SPC20 Price Control (2020 – 2022)

firmus energy Supply Ltd response to

The UR’s SPC20 Consultation

29 July 2019

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Introduction

firmus energy Supply Ltd welcomes the opportunity to respond to the Utility Regulator's (UR) SPC20 Consultation published 30th May 2019.

The following document focuses on the Business Expenditure Questionnaire (BEQ) and approved allowances necessary for the operational activities of firmus energy Gas Supply Ltd in the Ten Towns Network Area.

The SPC20 process to date has been defined by a transparent information sharing process and meaningful engagement between the UR and firmus energy, to the benefit of consumers across the Ten Towns Network Area. As a result we are providing comments for a number of key areas within the Manpower Costs, Operational Costs and Billing Costs that we believe require further consideration by the UR.

It remains firmus energy's intention to provide the UR with the necessary clarity and detail to support its forecast of expenditure levels required for the regulated tariff sector in the Ten Towns Network Area for the period 1st January 2020 to 31st December 2022.

Manpower Costs

Manpower

A comprehensive and detailed breakdown of all tariff and non-tariff FTEs was provided for the following four categories:

- Finance, HR, Billing and IT
- Regulation and Pricing
- Sales, Marketing and Customer Services
- Management

We welcome the UR's Consultation analysis and proposal to approve the Manpower allowances as submitted by firmus energy.

Recruitment Costs

Recruitment costs relate to the fees paid to our recruitment consultants and agencies for acquiring staff necessary for the Ten Towns Gas Supply Company. Recruitment costs from 2019 are based on an average of historic costs (i.e. 2016 and 2018), driven by and apportioned by FTEs as detailed within the Manpower section.

2016 and LBE 2018 showed an actual cost for recruitment, which was consistent with our budget expectations. This was not the case, however in 2017, due to the degree of staff turnover and the vacated positions remaining unfilled. Accordingly, we submitted our forecast based on the more appropriate and normalised average costs of 2016 and 2018.

Table 1

Recruitment £	2020	2021	2022
Total Ten Towns feSL Submission	29,824	30,595	31,366
UR Consultation	19,479	19,983	20,486
Variance	-10,345	-10,612	-10,880
Variance (%)	-35%	-35%	-35%

Table 2

firmus energy Recruitment Activity	2017	2018	2019 to Jun
Joiners	17	18	13
Movers	14	6	15
Leavers	20	14	9
Average heads	95	98	104
Churn % *	21%	14%	8%

Churn % is calculated by No. of Leavers / Average No. heads x 100

Contrary to our submission, the UR's Consultation Recruitment allowance was based on only the 2017 costs and consequently is 35% lower than firmus energy's requested allowance. As stated previously, we believe 2017 to be an unsuitable year for determining the SPC20 forecast, specifically due to the number of unfilled positions detailed in Table 2 above.

Furthermore, it is our opinion that historical costs should not be determined on any one particular year (in isolation) and, as such, we would request that the UR reconsiders its allowances for Recruitment to reflect the costs submitted in our original submission (see Table 1 above).

Operational Costs

Office Costs and Rates

The UR's Consultation applied the average actual office costs incurred by firmus energy in 2017 and 2018 to forecast office costs from 2019 onwards. We support this methodology and agree that FTEs are the most appropriate driver for calculating future allowances in years 2020 to 2022.

Supplier of Last Resort (SoLR)

In our submission, annual allowances were requested to offset costs borne from a SoLR event. The UR's Consultation proposed that any remuneration of costs incurred as a result of a SoLR event would be managed through the SoLR procedures and not included as part of price control considerations.

Further to the recent focus from the UR at industry forums to ensure all Suppliers are "SoLR-Ready", we would request the following allowances. The preparatory obligations required for SoLR readiness incurs a cost to the business and as such we have prepared Table 3 below showing indicative SoLR readiness measures and costs for the price control period.

Table 3

SoLR Readiness Requirements	2020	2021	2022
Annual Testing incl. Internal Resource	1000	1000	1000
Annual SoLR Training - 1 session	750	750	750
IT Development x 2 days	1300	1300	1300
Legal / Consultancy – 3 hours	750	750	750
Total	**3800**	**3800**	**3800**

We believe the above costs are a prudent forecast for the upcoming implementation and testing required for SoLR readiness.

