

Licence Modifications - firmus energy

Professional and Legal services in relation to GIS

**Consultation Paper
31 January 2017**



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, proportional, accountable, and targeted.

Be a united team.

Be collaborative and co-operative.

Be professional.

Listen and explain.

Make a difference.

Act with integrity.

Abstract

In our decision paper on the GD17 licence modifications for FE's gas conveyance licence, published on 28 October 2016, we stated that further engagement with FE and consultation was required before a decision could be made in respect of certain costs, referred to as GIS costs (and largely relating to LPS mapping and IT software licensing costs).

We have now decided that it is appropriate to deal with these costs through a licence modification and are now publishing a consultation on a licence modification in relation to the efficient level of costs that should be included within the FE allowances.

Audience

The licensee affected, other regulated companies in the energy industry, government, other statutory bodies and consumer groups with an interest in the energy industry.

Consumer Impact

The proposed costs in this consultation ensure that FE has sufficient allowances to operate its network efficiently and will increase the allowed distribution charges by 0.55%.

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ACRONYMS AND GLOSSARY

CMA	<p>Competition and Markets Authority.</p> <p>The Competition and Markets Authority (CMA) is a non-ministerial government department in the United Kingdom, responsible for strengthening business competition and preventing and reducing anti-competitive activities. The CMA began operating fully on 1 April 2014, when it assumed many of the functions of the previously existing Competition Commission and Office of Fair Trading, which were abolished.</p>
FD	Final Determination
FE	firmus energy (Distribution) Ltd
FOIA	Freedom of Information Act 2000
Gas Order	The Gas (Northern Ireland) Order 1996
GD14	This is the name given to the price control for PNGL and FE covering the period 2014 – 2016 (calendar years).
GD17	This is the name given to the next price control for the NI GDNs. It is proposed to cover the period 2017 – 2022 (calendar years).
GDN	Gas distribution network operator – FE, PNGL and SGN
i.e.	that is
NI	Northern Ireland
Opex	Operating expenditure
PNGL	Phoenix Natural Gas Limited
SGN	SGN Natural Gas Limited
Third Gas Directive	Directive 2009/73/EC of the European Parliament and of the Council of 13 July 2009 concerning common rules for the internal market in natural gas and repealing Directive 2003/55/EC
TRV	Total Regulatory Value: the Depreciated Asset Value plus any incentive adjustments including the profile adjustment.

1 Introduction

Purpose of this Document

- 1.1 With this document we are consulting on a specific licence modification to the gas conveyance licence (the Licence) held by Firmus Energy (Distribution) Ltd (FE).
- 1.2 We (the Authority, also referred to as the Utility Regulator) consider that the licence modifications proposed in this document are, in accordance with our legal and regulatory duties (summarised in the section Legal and Regulatory Framework below), appropriate for the purposes of reflecting and implementing our decision on a specific issue relating to FE's price control for the GD17 period (i.e. 2017 to 2022).
- 1.3 This licence modification consultation paper is presented against the background of a recent consultation and decisions in relation to the GD17 price control, including our final determination¹ and decision on the associated licence modifications (GD17 Decision)².
- 1.4 The GD17 Decision confirmed that we had not made a decision on the allowance to be given for costs relating to professional and legal services associated with certain activities relating to certain IT software licensing and related matters (collectively referred to as "**GIS costs**"), because further engagement with FE and consultation was required before a determination could be made on them.
- 1.5 Having undertaken further engagement with FE, we now consider that it is appropriate to provide an allowance for these costs and accordingly propose a licence modification to the price control conditions of the Licence. We are therefore publishing this consultation on our proposal to modify the Licence in relation to the efficient level of costs that should be included within the FE allowances.
- 1.6 We would also note that FE appealed against elements of the GD17 Decision by submitting a Notice of Appeal (NOA) to the CMA on the 25 November 2016, and has commented on these costs as part of that appeal. Our response to the FE submission was submitted on the 19 January 2017³.

Document Structure

- 1.7 This consultation document is structured in a number of chapters as follows:
 - Chapter 1 'Introduction' provides an overview of the purpose and structure of this consultation document and summarises our approach to making the proposed licence modifications as well as the legal and regulatory background to the proposed licence modifications.

