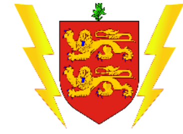

Office of the Sark Electricity Price Control Commissioner

Electricity Prices- Determination

8th November, 2019

Determination

1. Under section 3 of the Control of Electricity Prices (Sark) Law, 2016 (the "2016 Law"), my Office is charged with determining whether electricity prices set by a regulated electricity supplier on Sark are, or are not, fair and reasonable. Part II of the 2016 Law contains various powers enabling me as Commissioner to investigate electricity charges and under Part III of the 2016 Law, following completion of an investigation, the Commissioner is obliged to make a Determination, as described above.

2. My investigations and discussions concerning electricity prices charged by Sark Electricity Limited[1] (SEL), conducted over the period 21st January 2019 to 16th September 2019, led me to publish my provisional conclusions in a Draft Determination shared initially with Sark Electricity Limited on 17th September 2019 and released to the public on 1st October 2019. I came to the preliminary conclusion that the price of 66 p/kWh Sark Electricity Limited had been charging since 1st January 2018 was not fair and reasonable, nor was the 85 p/kWh Sark Electricity Limited has been charging since 1st November 2019. I have since consulted with Sark Electricity Limited as the regulated electricity supplier that will be affected by any Determination and the Policy and Finance Committee of the Chief Pleas of Sark. I also consulted others, as I saw fit and invited responses from other interested parties on the Draft Determination. The consultation period closed on 22nd October 2019. Sark Electricity Limited was provided with copies of all responses to the consultation and was supplied with copies of other evidence on which I relied. Sark Electricity was allowed a further two weeks to respond to every submission I received.

3. I received 35 responses to the consultation including Sark Electricity Limited. Of these, two gave no opinions, 30 were in general agreement with my arguments and two made no comment on the reasonableness, or otherwise, of my estimate of a reasonable price. Sark Electricity Limited contends that the proposed Determination is fundamentally flawed. I do not agree and will explain my reasoning below. As such, I confirm my assessment that SEL's current basic rate of 85p/kWh is not fair and reasonable. This is because SEL, the combined entity of Sark Electricity Limited and SEHL, has set the tariff in the expectation of recovering costs that I do not regard it is reasonable for customers to bear.

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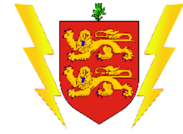
1. The Sark Electricity Company Limited (TSECL) generated electricity by diesel engines and distributed it through a distribution system of cables, switches and transformers, to customers on Sark from 1994 to 2013. In 2014, the name was changed to Sark Electricity Holdings Limited (SEHL) and a wholly owned subsidiary of SEHL was created called Sark Electricity Limited. The original company's assets were kept in SEHL and leased to Sark Electricity Limited which operates the electricity system and sells power to customers on Sark. I refer to SEL as the combined entity for the purposes of this document.

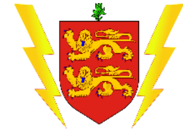


Next steps

4. Under section 15 of the 2016 Law, having determined that the basic rate is not fair and reasonable, I have powers by way of the making of a price control order, to set a maximum price for electricity sold on the island of Sark. I intend now to consider whether or not to exercise those powers and, if I do exercise them, what maximum price or prices may be appropriate. In order to assist me with my considerations I shall be consulting with SEL and other stakeholders.

Responses to the consultation

5. Of the 35 responses (several from more than one individual) to the Draft Determination, excluding SEL, two noted the contents and made no comment and six respondents did not respond directly to the five issues raised in paragraph 67 of the Draft Determination, but gave more general comments. Of the 26 submissions that referred to one or more of the questions raised:
   a) Wayleaves – six land holders responded of which two said they would grant them and four said that their agreement would be dependent on the owner of the electricity company.
   b) Impact of price on consumption – 22 mentioned that they would use more electricity, e.g. they would have a freezer, use their dishwasher and would use electricity for heating and cooking.
   c) 22 said that they would support wind power on the island and, of those, three said that the proposed height was too high and one stated that only one turbine would be acceptable. 15 respondents mentioned solar and/or battery technology in a positive light.
   d) Customer contributions to network capital expenditure. Six respondents mentioned connections, three had paid for them and three did not know as the house was purchased after the connection had been provided.
   e) Reasonable rate of return. 11 respondents said that the 5% real per annum rate of return was acceptable. Seven thought 5% was too high
6. Many other matters were raised by respondents. For example, 12 did not believe that all legal costs should be recovered from customers. 6 indicated that they were seriously considering going “off-grid”. One respondent wanted to understand whether it was a mistake in my calculations that led to the price changing to 53 p/kWh from 52 p/kWh and why I had not explained why I had settled “out of court” with SEL last year. Others raised the effect on business and the economy, young families leaving the island, what happens when the current power station lease expires, measures to prevent “own-generation”, delivering power via a cable from Guernsey, the possibility of the Island itself owning the power company, the threat of the loss of the electricity supply, lack of progress with the purchase of SEL by Chief Pleas, health and safety concerns, abuse of sole supplier position, concerns about the shareholder loan, “as new” valuations, SEL’s director showing a lack of concern for customers, SEL’s director not exercising “reasonable skill and care”, SEL’s philanthropy and negligence (a blind eye to moonlighting). All the responses were shared with SEL but only those from customers who gave their consent may be seen on the website www.epc.sark.gg.



7. I hope that many of these points are covered in this Final Determination. I invite respondents to contact me directly if they believe I have left some issues unanswered.

