

# **Licence Modification Decisions on Professional and Legal services in relation to GIS for firmus energy**

**Decision Paper  
24 March 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 decided that it was appropriate to deal with these costs through a licence modification and on 31 January 2017 we published a consultation on the proposed licence modifications.

We are now publishing our decision paper on the GD17 licence modifications for GIS costs.

## 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 costs in this decision 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

CCNI	The Consumer Council
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
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
TRV	Total Regulatory Value: the Depreciated Asset Value plus any incentive adjustments including the profile adjustment.
UR	Northern Ireland Authority for Utility Regulation (also referred to as the Utility Regulator, or the Authority)

# 1 Introduction

## Purpose of this Document

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- 1.1 This paper sets out our decision in relation to specific licence modifications 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 (UR)) consider that the licence modifications 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 decision is presented against the background of a recent consultation and decisions in relation to the GD17 price control, including our Final Determination<sup>1</sup>, on which we consulted, and the subsequent decision on the licence modifications to be made in respect of the GD17 period (GD17 Decision)<sup>2</sup>.
- 1.4 The GD17 Decision stated that we were not able at that time to make a decision on the allowance to be given for costs relating to professional and legal services associated with certain IT software licensing and related matters (collectively referred to as "**GIS costs**"), because further information from FE and consultation was required before a determination could be made in respect of those costs.
- 1.5 Having undertaken further engagement with FE, we now consider that we are in a position to make a decision in relation to the GIS costs, and to set an allowance in respect of them.
- 1.6 The purpose of this paper is therefore to set out our decision in relation to the GIS costs, and the specific licence modifications to the licence that are necessary to give effect to that decision. This paper includes details on the process that we have followed prior to making the decision.
- 1.7 We note that FE appealed against elements of the GD17 Decision by submitting a Notice of Appeal to the Competition and Markets Authority (CMA) on the 25 November 2016. As part of that appeal it has challenged the fact that no allowance was given for the GIS costs in the GD17 Decision, which it claims was an 'oversight'. Our response to this claim, which was submitted on the 19 January 2017<sup>3</sup>, was that there was no oversight, that we made it clear in the GD17 Decision that we were yet to be in a position to make a decision on the GIS costs and would do so later, and therefore that the appeal in relation to the GIS costs was premature. The submissions in this appeal can be found on the CMA's website.

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<sup>1</sup> <https://www.uregni.gov.uk/news-centre/gas-distribution-networks-price-control-gd17-period-2017-2022-published>

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

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

## Document Structure

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- 1.8 This decision paper is structured in a number of chapters as follows:
- Chapter 1 – Introduction: provides an overview of the purpose and structure of this decision document and summarises our approach to making the licence modifications as well as the legal and regulatory background to the licence modifications.
  - Chapter 2 – Professional and Legal Services - in relation to GIS costs: provides an explanation of how we have reached a decision on the GIS allowances, including consideration of the consultation responses in reaching our decision.
  - Chapter 3 – Update of Determination Values: provides the updated Determination Values that this decision will make.
  - Chapter 4 – Next Steps: outlines the timelines for the remainder of the licence modification process
  - The Annexes include copies of the consultation responses, the Licence showing the modifications being made as tracked changes, the updated PI model and the legislative notice for the licence modifications.

## Approach

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- 1.9 On 31 January 2017 we published a consultation<sup>4</sup> proposing a licence modification to the price control conditions of the Licence, with regard to the Professional and Legal costs referred to as the GIS costs.
- 1.10 Our consultation concluded on 1 March 2017. We received two responses from FE and the Consumer Council (CCNI). Their respective responses are available in Annex 1 and Annex 2 to this paper.
- 1.11 We have carefully considered the responses received from FE and CCNI.
- 1.12 Having considered the responses we have reached a decision on the licence modifications relating to GIS costs. We have set out our consideration of the consultation responses along with our decisions in Chapter 2 of this paper.
- 1.13 In line with the requirements of Article 14(10) of the Gas (Northern Ireland) Order 1996, the effective date of the licence modifications set out in this paper is 22 May 2017.

## Legal and Regulatory Framework

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- 1.14 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

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<sup>4</sup> <https://www.uregni.gov.uk/sites/uregni/files/consultations/2017-1-31%20Licence%20%20Consultation%20-%20FE%20Legal%20and%20Professional%20%20re%20%20GIS%20Costs%20-%20Final.pdf>

European Gas Directive<sup>5</sup>, and by having regard to a number of matters, as set out more fully in the Energy (Northern Ireland) Order 2003<sup>6</sup>.

