

Gas Network Extensions Northern Ireland

Gas to the West – Clarifications (1 – 19)

N ^o	Clarification	Utility Regulator Response
1	<p>Applicant Information Pack, section 4.19 and the weighting criteria, and the published criteria for gas licence applications and applications for consent to construct major-pipe-lines, gas storage or LNG facilities, sections 3.17, 3.18 & 3.21</p> <p>Is there a further breakdown of the percentage allocation i.e. Applicant Determined Costs, Operational Business Plan and Innovation and Technology Transfer?</p>	<p>The Published Criteria set out the marking scheme which the Authority is required to following when judging applications.</p> <p>Section 3.14 (b) of the criteria provides the breakdown for application determined costs, operational business plan and innovation and technology transfer. There is no further breakdown.</p>
2	<p>In the workbooks the capital expenditure is three years for transmission and three years for distribution, could the overall programme be considered as six years? If the three years are exceeded in transmission or distribution how will the costs be treated or would there be penalties applied?</p>	<p>The high pressure workbook assumes a capital expenditure period of three years between the award of licence and first commencement date. The low pressure workbook assumes a capital expenditure period of forty years from the first commencement date.</p> <p>These workbooks make these assumptions purely for the purpose of the competition. It is recognised that, in practice capital expenditure on the high pressure network may continue after the first commencement date, and that capital expenditure on the low pressure network may begin before the first commencement date.</p>
3	<p>Conclusions Paper, section 2.41 & 2.42. It is stated operating expenditure costs will not be competed on, and applicants should set out their proposals in the Operational Business Plan. The Operational Business Plan is weighted as 40%; therefore will the Opex costs be assessed under this heading or is it the intention that the successful applicant would undergo an Opex price control process at some point between the award of</p>	<p>Paragraph 2.41 states clearly that operating expenditure will not be considered as part of the application process for the high pressure licence.</p> <p>Paragraph 2.42 relates to a situation where an applicant has indicated that their application has been made assuming an operating cost pass through form of control. In this case the applicant will need to include in ‘other costs’ any costs relating to the establishment of arrangements to ensure that the pass through model cannot be used to the detriment of consumers. Applicants will need to justify these establishment costs in</p>

	the licence and the first operational commencement date, at which point costs will be revealed?	<p>their Operational Business Plan.</p> <p>The process by which operating cost allowances will be established following the grant of licence will be dependent on whether the successful applicant has chosen a ‘revenue cap’ or ‘cost pass through’ form of control with regard to operating costs.</p> <p>Those applicants choosing the ‘revenue cap’ option should expect that operating cost allowances will be determined in advance of the pipeline beginning commercial operations by means of a price control process.</p>
4	In the excel workbook, capital expenditure for construction is hardwired in, does this include construction supervision or is construction supervision to be competed on in the design and project management section?	<p>In the case of the high pressure workbook:</p> <p>All costs of work required by the licence holder to supervise construction including technical or cost assurance, design of the works, management or supervision of the construction contract, vetting the proposals of the contractor or vetting the statements issued by the contractor for payment should be included in the ‘design and project management cost’.</p> <p>As part of the operational business plan, the applicant should include a clear statement of these costs in its application, including quantum, and explain the scope of these services and identify any of these services it plans to procure through another party.</p>
5	Applicant Information Pack, section 4.6 VII, Is it correct the applicant publishes in the newspapers post submission of the application? Is proof of publication required i.e. submission of newspaper notices to the Utility Regulator within 14 days of publication?	<p>Yes, it is correct the applicant publishes in the newspapers post submission of the application.¹</p> <p>Yes, proof of publication is required and a copy of the publication should be sent to the Utility Regulator as soon as is practicable after publication.</p>
6	Applicant Information Pack, section 4.6 V, Bearing in mind the newspapers may publish on different dates, should the	This is not a stipulated requirement. However it would be a sensible approach to publish the notices as close to each other in time as is reasonably practical.