8. SEL contends that the Draft Determination was fundamentally flawed. It argues that:

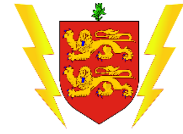
    a. I am biased and unable to exercise my powers fairly. I tried to bankrupt the company in collusion with Chief Pleas so that Chief Pleas could purchase SEL's generation and network assets at a reduced price.
    b. the incorrect price was considered, since 85 p/kWh was the proposed price, rather than the actual price of 66 p/kWh on the date of publication.
    c. only the costs of Sark Electricity Limited are relevant since it is the regulated entity, not Sark Electricity Holdings Limited. I should not "conflate the separate entities of SEL and SEHL", nor "ignore the fact that Sark Electricity Limited does not actually own the electricity generation equipment it uses to generate the electricity. Rather, these assets are owned by SEHL which is not a regulated electricity supplier under the Law. This calls into question the accuracy of the Proposed Determination's valuation of SEL's assets and the use of the depreciation charge of these assets in determining whether the 85 p/kWh price is, or is not, reasonable".
    d. I failed to provide for the profit required by section 13(2)(d) of the Law.
    e. I used my own estimate of SEL's costs whereas I should have used "actual costs as reported in SEL's books of account".
    f. I have not allowed SEL to recover the legal costs it incurred during 2018.
    g. The 53 p/kWh was designed to be close to the 52 p/kWh set in the Price Control Order of August 2019, in other words, I was "goal seeking".
    h. It is necessary to establish a range of prices, rather than just one.
    i. A consideration of fuel poverty and the risk of spiraling prices caused by wealthier customers deciding to self-generate is irrelevant.
    j. My approach to and correspondence with SEL and its representatives has become more aggressively partisan.
    k. I do not have the power to force SEL to change its business model.

9. As a consequence, SEL holds that any subsequent price control order made will be ultra vires and unreasonable. I examine each of these claims below.

SEL's arguments

10. Collas-Crill's response to the Draft Determination contains many assertions that are either untrue, misinterpretations, or reveal ignorance of the facts. I examine these below.

11. Collas-Crill misrepresents the price control process of 2018. The Price Control Process failed "largely due to your own failures". To be clear, neither SEL nor the Commissioner "won". Both parties agreed to settle. This meant that SEL did not carry out its threat to switch off the power to the island, and thereby impose great hardship, risk of loss of life, as well as threaten the integrity of the distribution cables. SEL also agreed to allow a valuation of the company to take place, which unfortunately, has not yet occurred, as described in paragraphs 46(a) and 55 below. I published my reasons for settling on 30th November 2018 and Chief Pleas released a Notice of 1st October 2019.

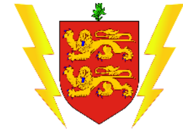


12. I will now deal with the allegation (a), that I tried to bankrupt the company in collusion with Chief Pleas. I will then examine the legal points and show that Collas-Crill has misinterpreted the 2016 Law. I conclude that the argument that any subsequent price control order I may make would be ultra vires and unreasonable is incorrect. I will deal with these points according to the labelling set out in paragraph 8 above. However, In answering some of the issues raised by SEL, either I have used information supplied to me by SEL under a Non-Disclosure Agreement (NDA) signed in November 2017, or which relates to a valuation report provided by the consulting engineer WSP. I agreed not to release details of this report until the negotiations between Chief Pleas and SEL to purchase the company have concluded. My responses on those matters are confined to a Confidential Annex to this Determination and may not be released to the public without the agreement of SEL or for the purposes of Court proceedings. Accordingly, whereas I have provided the Confidential Annex in the version of this Determination that is to be supplied to SEL, I have omitted it from the version that is to be published on www.epc.sark.gg.

(a) Bias and Collusion

13. SEL has not provided any (or adequate) justification for its accusations of bias and collusion with Chief Pleas. The minutes of the Policy & Performance Committee meeting on 8th January 2018, when Collas-Crill alleges such a plan was hatched, reveals a discussion where a Government appointee is reporting his progress to a Government Committee. They are very similar to those of the OFGEM chair in the UK reporting to a Select Committee in the UK Parliament.

14. Similarly, a reading of my correspondence with SEL and the Draft Determination do not support the allegation that my approach has been aggressive; in fact it demonstrates the opposite. I believe that I have been very accommodating to SEL, as shown by the following examples:
    - I offered to accept photographs of the serial numbers on the power station equipment so that SEL would avoid a criminal offence by failing to comply with a Section 5 Notice I had sent.
    - I gave further time to provide information required under a Section 5 Notice.
    - At his request, I organised a meeting with David Gordon-Brown in London to discuss our areas of disagreement and entered into a lengthy email exchange over a seven-month period.
    - I agreed not to publish the WSP report or share it with Chief Pleas whilst the negotiations for the purchase of the company were continuing.
    - At David Gordon-Brown's request, I restricted details of SEL's financial results to a confidential annex to the Draft Determination.
    - On account of David Gordon-Brown's medical procedure, I allowed SEL 10 weeks to consider the WSP report.
    - I sent, as a courtesy, a copy of the Draft Determination to SEL two weeks in advance of its publication.
    - I sent, as a courtesy, a copy of the revised Policy Statement and took SEL's comments into account before publication.



- I accepted SEL's comments on the Policy Statement, provided through Collas-Crill, despite them being sent two weeks after the closing date for submissions.