- 1.15 In fulfilment of our duties, we may propose to make modifications to gas licences under Article 14 of the Gas (Northern Ireland) Order 1996<sup>7</sup> (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 for consultation purposes. 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.
- 1.16 Since the coming into effect of the Gas and Electricity Licence Modifications and Appeals Regulations (Northern Ireland) 2015<sup>8</sup> 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:
- 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.
- 1.17 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 6 months in which to determine the appeal. These timelines can be extended to 7 months if required.

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<sup>5</sup> 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.

<sup>6</sup> <http://www.legislation.gov.uk/nisi/2003/419/contents>.

<sup>7</sup> <http://www.legislation.gov.uk/nisi/1996/275/contents>.

<sup>8</sup> <http://www.legislation.gov.uk/nisr/2015/1/contents/made>.



# 2 Professional and Legal Services – in relation to GIS costs

## Overview

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- 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 licence modification decision paper<sup>9</sup> we stated that a decision had not yet been made on these costs and further information 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.
- 2.4 This chapter details:
  - the background to GIS costs in GD17;
  - consultation responses received and the UR's consideration of the responses in formulating our decision;
  - the decision on GIS costs.

## Background

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- 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-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.

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<sup>9</sup> Paragraph 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>

- 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.

## Summary of UR's proposals in consultation

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- 2.10 After receiving a full response from FE on the queries relating to GIS costs, we published a consultation which proposed to grant allowances to FE in relation to GIS costs for the GD17 price control period. It also consulted on a licence modification to the price control conditions of the Licence held by FE in order to reflect this allowance.
- 2.11 The consultation paper highlighted that the UR had reviewed the information provided by FE and was satisfied that an allowance for GIS costs was not included through any other cost-line within the GD17 Decision and that an allowance for such costs was appropriate.
- 2.12 We noted in the consultation paper that the approach in GD17 has been to generally use 2014 costs as a baseline unless there is justification to apply a different allowance. The consultation stated that the UR had not seen any good reason to depart from this approach for GIS costs and noted that the actual costs for 2015 and 2016 were in fact lower than the 2014 actual costs.
- 2.13 The consultation paper proposed an allowance within GD17 for GIS costs which was based on 2014 actuals. This resulted in proposed costs of £853k (Dec 2014 prices) and we noted that in applying the allowances we would take into account the GD17 frontier shift.

## Consultation Responses and the UR's Consideration of Responses

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- 2.14 We received two responses to the consultation paper, from FE and CCNI.

### FE Response

- 2.15 FE disagrees with the £853,000 (pre-efficiency) allowance for GIS costs proposed in the consultation paper as FE's view is that £1.11 million is necessary for the GD17 period. FE has made a number of points in its response to this regard and we have included the main points made by FE in this section.
- 2.16 FE claims that the GIS costs that it submitted in its GD17 Business Plan Submission (in September 2015) were not challenged by UR in the GD17 Draft Determination<sup>10</sup> as they were 'granted' in full in the Draft Determination.
- 2.17 FE claims that system mapping is related to network growth. FE replicates some detail from its Business Plan Submission which attempts to justify the increased costs for LPS mapping, GIS Support, GIS Development and Positional improvement (one-off cost). With the exception of the Positional improvements costs FE claim that its expectation is that as the network grows and the workload increases the costs will increase.

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<sup>10</sup> <https://www.uregni.gov.uk/consultations/draft-determination-gas-distribution-network-operators-gd17-published-consultation>

- 2.18 FE states that the UR has changed its approach from the GD17 Final Determination which recognised GIS costs, software licences and fees for base maps as ‘fixed costs’.
- 2.19 FE explains that its 2015 and 2016 actual costs were lower than the 2014 actual costs as it purchased new maps for network planning during 2014 which were subsequently not needed. It explains that this was because gas mains were not laid by FE in those areas and renewal of these maps was not required in 2015 and 2016. FE claims that this situation will not occur again during the GD17 period.
- 2.20 FE states that while it has been working on Positional Improvement for the last number of years it has not incurred any consultant costs on this yet and plans to contract with consultants later in 2017 and continue into 2018.
- 2.21 FE makes comments that the question of GIS costs, which has been referred to the CMA, should only be decided by the CMA<sup>11</sup> and we should have no further role in this process. FE also argues that it would be grossly unfair, costly and inefficient if FE was required to re-apply to the CMA for permission to appeal a new decision by the UR on GIS costs.

### CCNI Response

- 2.22 In CCNI’s response they recognised the importance of FE having sufficient allowances to operate its network effectively; however they noted that they would expect a detailed explanation or rationale from a company seeking an uplift in costs.
- 2.23 They agree with the UR’s view that network growth does not necessarily equate to increased costs and they agree with the application of the frontier shift as it is consistent with the GD17 approach.

