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Mr John Guille
Policy & Finance Committee
c/o Zannette Bougourd
Chasse Marette
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24th November 2021

By email.

Copy to Conseillers

Dear Mr Guille,

I have seen SEL's letter of 18th November, addressed to you. Mr Witney- Price makes a number of allegations against my Office and I thought it might help if I provided you with the following information. Since Mr Witney-Price posted the letter onto the SEL Facebook site, I will circulate this response to Conseillers.

SEL claims that it is losing money and its revenues do not cover the operating costs of the business. This is not the first time SEL has made this allegation, yet it has never substantiated the claim with any supporting evidence, other than by reference to some large legal costs that the company has incurred. These costs exceed the £20,000 annual allowance for legal costs which is used for the purpose of calculating the maximum unit price permitted under the PCO. I take the view that the legal costs over and above the £20,000 allowance are not reasonably recoverable from customers without reasonable justification, which has not been forthcoming from SEL.

Turning to Mr Witney-Price's recent analysis, it is a relatively simple matter to demonstrate why it is in error, as I explain below.

Mr Witney-Price has set out the 2021 budget ("when you take the time to lay it out on paper"). He has calculated, correctly, the revenues I anticipated that SEL would enjoy when I set the Variation in December 2020. At the time, fuel costs for SEL were 35 p/litre, equivalent to 11.9 p/kWh. I estimated that SEL's cost of sales for the year would be £161,179 for island wide and £143,270 for SEL alone. I assumed that SEL's sales would be about 1,200,000 units, so SEL's profits were projected to be £44,500 for 2021, plus receipt of £37,695, representing half of the "under-recovery" of 2020. In other words, SEL's "operating profit" for 2021 was set at about £82,000. I also established the adjustment mechanism, whereby SEL's prices are allowed to vary in line with changes in fuel prices. This ensures that SEL's profits are compensated for movements in fuel prices. Customers will be well aware that the electricity price has been adjusted on a monthly basis.

Mr Witney-Price appears to have erroneously taken the present fuel cost of 17.5 p/kWh and the January unit price of 50 p/kWh in his attempt to repeat my calculations. He should have taken the fuel price at the time I published the Variation, i.e. 11.9 p/kWh. Mr Witney-Price's fuel cost figures in the table for SEL in 2021 are therefore approximately 45% too high. This is not the first time that errors in Mr Witney-Price's calculations have led him to draw an incorrect conclusion. Mr Witney-

Price has also incorrectly assumed that the depreciation charge for 2021 will be the same as in 2020. This is another, albeit smaller, mistake as some assets became fully written off during the year and the charge in 2021 is £3,000 lower. This was all explained in the papers my Office published last year.

Reworking Mr Witney-Price's table, but with the correct fuel and depreciation costs, shows that SEL was projected to make a profit of £25,500 on SEL's projected lower sales estimate of 1,150,000 units, after recovering half of the £75,390 shortfall, i.e. about £62,000 in all. According to SEL's August management accounts, the latest figures I have received, SEL's electricity supply business's profits for January to August 2020 amounted to £48,127 (i.e. all the £37,695 shortfall repayable in 2021 plus a further £10,432) and would have been £68,344 had SEL not given voluntary discounts to "commercial" customers[1]. These discounts were not proposed in SEL's responses to consultation on the Variation last year.

I hope Conseillers will now recognise that if SEL has made a loss, it is not on account of the operation of the PCO but on account of other expenditure, such as the legal costs which I refer to above in excess of the £20,000 annual allowance already incorporated for the purpose of the assessments of the PCO.

Mr Witney-Price's claim "So the truth of the 2021 budget when laid out is:

- There is actually no projected return of 2.2% in 2021
- There is no recovery of half the 2020 shortfall that was promised
- There is in fact a further projected loss to SEL of -£12,177"

is simply not the case.

*Under-recovery*

Mr Witney-Price complains about the under-recovery during 2020. This arose because consumption during 2020 was far lower than assumed when I set the price in December 2019, and the impact on SEL's profits was only partly offset by that arising from lower fuel costs. My forecast was too high on account of SEL providing my Office with incorrect historic consumption figures. Furthermore, SEL failed to engage with my Office when I proposed that prices could be adjusted more frequently in 2020 rather than once annually.

If SEL had engaged with my Office in 2019, a regular price adjustment mechanism, such as we now have, would have been introduced and the large under-recovery would not have existed at the end of the year. In any case, according to SEL's unaudited management accounts for 2020, SEL's operating profit for the year was still £43,782 with the additional £75,390 being held over to 2021/2022. SEL was not operating at a 'rolling loss' as claimed. I recall that Mr Witney-Price wrote to me in November 2020 stating: "*Maintaining profitability at 54p under demand as low as 1,150,000 units is an achievement I am proud of*." SEL's claims that my Office has set a price that requires SEL to operate at a loss is inconsistent with the facts and with this earlier statement.

[1] These figures do not take into account the billing error SEL disclosed in October. Once these are resolved, SEL's profits may be lowered by around £12,000 at most. See SEL's Facebook letter 8/10/2020

*Failure to engage*
SEL's failure to engage with my Office and its customers has caused the company significant problems during the time I have been involved with electricity supply in Sark. Amongst other things this has led, in my view, to:

- The loss of ~10% market share to own generation.
- Legal costs associated with the Moerman case.
- Loss of supply to 19 residents near La Tour.
- The accumulated under-recovery of £75,390 in 2020, though half will be recovered in 2021.

*Capital Expenditure*
When Alan Witney-Price acquired the company in March 2020, he should have been aware of the poor state of the equipment and systems and the 2019 PCO which stated that capital expenditure should be funded by SEL in the first instance and recovered through the electricity price over the period of its lifetime. He should have known that the capital expenditure required far exceeded just one year's depreciation charge. Therefore, the argument that SEL could not invest because the 2020 under-recovery exhausted the depreciation funds is without merit. Mr Witney-Price should not have taken over the company if he did not have sufficient funds to provide and maintain a safe and secure system of supply. A rate of return of 7.5% was offered as an incentive to providing the much-needed improvements. On acquiring the company, Mr Witney-Price stated his intention to introduce "green" technologies and has referred to his "not inconsequential assets" but has not invested in new equipment.

SEL has given a number of reasons why it has not undertaken the urgently required investment in new equipment. These include:

- The inability to mobilise suitably qualified engineers and equipment on account of covid.
- Absence of statutory wayleaves of which he should have been aware when he acquired the company
- Lack of faith in the regulatory regime, and now
- Lack of funds since the depreciation figure was exceeded by the 2020 under-recovery.

My letters to SEL, and its advocates, explain my belief that these are excuses rather than reasons. In my view, a reasonably well managed company would be willing to invest under the terms set out in the PCO. In fact, a number of parties with an interest in providing electricity in Sark have approached me and expressed their willingness to do so. As things stand, without some investment in SEL's plant and equipment, the quality and security of supply is likely to continue to deteriorate.

I believe I have carried out my duties as Commissioner to the best of my abilities and I have tried to be even-handed to both customers and SEL. I must record that I object to SEL claiming that I have set the regulatory framework so as to ensure that SEL operates at a loss. I hope that the above analysis demonstrates that, if SEL were to fail it will not be as a result of the Price Control Order but of poor management.

I would conclude by confirming that as Commissioner I continue to remain available to consider any reasonable proposal that SEL may have for capital investment and generally in relation to its activities.

If Conseillers require any further information or clarification, please do not hesitate to contact me directly.

Yours sincerely,

Anthony White

Commissioner
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