15. There is, therefore, no evidence to suggest that I am biased and, as such, unable to make a fair Determination.

(b) Wrong Price

16. There is some uncertainty on SEL's electricity price on 1st October 2019 and Collas-Crill asserts that this may cause the Determination to be invalid. This is incorrect. On 27th September 2019, Sark Electricity Limited posted a Customer Letter for 3Q 2019 dated October 2019. It stated that:

> "As many of my customers are much richer than my shareholders, we cannot continue this "Reversed Robin Hood" situation any longer, so effective with the beginning of this month I have to raising the price of electricity to 13.5p to let us break even, and a further 5.5p to try to recapture some of the losses from earlier this year. So your next bill will show your electricity price at 85p."

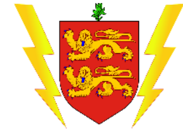
17. This was ten days after I sent the company an advanced copy of the Draft Determination. Subsequently, the letter became unavailable on the web-site. The Draft Determination was released to the public on 1st October 2019. Only after the Draft Determination had been released was the replacement letter brought to my attention. Therefore, the Draft Determination was correct when published. In any event, the Draft Determination shows that both prices are neither fair nor reasonable. This Determination is dated 8th November 2019 and the price SEL is currently charging is 85 p/kWh, according to the latest version of the 3Q 2019 SEL newsletter. However, SEL's lawyers, Collas-Crill, wrote a letter to me on 22nd October 2019, stating *"Rather, the current tariff for electricity is 66 p/kWh and it will remain so until 1 December 2019 when, as notified to SEL's customers, the price will rise to the higher tariff".* I have informed SEL of this inconsistency but have yet to receive a reply.

18. I am also surprised by the reference to "Robin Hood", as I have not found that customers are being subsidized by the shareholders of SEL. In most companies, the shareholders would ensure that the company was not incurring unnecessary expenditure, especially before endorsing a price rise of this magnitude.

(c) Only Sark Electricity Limited is the regulated entity

19. Until May 2019, SEL had not questioned the Commissioner's right to obtain information concerning the equipment required to provide the electricity supply. Indeed, SEL provided their own assessment of the replacement costs of this equipment as early as November 2017. SEL changed its position in a note to me of 21st May 2019 in which David Gordon-Brown wrote:

> *"As this is causing dissention between us, we have no choice but to move back to the exact way the law is written. It makes SEL the regulated company whose costs you have to consider*
>
> *This will exclude SEH and its costs from the process removing the difficult issues of dividends and the other SEH costs. These become an issue for the SEH directors alone*



to decide, as you suggest. Hopefully the process will now be easier and less contentious.

SEH will, of course, still continue to give you any information you require."

20. This last offer was subsequently withdrawn. In a letter to my Office of 16th September, Collas-Crill wrote:

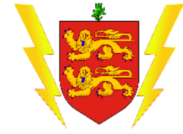
> *"Your position regarding providing access to documents and information is extraordinary. It demonstrates your failure to appreciate the significance of the fundamental company law concept of a separate legal personality. Your suggestion that a company can be compelled to produce documents and information which it does not have and has no right to obtain is absurd. Whilst we are dealing with your Notice issued to pursuant to section 5 of the Law in a separate chain of correspondence (in which we await a response from you), we take this opportunity to make clear to you that should you take formal steps to assert any such entitlement, this will be vigorously resisted and costs will be sought against you on an indemnity basis."*

21. This response surprised me. The claim that Sark Electricity Limited did not have the information I required (under a Section 5 Notice I had issued), nor had the right to obtain it appeared to contradict an agreement Sark Electricity Limited had entered into with my Office on 29th November 2018. Under this "Settlement Agreement" SEL gave an undertaking to:

> *…procure Sark Electricity Holdings Limited (SEHL) to provide access to such of its assets as may be practical and financial information in relation to that company, as may be reasonably required for Chief Pleas to consider the purchase of SEL and SEHL, provided that…"*

22. The 2016 Law does not consider whether or not the regulated supplier owns the appropriate equipment, just that the Commissioner should take the costs of the equipment, such as acquisition, maintenance and fuel, into account. It does not instruct me to ignore such costs if the regulated supplier does not own the equipment itself. Indeed, Section 5(1) of the 2016 Law provides the Commissioner with powers to obtain information from a regulated supplier for the purposes of carrying out an investigation or Determination under this Law. Moreover, under section 5(3) of the 2016 Law, the Commissioner is entitled to seek information from individuals if it is reasonable to believe they have access or control over it. Since SEHL is the sole owner of Sark Electricity Limited and David Gordon Brown is the sole director of both companies and an agreement exists between them relating to the business of the supplier, under section 5(5) and section 5(9), the two companies are "associated". As such, by refusing to provide the information I requested under a Section 5 Notice of 17th August 2019, Sark Electricity Limited is in breach of Sections 10 and 11(2) of the 2016 Law.

23. For the purposes of my investigation of SEL's electricity prices, I have treated Sark Electricity Limited and SEHL as one entity. I have been fortified in this approach because, as David Gordon-Brown, the sole director of both companies, wrote in a letter to me dated 20th November, 2017



> "So, as you have kindly signed an NDA with both companies, I will send you the financial statements for both and I suggest that we ignore the gash we've hacked through the company to split it into two and simply recombine them on paper for regulatory purposes."

24. In addition, David Gordon-Brown wrote to me on January 29th 2019 stating:

> "Whilst Sark Electricity is legally broken into two companies, in reality it operates as one company with a management team of one person, myself."