### UR Consideration of Responses

- 2.24 We have carefully considered the comments received in the responses and we have set out our considerations in relation to each of the points.

### **FE position on the proposed allowance for GIS costs**

- 2.25 The GD17 Draft Determination was clearly a set of proposed costs that would be subject to change as a result of consultation and further evidence. Indeed a number of changes were subsequently made that were in FE’s favour, and the overall impact of the changes since the Draft Determination was a significant increase to FE’s allowances. The decision we are making in this paper is based on updated information and is fully explained below. We do consider that an allowance for GIS costs is necessary, but we disagree with FE on the level of increases required by it as against its actual GIS costs in 2014.
- 2.26 In its consultation response, FE makes reference to its GD17 Business Plan submission and summarises that submission to explain why FE expects GIS costs to increase from GD14 levels. The summary is based on four cost areas: LPS mapping, GIS support, GIS development and Positional improvement. These points are considered below.

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<sup>11</sup> As noted in paragraph 1.7 of this paper, FE appealed against elements of the GD17 Decision by submitting a Notice of Appeal (NOA) to the CMA on 25 November 2016 and has commented on GIS costs as part of that appeal.

- 2.27 We note that FE's business plan submission also included other cost categories under GIS costs for Licences and LandWeb fees. In its business plan submission FE stated that it expects the costs for Licences to be in line with inflation with an increase in 2021 and 2022 for costs associated with above inflation rises. However it does not explain why the increases in 2021 and 2022 would be above inflation; nor does it explain why it has forecast a substantial increase in the costs for FAAR Software Licences in 2017 compared to the costs during the GD14 period.
- 2.28 For LandWeb fees, FE explained in its business plan submission that the current annual cost was £500 but this was expected to increase as customer numbers increased. FE's costs for LandWeb fees were £500 in each year of the GD14 period despite customer numbers increasing during this time and FE did not explain why the basis for the costs would change during the GD17 period.
- 2.29 We will now consider the individual points raised in the consultation.

### **LPS Mapping**

- 2.30 With regard to LPS Mapping FE indicates that as the network grows, an increasing amount of maps (or tiles) are needed which it quantifies as a £1.5k increase per annum. The UR noted in its consultation that 2014 costs were significantly higher than 2015 and 2016 and overall there was no evidence of increasing costs. FE explains this by stating that 2014 costs are driven by the fact that it bought maps in 2014 which it did not need.
- 2.31 Indeed in terms of the appropriateness of using 2014 costs as a basis for setting GD17 costs the FE evidence points to the fact that elements of its spend in 2014 were inefficient, and therefore using 2014 costs as the basis for setting GD17 allowances could be considered to be generous in this respect.

### **GIS Support**

- 2.32 With regard to GIS support, this would appear largely to consist of costs relating to routine maintenance and support of FE's GIS system. This could be considered business as usual and general operation of the systems. FE indicates that costs are expected to increase based on workload, but we have seen no evidence sufficient for us to conclude that this linkage exists or that the magnitude of the increase that has been requested is justified. We note that the 2014 costs for GIS support were higher than the costs incurred during 2015.

### **GIS Development**

- 2.33 FE has requested an allowance for a consultant to continue to develop the system over and above routine maintenance and support. FE has indicated that, as the network and customer base grows, GIS will be used increasingly for reports and to improve processes; it also requested an increase in 2021 and 2022 due to changes in reports and information required for the GD23 price control process. As the system is already well-established, and given the unknown nature of this type of work, we view the 2014 levels of expenditure as appropriate.

### **Positional Improvement**

- 2.34 FE's requested costs on Positional Improvement are driven by the Positional Improvement project undertaken by OSNI to redress inconsistencies between existing mapping and the new Global Navigation Satellite Systems (GNSS) based surveys. FE

notes that it needs to carry out work to move data to the newly corrected POST Positional Improvement format.

- 2.35 This change has impacted on all utilities and FE has been managing this for the last four years. We note FE's comments on the importance of the positional improvement work to manage its network e.g. emergency response. However, we also note that FE has been working without this project for four years and there is no evidence that this has had an adverse effect on its ability to act as a prudent operator. Furthermore we note that other GDNs have not requested such funds in GD17 and yet have continued to operate their networks in line with their obligations.