¹ The Gas Order, section 8 (3)
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	newspapers notices appear as reasonably close as practical .i.e. within few days of each other?	
7	<p>Applicant Information Pack, section 4.6 IV,</p> <p>Is there any restriction on email sizes accepted by Utility Regulator?</p> <p>Can softcopies of application be submitted on CD in addition to 3 hardcopies if required?</p>	<p>In order for the application to fall within the deadline both the hard copies and the electronic copy, must have been received by 12.00 noon on Tuesday 6 May 2014. Should an applicant wish to provide an electronic copy of their application on a CD ROM rather than by email, this will be deemed as acceptable by the Utility Regulator.</p> <p>In relation to email sizes, we advise that should these be greater than 50 MB the applicant should discuss this with us in advance so that we might have time to make the necessary arrangements.</p>
8	<p>The following question relates to the capital expenditure special conditions in the high pressure licence.</p> <p>Please can UR confirm the intended application of the pain gain sharing mechanism including:</p> <ul style="list-style-type: none"> • When the setting of capex allowances will take place? • Will these allowances be the final allowances that will be used for the purposes of applying the pain gain sharing mechanism? • Will the contingency figure included in the bidders case be added to any allowable capex or will it be subject to determination as part of allowable capex? • When the process of applying the pain gain sharing mechanism will take place? • How the pain gain sharing mechanism will be implemented including a worked example of how this will be facilitated in practice i.e. demonstrating time periods and costs. 	<p>Paragraph 3.16 of the Applicant Information Pack addresses the timing of setting capital expenditure allowances in the high pressure licence.</p> <p><i>In relation to the timing of the setting of capex allowances we plan to do so after materials have been purchased and after the construction tender has been completed in line with previous high pressure pipelines projects.</i></p> <p>These allowances for controllable capital expenditure will be the final allowances which will be used for the purpose of applying the pain gain mechanism.</p> <p>It is our intention that the contingency costs revealed in the licence application process should as far as is reasonable be reflected in the determination of final allowances.</p> <p>The pain gain mechanism will be applied once the actual level of controllable capital expenditure incurred has been verified and either approved or determined by us.</p> <p>In paragraph 3.13 of the application information pack we stated that “The sharing factor will be 35 % and symmetrical, i.e. if the licensee under spends they will give 35% of the under spend</p>

		<p><i>back, and customers will underwrite 35% of any overspend."</i></p> <p>We now wish to correct this statement as it is not based on the GB standard. The corrected last line of paragraph 3.13 should read <i>"The sharing factor will be 35%/65% for example - if the licensee under spends they will give 65% of the under spend back, and customers will underwrite 65% of any overspend."</i></p> <p>For example if the controllable capital allowance is set at £100 but the verified actual controllable capital expenditure is £110 then the licence holder will have their final controllable capital allowance adjusted to £106.50. If however the verified actual controllable capital expenditure is £90 then the licence holder will have their final controllable capital allowance adjusted to £93.50. These adjustments will not be subject to any later rolling mechanism.</p>
9	Is there any deadline beyond which questions of clarification will not be answered?	The deadline for receipt of clarification questions will be 12.00 noon on Monday 7 April 2014. This will ensure that all applicants have time to fully consider the responses provided by the Utility Regulator.
10	In the excel workbook, capital expenditure for wayleaves is hardwired in, does this include the administration of the wayleave, i.e. preparation of the wayleave pack, discussions with landowners etc or is wayleave administration to be competed on in the design and project management section?	<p>For the high pressure workbook</p> <p>None of the administrative costs identified in the question should be included in Design and Project Management costs.</p>
11	Security arrangements for Above Ground Installations (AGI), are these to be similar to existing AGI's i.e. electric fences, security cameras etc, or are lighter security arrangements required? Please advise as different levels security will require different levels	<p>For the high pressure licence</p> <p>The security arrangements will need to be established in the usual manner in accordance with all applicable statutory requirements and/or the advice of the competent authorities. It is not the role of the Authority to advise on the nature of the arrangements needed to comply with the</p>

	<p>of design.</p> <p>Will security arrangements be pass through on construction, and design to form part of competition?</p>	<p>requirements/advice.</p> <p>Security-related capital expenditure costs will be classified as a Controllable Capital cost and will be treated as such.</p>
12	<p>In relation to uncontrollable Opex (Sec. 3.21 of Applicant Info Pack), NIAUR states that the licence holder must demonstrate that there has been an “adequate challenge” on business rate assessments to justify. It is normal good commercial practice to seek efficiencies in this area by getting independent valuation and arguing the case with relevant authority. Can NIAUR confirm if this practice would be “adequate challenge” and if not can NIAUR specify what further activities would be required?</p>	<p>The methods that may be used in order to negotiate the most efficient price with the relevant authority will be a matter for the licence holder.</p> <p>The Authority does not propose to state in advance a set of actions that would constitute “adequate challenge” in all cases. It would be for the licence holder to take the appropriate steps and then to demonstrate to the Authority that they were in fact “adequate” in all of the circumstances.</p> <p>Whether this was considered to be the case may depend in part on the outcome that is seen to have been achieved – i.e. whether the business rate assessments appear realistic and efficient.</p>
13	<p>In Annex 7, there is an item <i>costs of establishing arrangements to protect customers from inappropriate behaviour</i> in the “Other Costs” item of the Workbook. How will measures/arrangement to protect customers be evaluated as part of the licence award process and how would this be regulated into the future for a company operating on the basis of operating cost pass through.</p>	<p>For the high pressure licence</p> <p>It is for each applicant to set out what arrangements it intends to put in place to achieve this objective. More detailed discussion can be found in paragraphs 3.25 and 3.26 of the Applicant Information Pack</p> <p>The proposed arrangements will be judged against the Published Criteria in particular those set out in paragraph 3.17 (a) and (c)</p> <p>Should an applicant be awarded the licence the regulatory regime, including the licence conditions, will reflect and require the fulfilment of the proposed arrangements.</p>
14	<p>In section 3.29 of the Info. Pack NIAUR states that the WACC will equal, as far as reasonable, the costs revealed by the competitive process particularly for the first price control period. Subsequently, at future</p>	<p>In the high pressure licence</p> <p>The licence holder may request that the cost of capital is locked in. However, whether this request was granted, and the level at and length of time for which it was granted, would be</p>

