



Conclusion of the Utility Regulator's Review of the SSE Airtricity Gas Supply (NI) Ltd Maximum Average Price in Greater Belfast and West Area

April 2022



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, Markets and Networks. The staff team includes economists, engineers, accountants, utility specialists, legal advisors and administration professionals.



Our mission

To protect the short- and long-term interests of consumers of electricity, gas and water.



Our vision

To ensure value and sustainability in energy and water.



Our values

- Be a best practice regulator: transparent, consistent, proportionate, accountable and targeted.
- Be professional – listening, explaining and acting with integrity.
- Be a collaborative, co-operative and learning team.
- Be motivated and empowered to make a difference.



Abstract

Protecting customers is at the heart of the Utility Regulator's (UR) role and ensuring that customers are not over-charged for energy from the price regulated supplier SSE Airtricity Gas Supply (NI) Limited (SSE Airtricity) is a core part of our work.

The UR commenced a review of the maximum average price with SSE Airtricity in January 2022. As per the normal review process, the UR has scrutinised the cost submission provided by SSE Airtricity to ensure that the inputs and calculation were correct and allowable under the price control formula.

Our review confirmed that all the inputs into the tariff model were correct, as were all the calculations. The calculation was carried out at the normal point in time consistent with the agreed timetable, which was shared with the Consumer Council for Northern Ireland and the Department for the Economy. This is also part of the normal process.

The UR has determined that the price increase being implemented by SSE Airtricity is allowable under their licence formula, being within the maximum level generated by the underlying cost drivers – notably wholesale gas cost inputs. However, if the current high level of wholesale prices is sustained it is likely that a further increase will be required in the coming months, although it is uncertain at this time when exactly that will be as market volatility is making it impossible to predict the direction of travel of future prices. Therefore, given the current volatility in the wholesale gas market, the tariff will be kept under constant review and should a further increase be required, SSE will submit another tariff calculation to the UR in due course.

The maximum average price for SSE Airtricity's domestic and small business customers in Greater Belfast will therefore increase to 198.32 pence per therm from 1 April 2022. This equates to an increase of 39% to the bills of all domestic customers and small business customers using less than 2,500 therms per annum. This 39% increase is not the full amount that SSE Airtricity could have increased the tariff by if they had passed through the full increase in the usual way.

SSE Airtricity are the commissioning/default supplier within the West area and as such the UR applies a supply price control to SSE Airtricity in the West area for domestic and small business customers. The review includes the West area in the maximum average price.



Audience

Customers and customer groups, industry and statutory bodies.

Consumer impact

For SSE Airtricity customers in the Greater Belfast area the cost of gas they use will be 39% higher. This change will affect all domestic customers and small business customers using less than 2,500 therms per annum. The change will take effect from 1 April 2022.

The impact of the tariff change on a domestic customer on a standard credit tariff with average consumption of 12,000 kWh per annum will be an increase of £244 per annum (including VAT) on their gas bill.



1. Context

- 1.1 On 7 January 2022 the Utility Regulator (UR), in consultation with SSE Airtricity Gas Supply (NI) Limited (SSE Airtricity), the Department for the Economy (DfE) and the Consumer Council Northern Ireland (CCNI) began a review of the SSE Airtricity maximum average price for domestic and small business customers using less than 2,500 therms per annum. The current maximum average price has been effective from 1 October 2021 and covers approximately 180,000 domestic and small business customers within the Greater Belfast Area.
- 1.2 The UR carries out formal reviews of the SSE Airtricity maximum average price on a bi-annual basis (in advance of April and October). On an ongoing basis the UR analyses the cost of wholesale gas on the forward curve, along with the forward purchases that SSE Airtricity has made to date.
- 1.3 The UR initiated this formal review to ensure customers were not overcharged and to approve the new maximum average price to become effective from 1 April 2022. The review is a formal process agreed by SSE Airtricity and the UR, and includes consultation with DfE and the CCNI. It is set out within the SSE Airtricity¹ price control.
- 1.4 SSE Airtricity uses the maximum average price to set the actual range of tariffs that are charged to customers. The tariffs are calculated on a weighted average basis, based on average usage and the number of customers using each tariff. SSE Airtricity cannot charge more than the maximum average price overall.
- 1.5 From 1 April 2022 the maximum average price for domestic and small business customers will be 198.32 pence per therm; increasing from 142.67 pence per therm in the current tariff which was last set on 1 October 2021. The tariff will be kept under constant review.
- 1.6 From 1 April 2022, the unit rates of tariffs for SSE Airtricity's customers in the Greater Belfast area will increase by 39%. These unit rates are detailed in Table 3 of this paper.