25. It therefore seemed reasonable for me to treat the two companies as one for regulatory purposes.

26. Collas-Crill contends that, by conflating the regulated entity Sark Electricity Limited with SEHL and calculating a profit based on an assessment of the Regulated Asset Value of SEHL's assets , I have corrupted the proposed Determination's methodology. On the other hand, Collas-Crill reports that:

> "SEL has reiterated, on many occasions that this methodology can be accepted as a genuine commercial valuation strategy"

27. Collas-Crill argues that it is just not an appropriate valuation methodology for Sark Electricity Limited, since this regulated company has no assets. Collas-Crill holds that I should consider Sark Electricity Limited's costs alone when deciding whether or not the prices charged for electricity are fair and reasonable. Figure 1 below shows the components of Sark Electricity Limited's costs for 2016, the last year for which audited accounts have been produced. They indicate that the lease payments to SEHL were the highest single component of Sark Electricity Limited's costs and amounted to 27% of the total. Under Section 13(2)(c) of the 2016 Law, I must consider "the quality and reliability of the supply of electricity and the economy and efficiency with which the supply of electricity is generated and distributed". Collas-Crill asserts that this requires me to consider only the electrical efficiency of the generators and network. I do not believe that the 2016 Law so constrains me. Rather, the 2016 Law instructs the Commissioner to "take all material matters into account".

28. Were I to consider only Sark Electricity Limited's costs, as Collas-Crill suggests, my duties would require me to investigate whether Sark Electricity Limited is purchasing the service from SEHL at a fair and reasonable price. After all, the price is entirely at the discretion of the sole director of both companies of which one is the wholly owned subsidiary of the other.

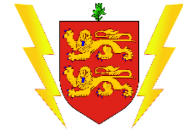
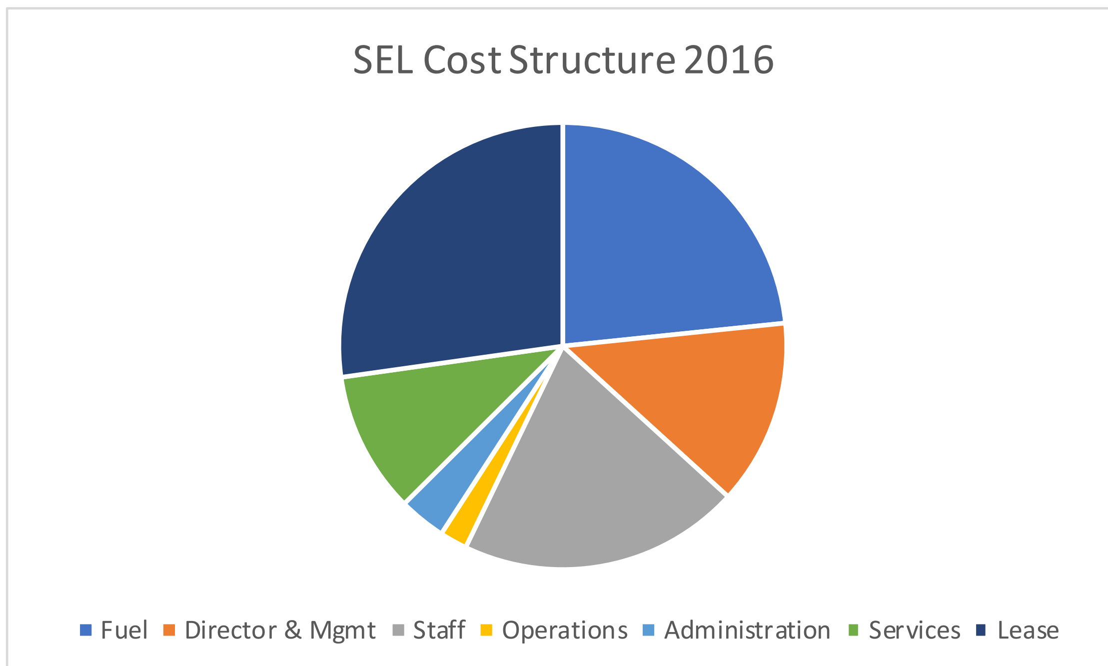


Figure 1



Source: Sark Electricity Limited's Final Accounts, 2016

29. The confidential Annex to this Determination reveals that, were the lease priced on a commercial basis, the annual lease payments would fall by around 50% and the "reasonable" price would be 52.5-57p/kWh. This confirms that the current price of 85p/kWh, or the earlier 66 p/kWh, are not fair and reasonable.

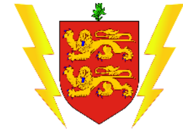
(d) Allowing no profit

30. The Draft Determination calculated a reasonable profit for SEL by deriving a value of the investment in SEL, then multiplying by an appropriate rate of return. This was described in paragraph 24 of the Draft Determination. It explained that the reasonable level of fixed costs was found by adding estimates of:
    - the fixed cash costs (Director's fees, management expenses, operations, services and administration,
    - depreciation, based on the assumed lives of the operational plant, and
    - a profit margin

31. In view of these facts I am at a loss to understand how Collas-Crill can allege that I have not allowed for a profit.

(e) Use of estimated costs

32. Collas-Crill is inconsistent in its arguments on this matter. In some places in its response it argues that the 2016 Law requires that I should assume all of their costs have already been subject to scrutiny by SEL. However, Collas-Crill also complain when I describe SEL's arguments as such. I interpret Section 13 (2)(c) of the 2016 Law as requiring the



Commissioner to consider the economy and efficiency with which the generation and distribution of electricity is provided.