¹ http://www.uregni.gov.uk/publications/2016-09-15_GD17_Final_Determination_-_final

² <https://www.uregni.gov.uk/gd17-licence-modifications>

³ <https://www.gov.uk/cma-cases/energy-licence-modification-appeal-firmus-energy>

- Chapter 2 Professional and Legal Services – in relation to GIS costs is an explanation of how we have derived GIS allowances, considering the most recent information available.
- Chapter 3 Update of Determination Values provides the updated Determination Values that this change will make
- Chapter 4 (Next Steps) provides details on how to submit responses to this consultation document and sets out our proposed timelines for the remainder of the licence modification process.
- An Annex is included to show the changes to the licence.

Approach

- 1.8 In proposing the licence modifications explained in this consultation, we have considered the comments and further information we have received from FE.
- 1.9 We note that the effective date of the licence modifications is to be at least 56 days after the publication of the licence modification decision, in line with the requirements of Article 14(10) of the Gas (Northern Ireland) Order 1996.

Legal and Regulatory Framework

- 1.10 Our principal objective in carrying out our gas functions is to promote the development and maintenance of an efficient, economic and co-ordinated gas industry in Northern Ireland, and to do so consistently with our fulfilment of the objectives set out in the European Gas Directive⁴, and by having regard to a number of matters, as set out more fully in the Energy (Northern Ireland) Order 2003⁵.
- 1.11 In fulfilment of our duties, we may propose to make modifications to gas licences under Article 14 of the Gas (Northern Ireland) Order 1996⁶ (the Gas Order). Article 14 sets out, in particular, the process we need to follow when making licence modifications. We need to give notice of at least 28 days of the proposed modification. We must give due consideration to any representations made during this period and, if we decide to proceed to modify the licence, publish our decision together with the licence modifications, stating the effect of the modifications and the reasons for any changes made from the consultation version. The effective date for the licence modification must be at least 56 days after the publication of the licence modification decision.
- 1.12 Since the coming into effect of the Gas and Electricity Licence Modifications and Appeals Regulations (Northern Ireland) 2015⁷ on 6 February 2015, the consent of the licence holder is not required to a modification to their licence. However, any licence modification decision made under Article 14 of the Gas Order may be appealed to the CMA by:

⁴ Directive 2009/73/EC of the European Parliament and the Council of 13 July concerning common rules for the internal market in natural gas and repealing Directive 2003/55/EC.

⁵ <http://www.legislation.gov.uk/nisi/2003/419/contents>.

⁶ <http://www.legislation.gov.uk/nisi/1996/275/contents>.

⁷ <http://www.legislation.gov.uk/nisr/2015/1/contents/made>.

- the licence holder concerned;
- any other licence holder materially affected by the decision;
- a qualifying body or association representing a licence holder concerned or a licence holder materially affected by the decision; or
- the Consumer Council for Northern Ireland.

1.13 If an appeal is brought to the CMA, the CMA will as a first step decide whether or not to give permission for the appeal to proceed . If permission is granted, the CMA has a period of 4 months, or in the case of licence modifications relating to price controls 6 months, in which to determine the appeal. These timelines can be extended to 5 months and 7 months respectively, if required.

2 Professional and Legal Services – in relation to GIS costs

Overview

- 2.1 The particular category of costs with which this issue is concerned are professional and legal services costs relating to GIS (geographic information systems) support and maintenance, GIS licences, GIS development, software licences for other smaller IT systems, namely FME and FARR, Land and Property Services mapping, and to Landweb fees (collectively referred to as '**GIS costs**').
- 2.2 In the GD17 final determination, an allowance for GIS costs was not included within the opex allowance. This was noted in the GD17 licence modification decision paper⁸ which stated that further engagement and consultation would be required before an efficient allowance on these costs could be determined.
- 2.3 We sent FE an information request in relation to these costs on 19 October 2016 and received a full response on 10 January 2017. We have reviewed the response and all related material and now propose an additional opex allowance to cover GIS costs for the GD17 period of £853k (Dec 2014 prices), pre efficiency.
- 2.4 This chapter details, with consideration of :
- The background to GIS costs in GD17.
 - The proposed GIS allowance.