	<p>reviews the cost of capital will be set using CAPM. How will this review apply where an applicant has chosen to the option to fix cost of capital for a longer period of time? Can the costs be reviewed and if so what would be involved in this review.</p>	<p>determined by the Authority exercising its discretion in accordance with its statutory duties. The Authority would take into account all of the relevant circumstances, and all of the information available to it, at the time of making its decision.</p> <p>As stated in paragraph 3.28 of the Applicant Information Pack, any locking in of the cost of capital would avoid the need for this cost to be included in periodic reviews.</p> <p>Once locked, cost of capital would not be reviewed until the conclusion of the locked in period.</p>
15	<p>NIAUR indicate that the normal price review period is 5 years but that this will be flexible within the licence. Can NIAUR clarify under what circumstances will this “flexibility” be operated and what other time frames might be envisaged? How would this review tie in with existing Price Control/Shadow Price controls for the existing licences?</p>	<p>At each periodic review the Authority will, as part of its overall determination, stipulate the date of the next review. This would be a matter for the discretion of the Authority, in accordance with its statutory duties, taking into account all of the relevant circumstances, and all of the information available to it, at the time of the determination.</p> <p>In making this determination a wide range of factors will be considered, including (in particular) developing best regulatory practice and any need to align periodic reviews across licence holders controlling similar classes of network asset.</p>
16	<p>At what stage in the application process will the Applications be considered binding on the Applicants? Is this once a preferred applicant is identified or upon award/execution of the licence.</p>	<p>Applicants should assume that they will be required to deliver on any and all commitments made as part of their application. The Authority will evaluate applications based on the information provided to it, and therefore expects that commitments will only be made within an application if an applicant is willing to be bound by them.</p> <p>However, this necessarily assumes the case of an applicant which proceeds with its application. No person is obliged to participate in the application process, and any applicant may withdraw from the process at any point up to the time at which a licence is granted by the Authority.</p>
17	<p>Can NIAUR confirm that there will no changes to the ‘published criteria’</p>	<p>The Published Criteria are set by the Department of Enterprise Trade & Investment (DETI) rather</p>

	during the licence competition phase?	<p>than by the Authority.</p> <p>However, the Authority understands that DETI confirms that the Published Criteria will not be amended during the process.</p>
18	<p>The application requires that a WACC should be bid for the 40 years of the licence. Can NIAUR confirm if any element of the WACC (e.g. Gearing and Return on Equity) will be written into the licence for the full duration of the licence? If not can NIAUR indicate the minimum time period for which the “tender WACC” would remain unchanged in the licence.</p>	<p>The Authority has not set out any proposals to write elements of the WACC into the licence.</p> <p>The Authority has not set out a minimum period for which the “tender WACC” would apply. As set out in the Applicant Information Pack, for both the high pressure licence (para 3.29) and the low pressure licence (para 3.59):</p> <p><i>‘It is our intention that the cost of capital will equal as far as reasonable the costs revealed by the competitive process. This will particularly apply in the first price control period. In setting the cost of capital at future reviews we would expect to apply the CAPM model’</i></p> <p>In making future determinations the Authority will take account of the capital structure revealed in the licence application process and whether it remains appropriate. In addition the Authority will consider the level of risk, how market conditions may have changed over time, and all other relevant circumstances.</p> <p>The Capital Asset Pricing Model will be one of a number of tools available to the Authority that is likely to have some use in making these various assessments.</p>
19	<p>Who is the cheque for the fee made out to?</p> <p>Is VAT to be included?</p>	<p>The cheque should be made out to ‘Northern Ireland Authority for Utility Regulation’.</p> <p>VAT is <u>NOT</u> to be included.</p>