33. Collas-Crill also argues that my choice of assumptions for estimating costs is biased and that *"In determining whether SEL's prices are fair and reasonable, it is clear that the most reliable indicator is SEL's actual costs".* I disagree. This effectively argues that there should be no scrutiny of costs and negates the purpose of the 2016 Law. My estimates of reasonable costs are based on publicly sourced information, discussions with industry experts and an analysis of SEL's reported costs. Many of my estimates have been required because SEL did not hold information it was reasonable for me to expect a reasonably well managed electricity generation and distribution company to hold. Collas-Crill complains that I have always taken the lowest estimate, which is incorrect. Indeed, some of the allowances I have made for costs are significantly higher than SEL has been spending.

34. Collas-Crill also raises an email I received from James Lancaster of Alderney Electricity dated 12th December 2018. They write:-

> *This is telling in that in that same email referred to clearly states that Mr. Lancaster' assumptions would support a price of 60p per unit. Mr. Lancaster goes on to write that "[if] you set a [sic] 55p per unit then it would appear that someone is going to shoulder a loss of about £220k".*

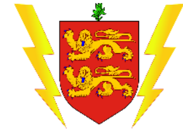
Collas-Crill have obviously erred since a price differential of 5p per unit would have led to a shortfall of £70,000. In fact Mr. Lancaster had calculated the shortfall on the basis of 69p per unit and arrived at a *"loss of about £200k".* The complete message tells a different story. Mr. Lancaster first estimated the fixed costs, including an allowance for depreciation, then continued:

> *"If we add the bottom range of your acceptable return i.e. 150k then the cost to be covered by electricity sales is between 900k and 1.05 million. Assuming 1.4 million unit sales, unit price would need to be between 64 and 75p.*
>
> *I know this is not what the good people of Sark want to hear, but without the actual figures in front of me, my assumptions would seem to support a price of 69p per unit. If you set a price a 55p per unit then it would appear that someone is going to have to shoulder a loss of about 200k."*
>
> *Hopefully, in amongst this you can see where my there are flaws in my assumptions and that this ends up supporting your recommendation*."

Mr. Lancaster had provided me with cost estimates but had over-estimated a number of items, such as rent, rates & insurance (which are not paid on Sark). This was further compounded by my under-estimate of the age of the SEL equipment, which led us both to over-estimate a reasonable value for depreciation and return on capital.

(f) Legal cost recovery

35. Collas-Crill also complains that I have not allowed for SEL's legal costs in arriving at my estimate of the cost a reasonably efficient operator would incur generating, distributing and supplying electricity whilst earning a reasonable return. I gave the reasons for this omission



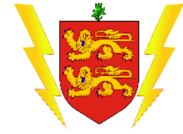
in paragraph 65 of the Draft Determination. The Policy Statement, to which Collas-Crill refers, states that reasonable legal costs responding to Determination and Price Control Orders could be recovered from customers. SEL has, indeed, sent me a schedule of their legal costs on 1st October 2019 which amounted to £446,707, less the £155,000 received from Chief Pleas in Settlement of the Appeal last year. However, I had already written to SEL on 13th September 2019 explaining that I required the costs to be scrutinized by a legally qualified third party, such as a legal costs draughts-person, to determine which costs were reasonable. SEL has not responded to this request.

36. The Policy Statement states that reasonable costs associated with responding to the Determination and Price Control Orders (Section 3, 14 and 16 of The Law), may be recovered through the electricity tariff. I do not think it is reasonable for customers to be forced to cover the costs of an Appeal. A decision to Appeal a Price Control Order, covered by section 20 of the Law, is a commercial consideration and is taken by the director and shareholders of a company. Should they win a case, they may be awarded costs by the Court. If they lose, the company will have to pay their own legal fees and, should the Court so decide, also the costs of the other side. I do not believe it is reasonable for a commercial entity to feel able to initiate Court proceedings in the knowledge that, whatever happens, it will be able to recover its costs from its customers. The representations I have received from customers are consistent with this view.

37. I have examined the schedule that SEL has provided. The schedule lists the legal costs covering the period of the 2018 Determination and the Price Control Order, These amount to £147,666.06. I believe that it is reasonable for customers to pay only reasonable costs through the electricity tariff and, until these costs have been scrutinized as I set out above (paragraph 35), I will not consider them for inclusion in an assessment of a reasonable price for electricity on Sark. In a SEL customer letter of December 2018, David Gordon-Brown stated that he hoped to pay off his legal bills by the end of summer 2019. I therefore judge that, by September 2019, customers have already paid the legal costs of SEL responding to the Determination and Price Control Order of 2018.

38. I am aware that SEL has continued to incur legal bills, as reported in SEL's letter to customers of 7th October 2019. This is despite David Gordon-Brown and my Office agreeing at a meeting to try to limit the use of lawyers in order to keep costs under control. However, although my Office's bills for January to June 2019 were £6,164, SEL's amounted to £63,636. This is because David Gordon-Brown continued to use lawyers. On 1st August 2019, David Gordon-Brown asked me to send all correspondence to a partner at Collas-Crill, irrespective of the subject matter of the correspondence. I have no wish to stop SEL using lawyers. I just do not think it is reasonable for customers to pay for such injudicious and prodigal behaviour.

39. I will ask SEL to send me an estimate of their legal costs of responding to the Draft Determination and, if issued, a Price Control Order, towards the end of 2019. This will give me time to have the bills scrutinised appropriately so that I may judge the reasonable legal expenses SEL may seek to recover in the tariff for 2020.