Background

- 2.5 We did not make a substantive decision on the total allowance for GIS costs within the GD17 Decision. This was because there were certain discrepancies in FE's business plan submissions..
- 2.6 More specifically, in submitting its business plan and supplementary papers in September 2015, FE had allocated GIS costs to one cost-line (customer management – emergency call centre) in its business plan template but its commentary was covered under a different cost line (network maintenance) in a supplementary paper.
- 2.7 One consequence of the discrepancies in the information submitted by FE was that the Final Determination did not propose an allowance for GIS costs either under "network maintenance" or under "customer management".
- 2.8 In its response to the Final Determination, FE queried the absence of a substantive decision on GIS costs. We considered the query and confirmed to FE that that we required further information from FE on its historical reporting of GIS costs (and the cost-

⁸Paragraph 2.16 - 2.18

<https://www.uregni.gov.uk/sites/uregni/files/media-files/2016-10-28%20GD17%20Lic%20Mod%20Consultation%20Decision%20paper%20-%20Final.pdf>

line to which they were allocated in the historical reporting), in order to make a substantive decision on the total allowance to be provided for GIS costs.

- 2.9 We sought that further information from FE on 19 October 2016 but had not received it by the time of making the GD17 Decision and therefore could not make a determination in respect of 'GIS costs' within the GD17 Decision.

Proposed GIS Allowance

- 2.10 Table 1 below provides an extract from the FE Business Plan on its requested allowances for GIS costs

Customer Management (Emergency Call Centre) Legal and Professional Fees	2017	2018	2019	2020	2021	2022	Total
LPS (mapping)	74,945	76,445	77,945	79,445	80,945	82,445	472,170
GIS support and maintenance	60,000	60,000	66,000	66,000	66,000	66,000	384,000
GIS smallworld licenses	7,775	7,775	7,775	7,775	7,930	8,089	47,118
FME software licenses	3,500	3,500	3,500	3,500	3,570	3,641	21,211
FAAR software licenses	2,000	2,000	2,000	2,000	2,040	2,081	12,121
GIS development	16,500	16,500	16,500	16,500	18,150	19,965	104,115
Landweb fees (land ownership)	700	800	900	1,000	1,100	1,200	5,700
Positional improvement (one off)	30,000	30,000	-	-	-	-	60,000
	195,420	197,020	174,620	176,220	179,735	183,421	1,106,435

Table 1 FE Business Plan Submission for GIS Costs

- 2.11 The requested allowances largely reflect ongoing work areas but also include one off costs totalling £60k on 'positional improvement' during the first two years of GD17. In relation to the "positional improvement" FE stated in its Business Plan Submission that a "...Global Navigation Satellite Systems a Positional Improvement project is underway and will continue through GD17...".
- 2.12 We note that FE, in its GD17 Business Plan Submission requested a 38% increase in GIS costs, compared to 2014 actuals (17% when excluding the proposed one off costs). No explanation or rationale for the increase in costs had been included in the Business Plan Submission.
- 2.13 FE provided some information on 28 October 2016 to provide an explanation of the increased costs: *"...and in our submission, an uplift has been applied to actual to reflect the increased workload and size of the system. GIS Development costs will grow in line with network growth and to facilitate internal and regulatory reporting"*.
- 2.14 FE has also provided further analysis on how these costs have broken down in other years as follows:

	2014	2015	2016
	Actual	Actual	Forecast
	£	£	£
LPS	70,260	53,889	56,631
GIS Support and Maintenance	48,000	44,444	50,000
GIS Smallworld Licence	7,775	7,892	7,931
FME Software licences	3,506	3,148	3,416
FAAR Software licences	1,148	1,247	1,346
GIS Development	11,000	15,471	16,000
Landweb fees	500	500	500
	142,188	126,591	135,824

Table 2 FE Actuals/Forecast of GIS

- 2.15 FE also provided a further summary of the 2012 & 2013 Actuals as follows:
- 2012 - £127k
 - 2013 - £137k
- 2.16 Having reviewed the FE information we are satisfied that an allowance for GIS costs is not included through any other cost-line within the GD17 Decision (or indeed within the Final Determination figures) and that an allowance for such costs is appropriate.
- 2.17 Our approach in GD17 has been to generally use 2014 costs as a baseline unless there is strong justification to apply a different allowance.
- 2.18 We have not seen any good reason to depart from this approach and propose to base our allowance on the 2014 costs. We note that the actual costs for 2015 and 2016 are lower than the 2014 actual cost. We also note from the FE submission that the one-off costs for 'Positional Improvement' started in 2015 and continued in 2016 and so will be included in those costs.
- 2.19 We have considered the FE explanation with regard the increase in costs over GD17, but, having considered the evidence of actual costs over several years, have not been persuaded that the increasing size of the system and workload is driving these costs. The growth of the network does not necessarily equate to increasing costs. Given the nature of these costs we would not have expected them to vary significantly with the size of the network, unless there was evidence to the contrary.
- 2.20 We do not view anything in the figures as suggesting a change in our approach of applying 2014 costs is required.
- 2.21 Therefore we propose to provide an allowance within GD17 for GIS costs which is based on 2014 actuals which results in a figure of £853k (Dec 2014 prices). In applying the allowances we take into account the GD17 frontier shift as set out below.
- 2.22 To illustrate, we have provided a year by year allowance in the Table below which also reflects the impact of the frontier shift. This is detailed in Table 25 of the GD17 FD.