¹ Price Control for SSE Airtricity Gas Supply (NI) Ltd and firmus energy (Supply) Ltd Final Determination 4th November 2019: https://www.uregni.gov.uk/sites/uregni/files/media-files/SSE%20Airtricity%20-%20SPC20%20Final%20Determination_v1.1.pdf



2. Background

- 2.1 In Northern Ireland, there are three distinct distribution areas for natural gas. These are the Greater Belfast area, the Ten Towns area and the West area. Phoenix Natural Gas Limited (PNGL) own and operate the distribution network in the Greater Belfast area, firmus energy (Distribution) Limited own and operate the distribution network in the Ten Towns area while Scotia Gas Networks (SGN) own and operate the distribution network in the West area.
- 2.2 In the Greater Belfast area SSE Airtricity² has operated as the incumbent gas supplier since 1996. Only one competing supplier has been active in the domestic gas market since 2010. SSE Airtricity is still the dominant and commissioning/default supplier in the Greater Belfast area and so the UR applies a price control which covers all domestic customers and small business customers using less than 2,500 therms (73,200 kWh) per annum. The market for business customers using more than 2,500 therms is more competitive and SSE Airtricity are not in a dominant position in that market so there is no price control for that sector.
- 2.3 In the new gas West area, which covers amongst others the areas around Strabane and Enniskillen, SSE Airtricity are the commissioning/default supplier and as such the UR applies a supply price control to SSE Airtricity in the West area for domestic and small business customers³.
- 2.4 Under the terms of SSE Airtricity's licence⁴ to supply gas, the Utility Regulator ("the Authority") has the power to control the maximum amount that SSE Airtricity can charge for gas. This price control is included in SSE Airtricity's licence. Below is an extract from the SSE Airtricity licence:

Control over charges

"The Licensee shall take all reasonable steps to secure that in any Relevant Year the average price per unit of gas supplied by it to Regulated Premises shall not exceed the maximum price calculated in accordance with Condition 2.4.2".

- 2.5 The UR has established a price control determination which sets out SSE Airtricity's allowed costs. The price control determination sets out how each of the costs will be treated in the maximum average price.

² In June 2012, Airtricity Energy Supply (Northern Ireland) Ltd purchased the entire issued share capital of Phoenix Supply Ltd and was subsequently renamed SSE Airtricity Gas Supply (NI) Limited (SSE Airtricity).

³ Connections in the West area have been growing steadily and are currently around 1,700.

⁴ SSE Airtricity Licence for the supply of gas: <https://www.uregni.gov.uk/sites/uregni/files/media-files/2020-10-01%20SSE%20Airtricity%20Gas%20Supply%20NI%20Ltd%20%28PSL%29%20Supply%20Licence.pdf>