### **General**

- 2.36 Overall, FE has requested a significant increase in GIS costs for the GD17 period when compared with its actual expenditure in the GD14 period. When faced with a request of this nature we would expect to see a clear justification from the company as to the reasons for the increase. FE has not provided such a justification.
- 2.37 FE claims that we have not explained why its justification has been rejected, but this is because it is inadequate, largely consisting of a series of descriptions of what falls within the GIS costs, which either have no clear link to the costs being requested, or are not supported by evidence that those costs will be what is claimed.
- 2.38 We note that FE makes reference to a change in position from the Final Determination (FD), whereby costs were stated as 'fixed costs'. To set the context of this statement, this was made in the Draft Determination and after evaluating all the relevant facts, have now moved this area to "IT and Telecoms", which is the appropriate location for this type of cost.
- 2.39 FE's claims that GIS costs will increase as the network and workload increases, have not been evidenced by FE's historic costs. On reviewing the actual costs over the 2012-2016 period, with the level of activity, the number of customer connections has doubled, along with expansion of the network by over 250km of pipeline; yet the GIS costs have not shown substantial increases and show evidence of going up and down over the years with 2014 being the year with the highest costs.
- 2.40 Having looked at the individual cost lines and also considered the overall GIS package of costs, we conclude that the 2014 actual costs (£142k) is a reasonable basis for setting the GD17 allowance and there is no justification to apply a different approach.
- 2.41 We note that CCNI disagree with FE's view that the costs should will increase with network growth and they would expect detailed rationale from FE for an uplift in costs.

### **Issues in Dispute before the CMA and steps for dealing with them**

- 2.42 In relation to FE's view that it is inappropriate for the UR to make licence modifications outside the CMA appeal, it is clear that our Decision Paper<sup>12</sup> on 28 October 2016 did not incorporate a decision in relation to GIS costs for FE. On the contrary, the Decision Paper states "we will continue to engage with FE on these costs for GD17 and will make a determination...". A decision therefore still requires to be made, and it is appropriate for the UR to continue with this licence modification process in order to make the determination on GIS costs for FE. We note also that when the CMA gave permission to

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<sup>12</sup> <https://www.uregni.gov.uk/sites/uregni/files/media-files/2016-10-28%20GD17%20Lic%20Mod%20Consultation%20Decision%20paper%20-%20Final.pdf>

FE's appeal, it was only agreeing to consider FE's arguments that GIS costs were appealable, not to accept them. In our view, FE's appeal on these costs was premature.

- 2.43 FE has claimed that it would be unfair and costly if it was required to re-apply to the CMA to appeal this separate decision on GIS costs. The UR notes that the rules for appeals to the CMA are set out in legislation, but in any event that there is sufficient time for FE to appeal this decision and for that appeal to be consolidated into the appeal which is already ongoing. The UR does not encourage this outcome, but it is a right available to FE, and it does not need to be a costly or onerous process.
- 2.44 Having considered the responses as set out above we have set out our final decision in relation to GIS costs for FE below.

## Decision on GIS Allowance

- 2.45 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**

- 2.46 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...".
- 2.47 FE has also provided further analysis on how these costs have been 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**

- 2.48 FE also provided a further summary of the 2012 & 2013 Actuals as follows:
- 2012 - £127k
  - 2013 - £137k
- 2.49 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.
- 2.50 FE's GD17 Business Plan Submission requested a 38% increase in GIS costs, compared to 2014 actuals (17% when excluding the proposed one off costs). FE claims that the increases are expected as these costs will increase as the network grows and workload increases.
- 2.51 In GD17 our approach was to generally use 2014 costs as a baseline unless there was a strong justification to apply a different allowance. We have considered the evidence of whether 2014 is an appropriate year to use for GIS costs.
- 2.52 As explained previously in this paper, FE's expectation of the cost increases has not been evidenced by their historic costs. The lack of evidence of a strong link with network/customer growth is clear when one looks at the actual costs incurred between 2012 and 2015 and the forecast costs for 2016. 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, and there has been no evidence to the contrary.
- 2.53 In terms of the appropriateness of using 2014 we have also considered the fact that the 2014 cost includes inefficient spend and the request for FE to receive an additional allowance for Positional Improvement.
- 2.54 The inefficiency in 2014 is of the magnitude of £16k per annum or £96k over GD17. The request for Positional Improvement allowance is £60k over GD17.
- 2.55 However we would highlight that in using 2014 actuals it is important not to seek to be overly precise in making adjustments for the fact that 2014 might be an atypical year. We do not find the two issues above to be material enough to justify an adjustment to 2014. There may be some level of headroom built into the 2014 figure because of the inefficient purchase of maps in 2014. Likewise there may be additional relatively small

projects which FE will progress in GD17. However we remain of the view that, based on the evidence provided there is no need to change from our approach of applying 2014 actual costs to apply in GD17.