(g) Goal Seeking

40. The accusation of goal seeking, based on the observation that 53 p/kWh is 1 p/kWh different from 52 p/kWh, is unfounded. The price in the Control Order last year was 49 p/kWh. A 3 p/kWh was included as a supplement for one year to ensure that SEL carried out a valuation of its assets to find the regulated asset value. It was also designed to provide sufficient funding to obtain an assessment of the prospects for lower cost forms of generation for the island.

(h) Reasonable Range

41. I do not believe it is necessary for me to provide a reasonable range of prices in order to determine whether the price charged by a regulated supplier is, or is not, fair and reasonable. I accept that there is some uncertainty in some of my assumptions and alternative ones could lead to different estimates of a reasonable price. However, the current price is so much higher than the resultant mid-point of any range I may derive, that it is reasonable for me to conclude that the current price is neither fair nor reasonable.

(i) Fuel poverty

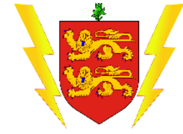
42. The matters the Commissioner is allowed to consider in determining whether the price charged by a regulated electricity supplier is, or is not, fair and reasonable, are not restricted in the 2016 Law (see Section 13(2)). The Commissioner is instructed to "take all material matters into account, …". I judge that a consideration of the potential for high electricity prices to cause hardship is such a matter. Section 13(2) of the 2016 Law states that material considerations include:

    f. The entitlement of the regulated supplier to receive such reasonable return, as the Commissioner thinks fit, on the assets (including plant and equipment and working capital) operated or used by the supplier for the purpose of generating and distributing the supply, and

    g. Any representations made in response to a request given under section 14, or otherwise.

43. I have received representations describing the hardship caused by the former price of 66 p/kWh and the inevitable distress that the current price of 85 p/kWh will create. I predicted that high electricity prices would encourage wealthier customers to decide to generate their own power and disconnect from the SEL network. This risk has been confirmed by the responses I have received to the Draft Determination and has occurred elsewhere.

44. In the past, SEL has responded to a reduction in the demand on its network by raising prices to maintain profits. This would exacerbate the hardship the poorer inhabitants of the island already suffer on account of high electricity prices. I do not believe it is reasonable to ignore this risk. This also represents an existential threat to SEL's business as a whole, a fact I have already pointed out to SEL's director. I judge that it would be within my powers to adjust the entitlement of the regulated supplier to receive a reasonable return as a result of a consideration of fuel poverty.



45. Nevertheless, I have found that the major reason for the previous high price and the present 85 p/kWh are caused by SEL passing on unreasonable costs to its customers. Were these costs funded by shareholders, the proposed price of 53 p/kWh would allow SEL to earn a reasonable return and profit margin.

(j) Aggressively partisan

46. Collas-Crill set out examples of my correspondence with SEL which it claims betray an aggressive approach. I set out below each paragraph and explain why Collas-Crill's allegation is false.

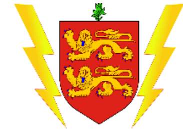
    a) In your letter to the SEL dated 31 January 2019 you write that *"In passing, I should add that I am disappointed that you did not accept my offer to share the valuation report, which I have commissioned, with Chief Pleas, as this would have saved expense for the people of Sark"*. You then go on to write that [that] *"finally, the isolated financial information you provided in the table without further breakdown of expenditure is not particularly helpful for the purposes of the determination I am obliged to make under the Law"*

       Response

       SEL had agreed, as part of a Settlement Agreement of 30th November 2018 that it would undertake a valuation of the company with Chief Pleas, as well as maintain a price of 66 p/kWh for electricity up to 28th February 2019. I wished to be in a position to determine whether the price was fair and reasonable from 1st March 2019 and, in the absence of SEL holding information which it was reasonable for me to assume they kept as a matter of good business practice, I wanted to instruct consulting engineers to conduct a valuation. David Gordon-Brown suggested that I should wait for the SEL/CP valuation to be undertaken. However, this would not have allowed me to meet the deadline of 28th February, so I commissioned WSP to carry out a valuation. If my report had been shared, it would have saved both Chief Pleas and Sark Electricity Limited the cost of commissioning an identical report. I do not regard the offer to save SEL expenses as being aggressive. Similarly, the Table SEL provided contained a series of numbers, as shown below. It is not possible to determine from the table the reasons for the low bank balance. As such, the table was of little use and I do not believe my response was aggressive..

	28 January 2017	28 January 2018	28 January 2019
Bank Balance:	£202,818.30	£260,515.84	£16,716.51
Accounts Payable:	£8,485.28	£8,343.38	£88,188.46

    b) In your email to SEL dated 13 March 2019 timed 13:03, you write *"my role is that of a Commissioner and I am charged with examining prices to determine if they are fair and reasonable. If I find that they are not, the Law provides me with the authority to introduce a maximum price in order to protect customers from, as you put it, "gouging". The confusion about Regulators and Commissioners is yours alone".*



Response

This paragraph is not aggressive. It was Mr Gordon-Brown who first used the term "gouging" in a letter to me of 25th November 2017, to describe the situation were the lease between SEHL and Sark Electricity Limited overpriced. I have since found this to be the case.

c) In an email dated 17 March 2019 timed 15:08, you wrote to SEL that *"I have suggested that you have incurred excessive costs from your management decision to split the company in two, pay for foreign travel and not consider obtaining wayleaves to gain access to cheaper finance. I have also suggested that you investigate using solar PV and wind to lower your generation costs."*