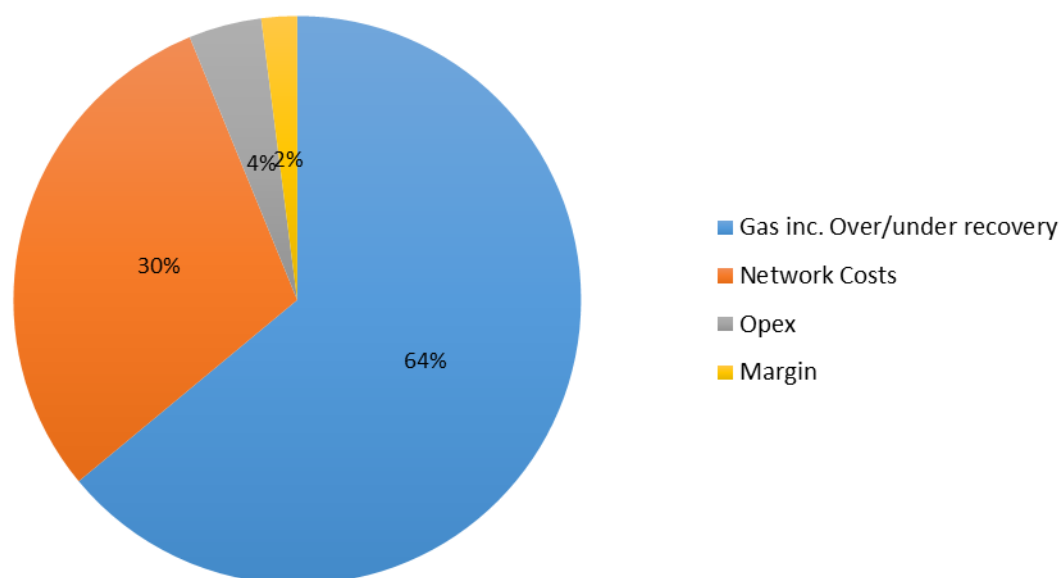
Elements of Maximum Average Price

2.6 The maximum average price is made up of a number of costs:

- Operating costs;
- Supply margin;
- Network costs; and
- Wholesale cost of gas.

2.7 The breakdown is shown in Figure 1 below.

Figure 1 – Makeup of the maximum average price from 1 April 2022



2.8 The UR scrutinises the costs within each of the elements of the maximum average price of SSE Airtricity's submission. SSE Airtricity uses the maximum average price to set the actual tariffs that are charged to customers. SSE Airtricity cannot charge more overall than the maximum average price.

Operating Costs and Supply Margin

2.9 Operating costs are the costs necessary for SSE Airtricity to run its supply business for tariff customers. These costs include the costs of billing, customer service, offices, meter reading, salaries and IT systems etc. The operating costs were determined under the price control carried out by the UR.



- 2.10 The margin refers to the amount of profit SSE Airtricity is allowed to make. The margin is also determined within the price control and is set at 2% of allowable turnover from price regulated customers.
- 2.11 In November 2019 the UR published the final determination for the SSE Airtricity price control⁵ which indicates the total amount of revenue that the Licensee can recover, in any relevant year, in respect of their gas supply businesses.
- 2.12 The price control determination runs from 1 April 2020 to 31 March 2023.

Network Costs

- 2.13 Network costs cover the charges for the use of the Northern Ireland transmission and distribution systems. These charges are reviewed and approved by the UR as part of the network price controls.
- 2.14 The SSE Airtricity price control determined that the transmission and distribution system charges will be treated as pass through charges which means that the customer pays no more or less than the actual cost of the network charges.
- 2.15 The costs for the transmission system are those costs involved in bringing gas from Scotland to Northern Ireland, via the Scotland to Northern Ireland Pipeline, and all the transmission pipelines within Northern Ireland. These costs are published on the [Gas Market Operator NI](#) and [National Grid](#) websites.
- 2.16 The costs for the distribution system are those costs associated with moving gas throughout the Greater Belfast area and the West area to homes and businesses. On the 15th September 2016, the final determination on the price control for Northern Ireland's gas distribution networks for the period 2017-2022 (GD17), and associated licence modifications for consultation, were published. GD17 is the distribution price control for Phoenix Natural Gas Limited (PNGL), firmus energy (Distribution) Limited and SGN Natural Gas Limited which was effective from 1 January 2017⁶. The distribution price control determines the amounts that PNGL can charge for suppliers to use the Greater Belfast or West network. These can be found on [the Phoenix Natural Gas](#) website.