Professional and Legal Fees

The UR's Consultation makes notable adjustments from firmus energy's BEQ submission for Professional and Legal fees. The first consideration was removing the driver so the allowances remain constant across the period (save for additional Supply price control fees in 2022), and the second proposal is to remove an allowance relating to General Data Protection Regulations (GDPR). Given the recent costs incurred in relation to GDPR, which we have provided in detail to the UR, we believe it would be prudent for the UR to provide an allowance for Data Protection Consultancy to cover ad hoc additional IT and legal fees. Given the relatively new need for GDPR related expenditure [May 2018], we have used recently experienced costs to guide our forecasts. We believe £20k per annum to be an appropriate forecast.

COST CONSIDERATIONS RESULTING FROM GDPR/DATA BREACH

Category	External
IT/Technical Consultancy	Data Analytics engagement CyberGuarded review/ modifications to O365
Legal	Review of outgoing communications to data subjects. Response to inbound queries
PR Company	Review of outgoing communications to data subjects Response to inbound queries
Communications	Prepare/deliver media statements Cost for outgoing mailer Setup/Management of dedicated phone line
	Internal
Internal/Staff Costs	1xIT, 1xDPO, 1xDirector, 1xHR,Other staff Downstream cost for SAR responses - all depts.

Unquantified costs

Category	Item
Legal	Defending possible actions
Regulatory/Compliance	Potential for monetary penalty from ICO
Commercial	Possible cost for reimbursing customers/other institutions who have suffered financial loss

The above notes highlight the potential impact of Data Protection measures and subsequently we would request that the UR revise its decision to not approve any monies for GDPR related matters.

Information Technology (IT) Capex and Opex

In 2015, during the SPC17 process, firmus energy began their engagement with the UR and external Consultants Gemserv, to discuss the need to replace its ageing billing/IT system – IUS. As part of this process, firmus energy provided a detailed business case, outlining the requirements for an IT upgrade and implications for consumers and operations, should it not be implemented. As part of the UR's Final Decision paper they concluded that the need for the new system was justified and subsequently approved allowances within the SPC17 Final Determination relating to the new IT system.

In May 2018 the General Data Protection Regulations (GDPR) came into effect. GDPR became the firmus energy IT department's immediate priority and as a result, any advancement of the IT systems upgrade project was rescheduled accordingly.

[redacted]

[redacted]

[redacted]

[redacted]

[redacted]

[redacted]

As a result of this procurement exercise, to date, it is apparent that the costs in the firmus energy submission are not sufficient to ensure implementation of the new IT system. Therefore, we have engaged with the UR to ensure they now have an accurate picture of the specific operational IT costs required from 2020 to 2022.

Consequently we would request that the UR reconsiders the approved allowances for firmus energy IT Capex and Opex requirements.

[redacted]

[redacted]

[redacted]

[redacted]

[redacted]

- [redacted]

[redacted]

REVISED SPC20 IT OPEX and Additional Capex Submission (Spread evenly over 3 years)

IT Opex and Additional IT Capex	2020	2021	2022
Tariff	348,218	348,230	348,261
Non-Tariff	3,769	3,757	3,726
Ten Towns Total	**351,987**	**351,987**	**351,987**

As determined by Gemserv and the UR during the SPC17 process, firmus energy justified the need for a new IT system. In order for us to proceed with this project we would require support from the UR in terms of SPC20 allowances and a revision to those outlined in the Consultation, as detailed above.

Following recent discussions with the UR, we would ask that approval for the IT costs in principal be provided in advance of the UR's final determination (anticipated September 2019) in order that we can optimise momentum in the procurement process.

New IT System Cost Allocation Methodology

The UR has indicated that it is considering allocating the costs of the new IT system using tariff and non-Tariff bills created. It is our opinion that this is not a suitable methodology, as the system is not specifically used only for billing but instead caters for every element of a customer's requirements. Furthermore, a significant element of the new IT systems operational capabilities is to manage approximately 2,700 PAYG meter read calculations and forecasts on a daily basis[1]. Consequently, we would request that apportionment of costs is calculated using tariff and non-tariff customer numbers and not bills created.

Other Capex

The previous section in this response dealt with Capex relating to the proposed new IT System, however we also welcome the UR's Consultation proposal to approve the costs relating to our server replacement and staff hardware refresh including meter reading tablets.

Call Centre

We acknowledge the UR's view that Call Centre costs wouldn't necessarily increase at the same rate as the increase in customer numbers, however do not believe it is appropriate to use a single year (2017/18) as an 'historical trend'. Subsequently we have provided a new proposal that is based on an historic (2 year) Call Centre '*cost per customer*', and is in line with the UR's approach.