Professional and Legal Costs in relation to GIS costs (£k, in Dec 2014 prices)	2017	2018	2019	2020	2021	2022	Total
GD17 Final Determination (pre efficiencies)	142.2	142.2	142.2	142.2	142.2	142.2	853.1
GD17 Final Determination (post efficiencies)	141.8	140.7	139.6	138.7	137.7	136.8	835.3

Table 3 FE Proposed GIS allowances

3 Update of Determination Values

Overview

- 3.1 We had previously indicated to FE that any additional allowance in respect of GIS costs could be provided through the opex uncertainty mechanism. However, FE made a number of comments on the suitability of that mechanism for this particular decision. We have taken FE's comments into consideration and agree that, although the uncertainty mechanism could potentially be used, the better option is to modify the relevant aspects of the price control conditions of the Licence.
- 3.2 Accordingly, we propose to implement our substantive decision on the total allowance for GIS costs over the GD17 period by modifying the Licence.
- 3.3 This chapter details:
- the proposed licence modifications ; and
 - the associated reasons and effects.

Proposed Licence Modifications

FE

- 3.4 We propose to modify Condition 4.7: Current Designated Parameters and Determination Values of the Licence to include the additional values as proposed in Chapter 2.
- 3.5 The Determination Values below, are set on the Average 2014 price base of the FE licence, as opposed to the price base used in GD17 FD, which used December 2014 prices for all GDNs due to the fact that different licences have different price bases. Therefore the figures discussed in Chapter 2 above are in December 2014 prices and need to be adjusted to Average 2014 prices before they are included in the FE licence.
- 3.6 The Designated Parameters do not change, with regard to this proposed licence modification.

Description (for Conveyance Categories i and Formula Years t)	Determination Values		All Values in £(000's) and Indexed to RPI 2014					
			t=2017	t=2018	t=2019	t=2020	t=2021	t=2022
Operating Expenditure	$O_{E,t}$		6,334	6,293	6,446	6,656	6,929	7,205
Cash Flow (calculated in accordance with Condition 4.4.6)	$F_{E,t}$		-5,538	-2,697	-2,163	-1,723	-1,369	-854
Revenue Per Unit	$P_{E,1t}$	$i = 1$	0.4335	0.4335	0.4335	0.4335	0.4335	0.4335
	$P_{E,2t}$	$i = 2$	0.3046	0.3046	0.3046	0.3046	0.3046	0.3046
	$P_{E,3t}$	$i = 3$	0.2730	0.2730	0.2730	0.2730	0.2730	0.2730
	$P_{E,4t}$	$i = 4$	0.2168	0.2168	0.2168	0.2168	0.2168	0.2168
	$P_{E,5t}$	$i = 5$	0.2558	0.2558	0.2558	0.2558	0.2558	0.2558
	$P_{E,6t}$	$i = 6$	0.2324	0.2324	0.2324	0.2324	0.2324	0.2324
Total Conveyance Revenue	$R_{E,t}$		17,818	17,813	18,694	19,624	20,601	21,615
Total Regulatory Value (calculated in accordance with Condition 4.4.8)	$TRV_{E,m}$							202,350

Table 4 – FE Current Determination Values

- 3.7 The above table represents the current Determination Values in Condition 4.7 of the Licence.