⁵ Price Control for SSE Airtricity Gas Supply (NI) Ltd Final Decision 4th November 2019

https://www.uregni.gov.uk/sites/uregni/files/media-files/SSE%20Airtricity%20-%20SPC20%20Final%20Determination_v1.1.pdf

⁶<https://www.uregni.gov.uk/news-centre/gas-distribution-networks-price-control-gd17-period-2017-2022-published>



Wholesale Gas Costs

- 2.17 As determined within the SSE Airtricity price control, the gas cost element of the maximum average price incorporates the wholesale cost of gas as well as charges for transporting gas through Great Britain and costs for securing credit cover associated with purchasing wholesale gas.
- 2.18 The SSE Airtricity price control determines that gas costs are treated as pass through which means that the customer pays no more or less than the actual cost of gas. Therefore where wholesale gas costs decrease or increase over those set in the tariff, the resulting savings or additional costs are passed on to the customer.
- 2.19 SSE Airtricity has a gas purchasing strategy in place which means that they purchase a percentage of their forecast volumes in advance on an ongoing basis. This is known as hedging and limits the exposure to fluctuations in wholesale gas prices and therefore aims to create more stability in the gas price for final customers. It is important to note that SSE Airtricity's hedging strategy will be specific to it, and due to the specific timing of forward gas purchases the price paid will be different from other suppliers who will purchase different volumes at different time periods (and hence at different prices as the gas market moves on a daily basis). Hence, the overall wholesale cost of gas for SSE Airtricity will likely always differ somewhat from that of other gas suppliers even though they are purchasing from the same gas market.
- 2.20 At the time of review, the overall cost of gas for the maximum average price is estimated based on a combination of actual gas purchases that have already been secured, along with forecast volumes of gas required, and the forecast wholesale cost of that gas which has yet to be bought (based on the gas price forward curve). Buying gas in advance (hedging) can help to reduce any over/under recoveries building up as the price of the hedged gas in the maximum average price is known when the price is set.

Over/Under Recovery from Previous Tariff Periods

- 2.21 Wholesale gas costs make up a large component of the final maximum average price and as these costs can be volatile there will always be a difference between the outturn cost of the wholesale gas that has yet to be purchased compared to the forecast costs that were included when the maximum average price was set.
- 2.22 Where the wholesale gas costs out turn less than was forecast in the



maximum average price, SSE Airtricity will 'over recover'. This means that they recovered more money from customers than they spent on gas costs and they will subsequently refund the over recovered difference to customers in the following tariff period.

- 2.23 Alternatively, where the wholesale gas costs turn out higher than forecast in the maximum average price, SSE Airtricity will 'under recover', the means they spent more on gas costs than they recovered from customers and they will therefore be able to re-charge the under recovered difference to customers in the following tariff period. This ensures that customers only pay for the actual cost of gas.
- 2.24 Therefore, each maximum average price includes an amount of over or under recovery which was accumulated during the previous tariff period.
- 2.25 Both SSE Airtricity and the UR strive to keep the over/under recovered amount as low as possible in order to avoid distortion of the maximum average price. This is carried out through ongoing monitoring and tariff changes being put through when over or under recoveries are accumulating to such an extent that they would adversely affect the tariff.