Call Centre £	**2020**	**2021**	**2022**
Tariff Cost	29,883	33,310	36,941
Non-Tariff Costs	323	359	395
Total Ten Towns	**30,207**	**33,670**	**37,337**
Driver/Apportionment	Forecast driven by an historic average cost per customer		
UR Consultation	23,923	24,738	25,572

We would ask the UR to consider this approach and the update the cost allowances accordingly.

Advertising Website and Sales Development

Firmus energy remains of the view that advertising and marketing costs are necessary (as per submission) even for a regulated business, however, we welcome the UR's commitment to *"keep this under review as the market develops"*.

Billing Costs

Credit Checks

The UR's Consultation proposes allowances based on the 2017 and 2018 average driven forward by credit customer numbers. Similar to the Call Centre costs, we have reviewed this cost line based on the UR's approach and determined a more appropriate forecast rate per customer. The analysis has been provided in our accompanying spreadsheet and the results are detailed in the table below.

Credit Checks £	**2020**	**2021**	**2022**
Tariff Cost	5,374	6,096	6,913
Non-Tariff Costs	366	407	447
Total Ten Towns	**5,741**	**6,503**	**7,360**

[1] Based on 975,778 PAYG transactions in 2018 in Ten Towns Network Area

Driver/Apportionment	Forecast driven by an historic average cost per customer		
UR Consultation	4,108	4,654	5,267

Bank and Interest Charges

In line with Call Centre costs and Credit Checks, we have reviewed this cost line following the UR's approach and again have provided updated analysis and cost forecasts based on a 'cost per unit' methodology. Rather than cost per customer, we have employed a cost per unit volume, reflecting that bank charges will correspond to revenue generated. The analysis has been provided in our accompanying spreadsheet and the results are detailed in the table below.

Bank and Interest Charges £	**2020**	**2021**	**2022**
Tariff Cost	2,038	2,255	2,479
Non-Tariff Costs	3,726	3,779	3,832
Total Ten Towns	**5,764**	**6,034**	**6,312**
Driver/Apportionment	Forecast driven by an historic average cost per unit volume		
UR Consultation	4,968	5,201	5,440

Bill Processing Customer Information and Postage

Bill processing is subject to retrospective adjustment relating to actual bills, invoices PAYG statements and other literature sent out to tariff customers such as direct debit confirmations, credit control/debt reminders, property handover letters. There are also a number of items that may be sent out during the year that we would deem to be allowable costs based on their status as a licence requirement. For example a change of tariff letter may be sent out once, twice or not all in a year (such as 2014). Also any change in Terms and Conditions will require provision of a notice and a Terms and Conditions booklet for all customers.

The UR's Consultation is materially lower than the firmus energy submission, owing to the view that until the actual activities carried out are known, the allowance will be based on historic costs and adjusted retrospectively. We acknowledge the UR's approach, however, we would request confirmation that the rates submitted (which will be used in the annual retrospective adjustments) have been approved. Furthermore, we would request that any Royal Mail increases or decreases in postage costs would also be applied to our annual amendments. Below are the rates submitted as part of our BEQ, for which we seek confirmation of approval.

Stationery Unit	**Requested stationery unit allowance Oct 18 prices**	**Postage allowance (as per Royal Mail)**
Welcome Pack	£1.672	£1.250
Customer Literature (EE/Energy Care/ Winter heating tips etc.)	£0.166	£0.570
Domestic Bill	£0.166	£0.570
DD Statement	£0.166	£0.570
PAYG Statement	£0.166	£0.570
Change of Tariff Notice (October April)	£0.166	£0.570
DD Notification	£0.166	£0.570
Credit Control Reminder	£0.166	£0.570
Handover Letters	£0.166	£0.570
New T&Cs Booklet	£1.096	£0.570

Conclusion

Firmus energy acknowledges and welcomes the UR's meaningful engagement throughout the SPC20 process. Through this response we have brought to the UR's attention a number of key areas that we believe require further consideration, most specifically, the IT Capex and Opex costs relating to the new billing system

To conclude the SPC20 process, we request that we continue our IT System Costs engagement with the UR, with the view to ensuring a UR Final Determination that facilitates firmus energy implementing this necessary project.

We would be happy to discuss any of the comments made in this response, or provide further clarification as necessary.