Response

I do not believe that this paragraph is aggressive. Mr Gordon Brown had taken issue with my statement *"Also, you are incurring substantial additional unreasonable costs."* I sent the response mentioned above after he had replied:

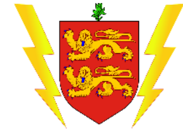
> "Empty allegations like this provide no help. The only suggestion for reducing cost I have seen so far was to issue bonds at 3%. Reality seems to have now changed this to 6%, but you have still not offered any advice on who might be willing to offer to loan us unsecured funds even at 6%. I have been unable to find any below 16%."

d) In an email dated 25 March 2019, you write *"I have received this note and am disappointed that you still do not understand how valuations are undertaken in the commercial world."*

Response

This excerpt from my note to David Gordon-Brown is mild, given the circumstances. David Gordon Brown had instructed a valuer, a Mr Isaacs, to value the combined entity of Sark Electricity Limited and SEHL in March 2017 and he produced a report in July 2018. I was asked by David Gordon-Brown to contact Mr Isaacs so that I could understand why his valuation was far greater than the value reported by WSP. I discovered that David Gordon-Brown had not informed Mr Isaacs of the existence of the 2016 Law. The full paragraph gives a more complete picture.

"I have received this note and am disappointed that you still do not understand how valuations are undertaken in the commercial world. A valuer will anticipate the future cashflows a business may generate, as Mr Isaacs described. The valuer will have regard to the commercial and regulatory environment in which the company operates. In this case, the Control of Electricity Prices (Sark) Law, 2016 is relevant and Mr Isaacs, or any other independent valuer would take it into account, were he to undertake another valuation. The valuer would see that the company would be allowed to make a 'reasonable' profit. I have stated that, in accordance with accepted regulatory practice, I will determine a reasonable profit level on the basis of a return on a Regulated Asset Value (RAV) and that this RAV is set at the current replacement value written down according to depreciation. This is standard practice in commercial transactions for utility



assets in the UK and around the world. As such, the value of the electricity system on Sark will be related to the RAV. Therefore, the WSP value is not an "unnaturally low valuation". I am afraid that you have built up an unrealistic valuation expectation, based on your unique practice of sometimes not depreciating network assets and Mr Isaacs valuation, which did not consider the implications of the 2016 Law."

47. Collas-Crill also claims that paragraphs 14, 58 and 66 of the Draft Determination are being "pejorative with respect to SEL." They are not; I have simply and accurately reported the positions adopted by SEL. For example, Collas-Crill suggests that paragraph 3 of the Draft Determination, which describes my interpretation of Sark Electricity Limited's position that I should not make my own assessment of whether the supply of electricity on Sark is provided in an economic and efficient manner, is incorrect. The claim is contradicted and inconsistent with Collas-Crill's own response to the Draft Determination. In paragraph 2.6.3 they describe how I should decide whether the price currently charged by SEL is, or is not, fair and reasonable. They state that the Commissioner ought to:

    "Take into account SEL's actual business, actual assets and actual costs of generating and distributing the supply of electricity…."

48. In paragraph 1.10.2, Collas-Crill argues:

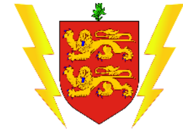
    "At no point does the Law suggest that you should use the "estimated cost" or that you should calculate the "cost of" these costs. In determining whether SEL's prices are fair and reasonable, it is clear that the most reliable indicator is SEL's actual costs."

49. I have, therefore, accurately described SEL's view that I should take SEL's actual costs when deciding whether SEL's prices are, or are not, fair and reasonable. I assume that Collas-Crill was unaware of these contradictions.

50. Collas-Crill complains in 1.16.5 (b) that I *"baselessly insinuate that the legal costs incurred by SEL were as a result of hindering your investigation; and in paragraph 39 in respect of the NDA in which you claim that the fault of one not being agreed rests with SEL".* The history of the NDA concerning WSP, the consulting engineer, and SEL is described below.

51. In order for me to arrive at an estimate of a fair profit, as according to section 13(2)(d), (e) & (f) of the 2016 Law, I required an estimate of the regulated asset value of the equipment used to generate and distribute the supply of electricity. This estimate required an assessment of the investment cost and commissioning dates of the equipment used to generate and distribute SEL's electricity to SEL's customers. SEL claimed not to keep such records, so I instructed an engineer to undertake such an assessment.

52. I wrote to SEL on 21st January explaining that Mr Edwards, of consulting engineers WSP, would be on Sark on 4th February 2019. I asked SEL to assist him and provide him with information concerning the electrical equipment. I also shared a copy of a letter from WSP explaining that, under their confidentiality agreement with my Office, WSP would not release any confidential information. Nevertheless, WSP asked that, should SEL require its own NDA, would they please send it to WSP in advance? Such an NDA was not forthcoming when Mr Edwards arrived on Sark and was only provided at 13.12pm on 4th February. This



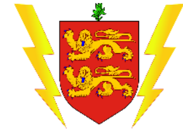
draft NDA attempted to restrict WSP to provide only the replacement cost value of the assets, rather than the regulated asset value (i.e. the replacement cost less the accumulated depreciation). WSP explained why they could not sign this NDA:

"As you will have gathered from your own reading, the NDA is explicit in preventing us from sharing any confidential information with yourself except our own calculated as new asset replacement value (clause 2.1.6 and 2.2). With this agreement in place we would be unable to complete our contractually agreed duties therefore placing ourselves in breach of our own agreement."