3. Why is the Maximum Average Price for SSE Airtricity increasing?

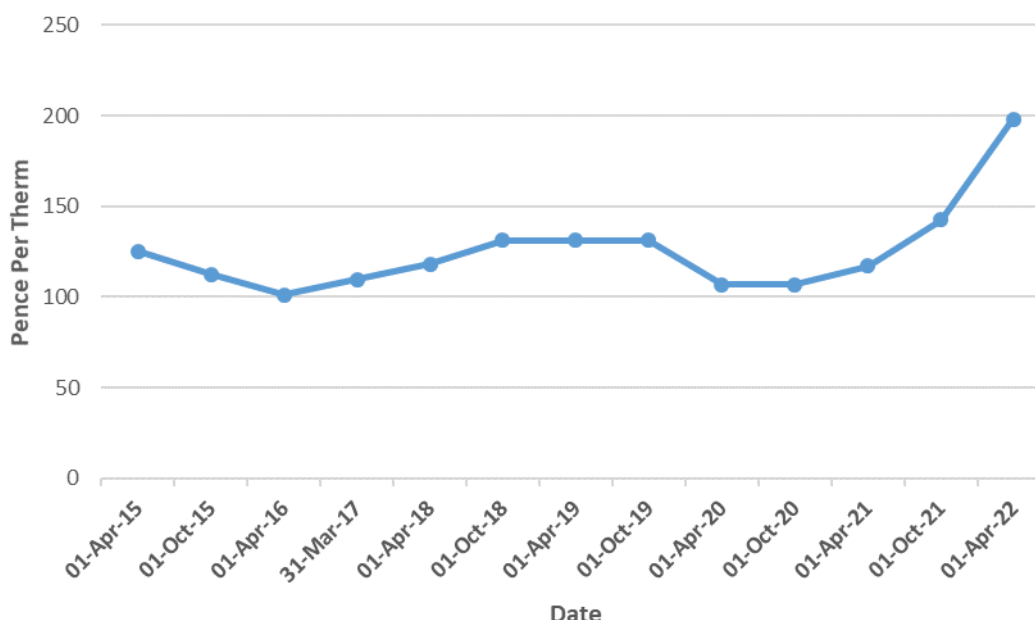
- 3.1 The maximum average price for SSE Airtricity's tariff customers in Greater Belfast and in the West will increase to 198.32 pence per therm from 1 April 2022.
- 3.2 Table 1 below shows the movement in the regulated maximum average price from May 2008 to date.

Table 1 - Historic maximum average price

Effective from date	Approved Maximum Average Price (p/therm)
01-May-08	128
01-Oct-08	152.58
08-Jan-09	118.92
01-Oct-09	96.32
01-May-11	133.97
01-Apr-12	122.64
01-Apr-13	133.26
01-Apr-15	125.17
01-Oct-15	112.5
01-Apr-16	101.01
31-Mar-17	109.63
01-Apr-18	118.25
01-Oct-18	131.17
01-Apr-19	131.17
01-Oct-19	131.17
01-Apr-20	106.67
01-Oct-20	106.67
01-Apr-21	117.15
01-Oct-21	142.67
01-Apr-22	198.32



Figure 2 - Historic maximum average price



- 3.3 The overall increase in the SSE Airtricity tariff is primarily due to the increase in the cost of wholesale gas