Description (for Conveyance Categories i and Formula Years t)	Determination Values		All Values in £(000's) and Indexed to RPI 2014					
			t=2017	t=2018	t=2019	t=2020	t=2021	t=2022
Operating Expenditure	$O_{E,t}$		6,475	6,432	6,584	6,793	7,065	7,340
Cash Flow (calculated in accordance with Condition 4.4.6)	$F_{E,t}$		-5,581	-2,738	-2,199	-1,753	-1,392	-871
Revenue Per Unit	$P_{E,t}$	$i = 1$	0.4359	0.4359	0.4359	0.4359	0.4359	0.4359
	$P_{E,t}$	$i = 2$	0.3062	0.3062	0.3062	0.3062	0.3062	0.3062
	$P_{E,t}$	$i = 3$	0.2745	0.2745	0.2745	0.2745	0.2745	0.2745
	$P_{E,t}$	$i = 4$	0.2180	0.2180	0.2180	0.2180	0.2180	0.2180
	$P_{E,t}$	$i = 5$	0.2572	0.2572	0.2572	0.2572	0.2572	0.2572
	$P_{E,t}$	$i = 6$	0.2336	0.2336	0.2336	0.2336	0.2336	0.2336
Total Conveyance Revenue	$R_{E,t}$		17,915	17,910	18,796	19,732	20,714	21,733
Total Regulatory Value (calculated in accordance with Condition 4.4.8)	$TRV_{E,m}$							202,571

Table 5: FE – Proposed New Determination Values

- 3.8 The table above represents the effect of the proposed licence modifications, in terms of the values changing for the GD17 price control period.
- 3.9 The licence (Annex 1) set out the figures for the full revenue recovery period until 2045

Reasons

- 3.10 The reason for the licence modification is to ensure that FE receives an efficient set of allowances to operate its network functions, including those related to GIS costs.
- 3.11 The reason for modifying the Determination Values is because they form an integral part of the licence formulae which in turn produces a set of revenues and prices which will drive the tariffs set by FE to operate its business.

- 3.12 The Determination Values that are required to change as a consequence of the proposed increased opex allowance are detailed below.

Determination Values	Description (for Conveyance Categories i and Formula Years t)	Document Reference re: Reasons for Proposed Licence Modification
$O_{E,t}$	Operating Expenditure	See chapter 2 above for details of the change.
$F_{E,t}$	Cash Flow (calculated in accordance with Condition 4.4.6)	Changed due to the updated values of the Opex change above
$P_{E,i,t}$	Revenue Per Unit	Output of FE Pi model based on increase in Opex costs above
$R_{E,t}$	Total Conveyance Revenue	Output of FE Pi model based on increase in Opex costs above
$TRV_{E,m}$	Total Regulatory Value (calculated in accordance with Condition 4.4.8)	The TRV has changed due to the updated values of the Opex change above

Table 6: FE – References for Substantiation of Proposed Determination Values

Effects

- 3.13 The changes detailed above will result in a small increase to conveyance charges and enable FE to recover its costs for professional and legal services costs relating to GIS costs.
- 3.14 This proposed increase can be added to the existing PI model⁹ to show the effect of this change.
- 3.15 Should the the proposed modification proceed to be made, it will have the following consequential effect on the existing distribution network tariff:
- 0.55% increase or £0.0024 which is a ¼ of a penny per therm using the distribution domestic tariff (i=1).
- 3.16 The impact on a final domestic bill will be 0.2% increase or £0.95 extra on an annual basis.

⁹ <https://www.uregni.gov.uk/sites/uregni/files/media-files/Annex%2010%20PI%20Models%20-%20FE.xlsm>

4 Next Steps

Submission of Consultation Responses

- 4.1 This is an open consultation paper. We invite stakeholders to express a view on any particular aspect of the paper or any related matter. Responses should be received on or before 12noon on Wednesday 1 March 2017 and should be addressed to:

Paul Harland
Finance and Network Assets
Queens House
14 Queen Street
Belfast
BT1 6ED
Tel: 028 9031 1575

Email: Gas_networks_responses@uregni.gov.uk with cc to paul.harland@uregni.gov.uk

Our preference would be for responses to be submitted by e-mail.

- 4.2 We note that we may make public any responses to this consultation on licence modifications. 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.
- 4.3 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.
- 4.4 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.

This document is available in accessible formats. Please contact Paul Harland on 028 9031 1575 or email: Gas_networks_responses@uregni.gov.uk with cc to paul.harland@uregni.gov.uk to request this.

Timelines

4.5 Table 7 provides an overview of the next steps.

Next Steps	Date
Closure of GIS consultation on proposed licence modifications	1 March 2017

Table 7: Next Steps

Annex

Document	Document Link
Annex 1	FE Licence – Proposed Modifications