53. As a consequence of SEL's insistence on WSP signing an NDA, WSP's investigations were conducted without the opportunity to inspect the power station. Their report was sent to SEL on 12th March 2019. SEL provided some preliminary thoughts on 14th March and sent a formal response on 25th May. By then, the company had decided to undertake its own assessment of commissioning dates and the report was accompanied by a copy of their own assessment of the replacement value and the depreciated replacement value. However, SEL stated that the information could not be shared with WSP unless they signed the NDA. WSP had already explained why they could not sign the NDA with the insistence on replacement costs, as well as what they considered to be an unusual and unreasonable clause on damages.

54. I subsequently discovered inconsistencies between SEL's assessment and the capital expenditure in the audited accounts of SEHL and asked Sark Electricity Limited for an explanation. I also informed SEL that, owing to these inconsistencies, together with data, arithmetical and logical errors, I was unlikely to be able to rely on their work. No explanation has been provided, despite being served a Notice to provide such information under Section 5 of the 2016 Law. On 21st May 2019 and 16th September 2019, I received contradictory emails from Sark Electricity Limited and Collas-Crill, as described in paragraphs 19 and 20 of the main text of this document. Sark Electricity Limited repeated its claims that I have no right to require information about SEHL as it was not relevant to the price control and, in any case, since they were separate legal entities, Sark Electricity Limited had no control over SEHL and could not provide such information. This contradicts the Agreement my Office signed with SEL on 29th November 2019 mentioned in paragraph 21 above.

55. Sark Electricity Limited's refusal to provide this information is a breach of Section 10 and 11(2) of the 2016 Law. Collas-Crill also wrote on 29th August 2019 saying that, perhaps, my suggestion, in January 2019, that Sark Electricity Limited might take comfort from my Office's NDA with Collas-Crill, "may have merit". I did not think it was reasonable for my Office to incur additional costs pursuing the matter further, since SEL was still obstructing the valuation it had agreed to undertake with Chief Pleas by insisting that the valuation had to be made on the basis of replacement costs. (Hansard Chief Pleas Christmas Meeting 16th January 2019, paras 285-325). My judgement has been confirmed by SEL's continuing insistence on restricting valuations to replacement costs, according to Hansard of Chief Pleas 31st October 2019. My statement that Sark Electricity Limited was responsible for WSP being unable to sign the NDA with SEL is correct.



(l) Business model

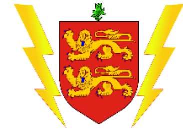
56. It is clear to both SEL and my Office that some new forms of generation can provide electricity at average costs that are lower than the variable costs of the diesel engines employed by SEL. This is supported in SEL's letter to me of 21st September 2019:

> "As long ago as 2013 we had advanced plans to supply Solar Panels to our customers with the company providing the installation and even the financing if necessary. This had to be put on hold because of the aggressive approach of a senior group of Conseillers drove away the man trained to run this program and also made it inadvisable to tie up the company funds necessary to proceed with it.
>
> We have worked with a number of universities and renewable energy developers to bring RE to Sark. We are currently working with two separate groups to bring different forms of RE to Sark. Unfortunately, I have just received another government refusal to cooperate which may cause the most advanced one to pull out.
>
> If you are willing to suggest problem areas that need to be addressed, it would be of enormous help to Sark if you could create a focus on initiating a serious consultation on Renewable Energy planning rules. Specifically, we need to change the planning rules to allow newer, larger scale renewable energy."

57. This was consistent with a letter to customers dated 7th October 2019 which states:-

> "I am keenly aware that this price is unsustainable and that an equitable settlement is urgently needed to avoid a repeat of last November's events. To that end I am planning to convene a "Town Hall" event mid-November to discuss the entire situation and let everyone have their say. At this meeting we hope to also introduce a constructive and forward-looking Sark Green Deal aimed at resolving historic conflicts and transitioning Sark to a low carbon and low-cost energy system. We are particularly interested in complementary funding options capable of accommodating Sark's unique legal environment."

58. SEL offers to buy electricity generated by solar PV panels on its customers roofs for 15 p/kWh and customers are willing to accept this price for their power since it provides them with an acceptable return on their investment. It is therefore clear that, were SEL to build more of this type of generation, the cost of electricity would fall. At some level of intermittent generation from solar PV, there would be a detrimental impact on the operation of the diesel generators, as explained in the Determination of March 2018. To my knowledge, SEL has not carried out the necessary analysis of the local wind regime, solar radiation and demand pattern to establish the optimum strategy to exploit this resource.
59. I am not seeking to change Sark Electricity Limited's business model. Nor am I trying to impose renewable generation on Sark Electricity Limited, as Collas-Crill has alleged. The imposition of renewable electricity targets is a matter for Chief Pleas. I have, however, pointed out to David Gordon-Brown that, if SEL carries on ignoring cheaper forms of generation, and continues to believe that all costs it incurs may be recovered through the electricity tariff, this will encourage customers to go "off-grid". This will cause SEL to lose



business and inflict serious damage on the economy of Sark and the prospects for many of its inhabitants.

Conclusion

60. Collas-Crill's arguments have not demonstrated that the current price of electricity sold by Sark Electricity Limited is fair and reasonable. Furthermore, Collas-Crill has not shown that I have erred in the performance of my duties as Commissioner in my consideration of Sark Electricity Limited's costs and profit margin. I confirm that the current price of electricity is not fair and reasonable.

Anthony White
Commissioner

8 November, 2019