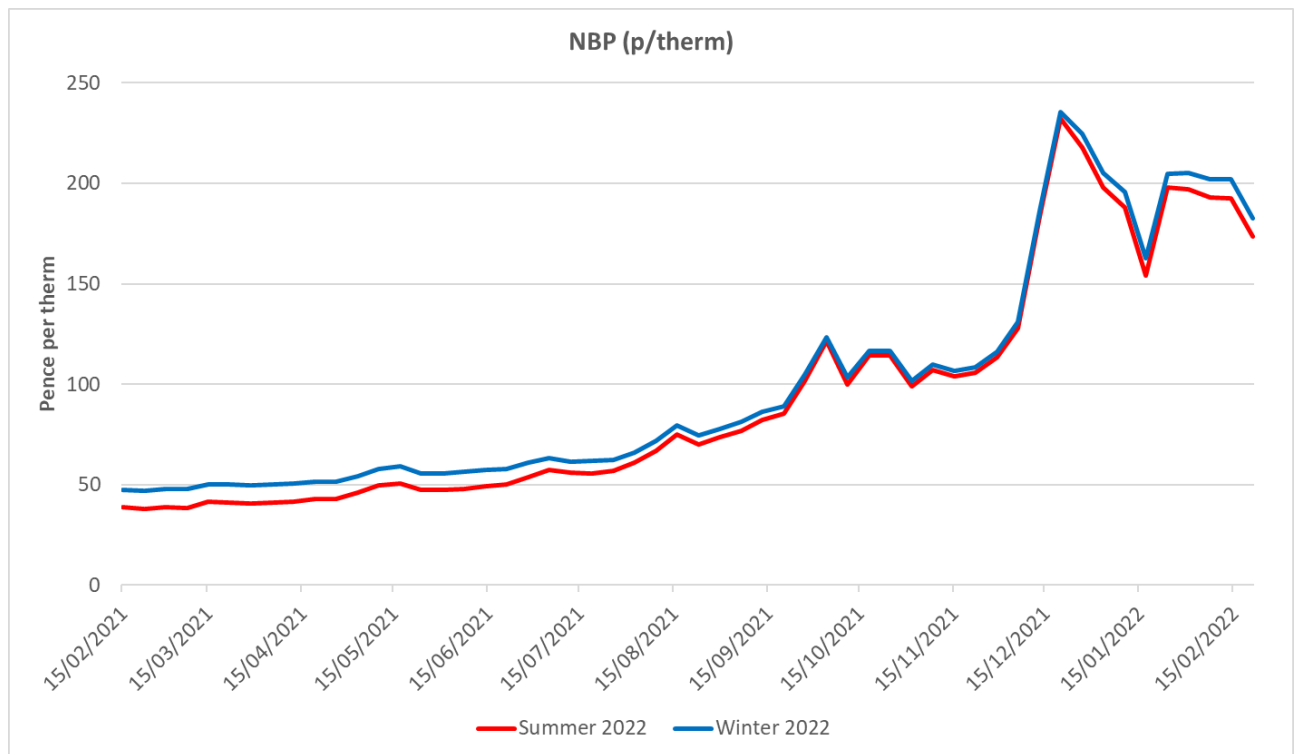
Increase in Forecast Cost of Wholesale Gas

- 3.4 Forecasted gas costs on the forward curve have increased significantly over the last year, as is shown in Figure 3 below. There are a number of factors contributing to the higher prices. This increase in wholesale prices has been caused by a shortage in supply due to a number of factors:

- Russia reducing supply to Europe;
- High Liquefied Natural Gas (LNG) demand in Asia (diverting supply away from Europe);
- European gas storage supplies already depleted from the 2020 winter have not been replenished as quickly as usual due to high summer gas prices;
- High uncertainty about future supplies from Russia due to the conflict in Ukraine



