potentially sharing of I&C customer data (contact details, consumption, MPRNs) with other suppliers to allow effective marketing from other suppliers. This could potentially be a database, perhaps managed by the network company for example, or made available to other suppliers by Power NI as a one off action and a condition of the price control removal and the furtherance of the UR statutory duty to promote competition. The rationale for such a measure is that as former incumbent Power NI has access to this information on the bulk of the customers in the 0-50MWh market as most customers are either still with Power NI or have at one time been a Power NI customer. Whilst there may be data protection issues with this proposal the UR feels in

principle it may be the right thing to do. The proposal however is only at an early development stage. We would welcome respondent's views on this measure;

- Information session with small business representative bodies and consumer groups to ensure they are aware of the changes and their need to assist their members/consumers access information and the best switching opportunities, if any, for customers; and
- Implications on the 'K' factor (reconciling the amount relating to those customers who will no longer be price controlled).
- We would also be interested in any other proposals from respondents which they believe would make the market more open and transparent and the rationale behind any such measures.

4.59 It may be that these actions are not required, however the UR is keen to hear respondents' views on these and what other possible actions may need to be taken to ensure customer protection, a level playing field for all suppliers and that Power NI does not have any commercial advantage over other players if the price control is removed.

4.60 A final consideration to note at this point concerns the possibility that the Power NI/Energia combined share may increase again over time after the I&C de-scoping has occurred. If this happened and their combined market share in the 0-50MWH category materially increased above the 50% dominance level, to the extent that they were once again presumptively dominant, or proved dominant after a full economic market assessment was carried out, what should the UR response be? The answer to this is not straightforward, and it would be necessary for the UR to consider all the circumstances at the time before reaching a final policy decision. However it is important to note that the UR will continue to monitor the combined market shares in this sector, together with other variables related to this I&C market sector through our REMM regime and should the scenario described above occur then there would be a requirement for the UR to consider action and reconsider the need for customer price protection in that scenario. We are happy to take consultee's views on this matter as part of this consultation.

Q5. Do respondents agree with the UR's proposal to reduce the scope of the Power NI price control and remove price regulation on the 0-50MWh market?

Q6. Do respondents agree that there is insufficient evidence for the 0-10MWh sub-sector being treated differently to the rest of the 50MWh market?

Q7. Do respondents think any other actions need to be taken in advance of the price control being removed on the 0-50MWh market?

Q8. Do respondents agree with the potential measure of sharing customer data in the 0-50MWh market with all suppliers? Please provide detail if you believe there are potential issues.

Q9. What other measures do respondents believe could be put in place? Please provide detail and rationale for these measures.

Q10. What are respondents' views on the issues that may arise should Power NI's combined market share in the 0-50MWh sector increase again to substantially above the 50% level? Do respondents consider that regulatory intervention to fully protect customers would then be required?

5. CONSULTATION QUESTIONS

5.1 The UR is keen to hear the views of interested stakeholders and invite representations on the following questions:

Q1. Do respondents agree that where this consultation has an impact on the groups listed, those impacts are likely to be positive in relation to equality of opportunity for energy consumers?

Q2. Do respondents consider that the proposals for the Power NI price control need to be refined in any way to meet the equality provisions? If so, why and how? Please provide supporting information and evidence.

Q3. Do respondents agree with the proposal that the structure and form of the control remain the same?

Q4. Do respondents agree with the UR minded to proposals in relation to the extension of the Power NI price control?

Q5. Do respondents agree with the UR's minded to position to reduce the scope of the Power NI price control and remove price regulation on the 0-50MWh market?

Q6. Do respondents agree that there is insufficient evidence for the 0-10MWh sub-sector being treated differently to the rest of the 50MWh market?

Q7. Do respondents think any other actions need to be taken in advance of the price control being removed on the 0-50MWh market?

Q8. Do respondents agree with the potential measure of sharing customer data in the 0-50MWh market with all suppliers? Please provide detail if you believe there are potential issues.

Q9. What other measures do respondents believe could be put in place? Please provide detail and rationale for these measures.

Q10. What are respondents' views on the issues that may arise should Power NI's combined market share in the 0-50MWh sector increase again to substantially above the 50% level? Do respondents consider that regulatory intervention to fully protect customers would then be required?

Timeframe and next steps

5.2 The following timetable highlights the remaining various stages of the price control review process and (approximately) when the UR expects each milestone to be achieved.

Table 6:Reminder of Price Control Review timetable

Date	Milestone
June 2016	Utility Regulator to publish price control proposals consultation paper
August 2016	End of consultation period
November 2016	Utility Regulator to publish final decision
January 2017	Utility Regulator to consult on licence modifications to implement price control decisions – 28 days
April 2017	Licence Modifications become effective

5.3 In addition to Power NI, the UR hopes that a wide range of interested parties will actively participate in this consultation process, including customers/customer representatives and rival retailers.

5.4 Feedback to this consultation from interested stakeholders will help to shape the UR's decision paper containing proposals which is planned for November 2016. The decision paper, similar to this consultation paper, will include details of respondents' feedback to this consultation and include the UR's decisions with regards to the Power NI proposed rollover and the scope of their control.

ANNEX 1

We have published the consultation responses and these are available at the following links.

Power NI	http://www.uregni.gov.uk/uploads/publications/Power_NI_response_Price_Control_Approach_Consultation.pdf
CCNI	http://www.uregni.gov.uk/uploads/publications/Consumer_Council_response_to_UR_Electricity_and_Gas_Retail_Supply_Price_Control_s.pdf
SSE Airtricity	http://www.uregni.gov.uk/uploads/publications/SSE_response_to_UR_PC_approach_paper_consultation_81215.pdf