- 2.56 Therefore our final decision is that for the GD17 period, we will provide an allowance to FE for GIS costs based on 2014 actuals. This results in a figure of £853k (Dec 2014 prices) over the six year period. In applying the allowances we will take the GD17 frontier shift into account as set out below.
- 2.57 To illustrate, we have provided a year by year allowance in the Table below which also reflects the impact of the frontier shift. Details of the frontier shift are set out 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 GIS allowances**



# 3 Update of Determination Values

## Overview

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- 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 have decided 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 modifications; and
  - the associated reasons and effects.

## Licence Modifications

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- 3.4 We will modify Condition 4.7: Current Designated Parameters and Determination Values of the Licence to include the additional values as decided in Chapter 2. There is a link to the legislative notice for the licence modifications in Annex 3 to this paper.
- 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 the licence modification.

Description (for Conveyance Categories <i>i</i> and Formula Years <i>t</i> )	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	$P_{Eit}$	<i>i</i> = 1	0.4335	0.4335	0.4335	0.4335	0.4335	0.4335
	$P_{Eit}$	<i>i</i> = 2	0.3046	0.3046	0.3046	0.3046	0.3046	0.3046
	$P_{Eit}$	<i>i</i> = 3	0.2730	0.2730	0.2730	0.2730	0.2730	0.2730
	$P_{Eit}$	<i>i</i> = 4	0.2168	0.2168	0.2168	0.2168	0.2168	0.2168
	$P_{Eit}$	<i>i</i> = 5	0.2558	0.2558	0.2558	0.2558	0.2558	0.2558
	$P_{Eit}$	<i>i</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>i</i> and Formula Years <i>t</i> )	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	$P_{Eit}$	<i>i</i> = 1	0.4359	0.4359	0.4359	0.4359	0.4359	0.4359
	$P_{Eit}$	<i>i</i> = 2	0.3062	0.3062	0.3062	0.3062	0.3062	0.3062
	$P_{Eit}$	<i>i</i> = 3	0.2745	0.2745	0.2745	0.2745	0.2745	0.2745
	$P_{Eit}$	<i>i</i> = 4	0.2180	0.2180	0.2180	0.2180	0.2180	0.2180
	$P_{Eit}$	<i>i</i> = 5	0.2572	0.2572	0.2572	0.2572	0.2572	0.2572
	$P_{Eit}$	<i>i</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 – New Determination Values**

- 3.8 The table above represents the effect of the licence modifications, in terms of the values changing for the GD17 price control period.
- 3.9 A copy of the Licence is included in Annex 4 setting out the figures for the full revenue recovery period until 2045. The modifications to the Licence are shown as tracked changes in this Annex.

## 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 in respect of 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 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 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 The PI model has been updated to show the effect of this change. The updated PI model is included as an annex to this paper (Annex 5).
- 3.15 The modification to be made, 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.

# 4 Next Steps

## Conclusion and Next steps

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- 4.1 This paper represents the Utility Regulator's decision on modifications to the FE Licence. The modifications outlined in this decision paper will take effect from 22 May 2017.
- 4.2 This timetable means that the effective date of the licence modifications will be 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<sup>13</sup>. This period provides an opportunity for the licence holder subject to the price control, any other licence holder materially affected by the decision, a qualifying body or association representing one of those licence holders, and/or the Consumer Council for Northern Ireland to appeal the decision on the licence modifications to the CMA.
- 4.3 An application to the CMA for permission to appeal must be made within 20 working days from 24 March 2017.
- 4.4 This document is available in accessible formats. Please contact Paul Harland on 028 9031 1575 or email: [Gas\\_networks\\_responses@uregni.gov.uk](mailto:Gas_networks_responses@uregni.gov.uk) with cc to [paul.harland@uregni.gov.uk](mailto:paul.harland@uregni.gov.uk) to request this.

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<sup>13</sup> <http://www.legislation.gov.uk/nisi/1996/275/contents>

# Annexes

Document	Document Link
Annex 1	<a href="#">Firmus Energy Response to consultation</a>
Annex 2	<a href="#">Consumer Council for Northern Ireland Response to consultation</a>
Annex 3	<a href="#">Notice under Article 14(8) of the Gas (Northern Ireland) Order 1996 – Modifications of the Gas Conveyance Licence Held by Firmus Energy (Distribution) Limited</a>
Annex 4	<a href="#">FE Licence – Modifications</a>
Annex 5	<a href="#">Final PI Model</a>

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