Figure 3 – Movement in forward curve of wholesale gas cost



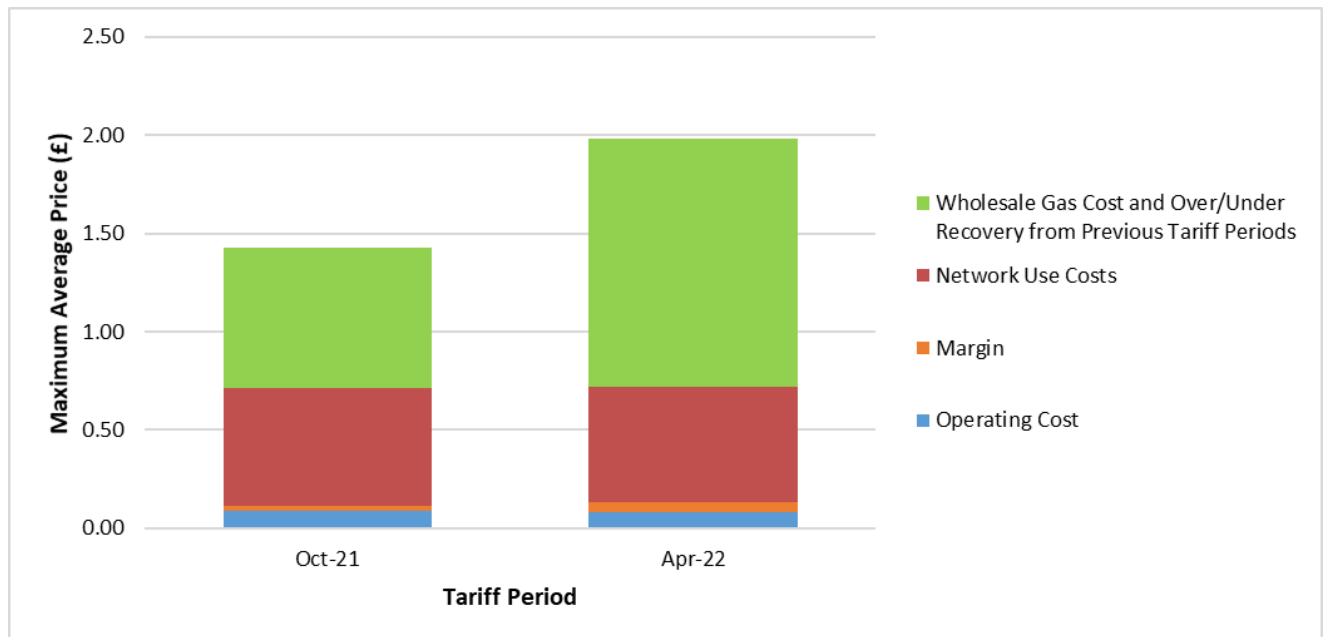
Source: Intercontinental Exchange



4. Breakdown of Maximum Average Price

- 4.1 The graph shown in Figure 4 below compares the breakdown of the April 2022 price with a breakdown of the previous price set in October 2021. As explained previously, the increase in the price is overwhelmingly due to the significant increase in the cost of wholesale gas in 2021 and 2022.

Figure 4 – Breakdown of April 2022 price compared with the previous price



Impact on Tariff

- 4.2 As already stated, SSE Airtricity uses the maximum average price to set the actual tariffs charged to customers. The tariffs are calculated on a weighted average basis, based on average usage and the number of customers on each tariff. SSE Airtricity cannot charge more than the maximum average price overall. From 1 April 2022, the unit rates of tariffs for SSE Airtricity's customers in the Greater Belfast area will increase by 39%.



- 4.3 The new unit rates for tariff customers that will apply from 1 April 2022 are shown in Table 3 below. Table 4 shows the percentage increase for each individual unit rate of the domestic and small business tariffs.

Table 3 – SSE Airtricity’s tariff unit rates from 1 April 2022 (shown in p/kWh including VAT)

SSE Airtricity Gas Supply (NI) Tariffs	Domestic (inc. 5% VAT)	PAYG (inc. 5% VAT)	IC1 (inc. 20% VAT)
Up to 2,000 kWh	9.835	7.155	11.24
Over 2,000 kWh	6.739	7.155	7.702
Over 73,200 kWh	-	-	-
Direct Debit discount	£22.05	-	£22.05

Table 4 – Percentage increase in SSE Airtricity’s tariff unit rates from 1 October 2021

SSE Airtricity Gas Supply (NI) Tariffs	Domestic	PAYG	IC1
Up to 2,000 kWh	39%	39%	39%
Over 2,000 kWh	39%	39%	39%
Over 73,200 kWh	-	-	-

- 4.4 SSE Airtricity’s typical domestic credit bill will rise to £870 per annum⁷ from 1 April 2022. This equates to an increase of around £244 per year compared with the existing tariff.

Comparison with GB and Ireland

- 4.5 Figure 5 below, shows the average annual bill of a domestic customer for SSE Airtricity compared with Bord Gais⁸ in Ireland and the Default Tariff Cap level in GB⁹. The average annual bill amounts in this graph have been calculated based on actual tariff unit rates (including VAT) and are based on an average annual consumption of 12,000kWh.
- 4.6 From 1 April 2022, SSE Airtricity’s tariff will cost the typical domestic credit customer £870 per annum, which is 13% less than the GB Gas Price Cap average and 2.5% less than the Bord Gais standard gas tariff in Ireland.

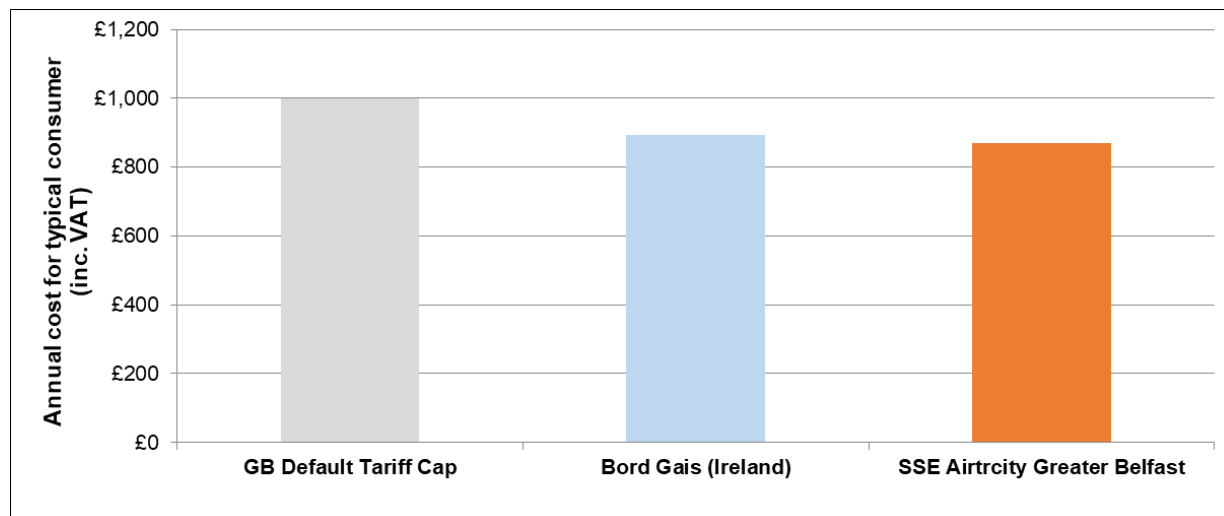
⁷ Based off a typical consumption of 12,000 kWh per annum. Including VAT. Excluding discounts.

⁸ <https://www.bordgaisenergy.ie/home/our-tariffs>

⁹ <https://www.ofgem.gov.uk/publications/default-tariff-cap-level-1-october-2021-31-march-2022>



Figure 5 - Comparison of average annual domestic bills (based on standard domestic credit customers with estimated usage 12,000kWh per annum including VAT)



Conclusion

- 4.7 The UR has reviewed the maximum average price submission provided by SSE Airtricity and reviewed SSE Airtricity's forecasts against its own market analysis. The UR is satisfied that the inputs and calculations in the submission are correct.
- 4.8 The UR has determined that the price increase being implemented by SSE Airtricity is allowable under their licence formula, being within the maximum level generated by the underlying cost drivers – notably Wholesale gas cost inputs
- 4.9 The new SSE tariff will be kept under review and a future change may be required in the coming months. A future change is likely to be a further increase if the current high level of wholesale gas costs is sustained. The UR also retains the flexibility to initiate a review of gas prices at any stage if it is considered to be in the interest of customers.