mutualenergy

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Roy Colville
Queens House
14 Queen Street
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15 August 2016

Dear Sir,

Price Control for Northern Ireland's Gas Transmission Networks GT17

1. Mutual Energy Limited (MEL) is grateful to have the opportunity to respond to this consultation on behalf of its three wholly owned subsidiaries Premier Transmission Limited, Belfast Gas Transmission Limited and West Transmission Limited (formerly Northern Ireland Energy Holdings Limited) which hold licences to convey gas granted pursuant to the Gas (NI) Order 1996.

Submission format and timing

2. The GT17 price control represents a significant change to the price control process for Mutual Energy's gas businesses. Historically price controls have been carried out 3 yearly on a set programme with a prescribed reporting format which aligned with our internal accounting format. Whilst we accept the rationale for the change in formats and additional disclosure proposed, the discussions between GNI, NIAUR and ourselves to develop a new reporting template only reached conclusion at the end of June with the issuance of the new template. This template is in a format which does not align with our accounting costs codes, thereby requiring additional historical reanalysis of costs (both for historical cost reporting and as a guide for forecasting), and requires a significant amount of additional work compared to previous submission's.

3. The timing of the price control is not in line with our current reporting schedule and therefore was not planned for at this time. The process requires input from every budget holder within the gas operations team in months that are the operations teams' busiest period, as most planned maintenance and inspections are purposely scheduled through this time. Irrespective of the changes in the reporting format the time allowed for preparation of the price control submission is insufficient to allow us to provide robust explanations and verifications to support our costs. The GD17 price control allowed 3 full months between publication of the approach and submission of the business plans, and this period did not coincide with any holiday period or peak-maintenance season. The GT17 price control includes only 2 months between these milestones and these months consist entirely of the summer period where staff availability is significantly reduced and operational staff are stretched. As a result, it will not be possible for us to provide a business plan at the level of detail which we feel is necessary.

4. Paragraph 2.7 of the paper notes that licence holders should "demonstrate that responsibility for the assurance of the data and plans submitted resides at board level" however our next board meeting is scheduled for 29th September and therefore the insufficient time allowed for the submission does not allow us to ensure that this is the case.

5. **We therefore request that the deadline for the submission of the business plan be delayed for at least one month to allow 3 month's preparation time, giving sufficient time for consideration and approval by the Board.**

Social Enhancement Account

6. We note that the paper proposes changing the arrangements on which our gas businesses were financed, taking a preliminary view that the Social Enhancement Account mechanism is no longer required. Any change to the underlying arrangements requires extensive work with our long term financiers, incurs costs of legal opinions, legal reviews and licence changes. We would like to note that in any period NIAUR may set the Z factor to zero and therefore not allow the retention of savings. If NIAUR are not content with the Social Enhancement Account, then setting the Z factor to zero achieves the same result without imposing the costs of the changes on the customer.

7. The Social Enhancement Account mechanism can be used to help avert tariff fluctuations caused by timing. If costs of a project are incurred in a later tariff year than anticipated the mechanism can be used to allow money to be held over from one year to the next, avoiding a reimbursement to shippers in one year to collect again through the tariff in the next year. The concept of this mechanism was conceived by NIAUR and we do not understand the rationale for wanting to remove this tool from the tool box at cost to the consumer.

8. As part of the Gas to the West project we had proposed to apply £3m from this Account to apply to the arrangement costs of the financing, so returning this cash to customers over the duration of the financing of this project, and we are keen to discuss this with NIAUR.

West Transmission Limited Weighted Average Cost of Capital (WACC)

9. The Gas to the West licence award process established a WACC based on the prevalent market conditions at the time. It should be noted that the final WACC achieved will be dependent on the market conditions prevailing at the time of issue. Based on current market conditions this may indeed be lower than bid, however it should be noted that this may move up or down between now and issue of the bond.

Scope of the Price Control

10. The TSO's are currently finalising a mobilisation budget to capture the costs which will be incurred in advance of 1st October 2017, such as backfill costs to cover internal effort required to support the new system build, the CJV organisation set-up, and staff release to commence employment within the CJV in advance of Oct'17. This budget is to be agreed with UR within the NIED project and we do not envisage that the evaluation of these costs will form part of the GT17 process.

11. The treatment of any expenditure which does not increase overall capacity as controllable opex is a clear definition, albeit very different from the tax or accounting definition. Definitive costing in advance is however particularly difficult. Our assets were all constructed at the same time as opposed to a large network growing over time. This leads to a certain concentration of repex costs as particular asset components reach the end of their useful life. In the case of our network the asset age is approximately in the 20-25 year band, and a number of larger plant types reach end of life in this period. In the absence of detailed functional design, itself a costly process best carried out close to the replacement needed, costs can therefore be indicative and we hope NIAUR will recognise this constraint in this process. Again in a network with a rolling replacement program the utility will have access to current prices for a large variety of the work which are readily applicable, making this much easier.

Other Comments

12. In respect of the CJV we note the comment that there are "unlikely to be any unforeseen developments". The majority of major changes have historically been driven by regulatory decisions, mostly of EU origin. Whilst there is visibility for the next couple of years on the issues being discussed, the actual outputs can be very different and so unforeseen developments are actually likely. Often it will be the IT impact of proposed European wide rules changes which can be very costly.

13. We note that the price controls will be based upon an expected split of activities between the two licensed entities, with differences to be accommodated by recharging between licensees. This adds additional complications in respect of the tax and legal position of these recharges. In our view the most efficient approach would be a modification of allowances as part of the reconciliation process.

14. Paragraph 2.33 notes there could be additional cost savings delivered if GNI(UK) and MEL acted jointly rather than separately when awarding contracts such as the Maintenance and Emergency Response Contract (MERC). There are a number of constraints to the extent this can be done and this option was explored with GNI in 2010 when we aligned procurements. We do not see any further benefits achievable within the permissible legal parameters of two separate entities. Each entity bears its own responsibility for the safety and operation of its assets, for which the MERC contract is one of the most critical contracts. It is not possible to award such a contract on a joint basis for a number of reasons, not least the fact that each entity must retain control of its own operations.

15. It is proposed that going forward MEL's gas businesses submit forecasts of uncontrollable costs, including Transportation Agreement costs. Whilst we can endeavour to provide these we have limited knowledge of works planned on the GNI assets and expected future costs and therefore any information provided is limited by the provision and accuracy of information received by GNI (UK).

16. Paragraph 2.41 notes a potential catch-up of allowances to the frontier. It is not clear how NIAUR intends to do this but it should be noted that any such catch up should not bring allowances in line with larger companies who benefit from economies of scale which are not present in our businesses.

17. As a mutual business our aim is to operate cost effectively and deliver savings to consumers, therefore we appreciate NIAUR's wish to exclude any profit margins to other companies. Where it is more cost effective to do so Mutual Energy jointly tenders for individual licenced gas company services via a services company. There are costs in operating the services company which have to be charged and paid but overall the benefits outweigh these costs. In such circumstances the costs and not just the benefits of providing services this way needs to be allocated to the licenced gas companies. It should be noted that companies are expected to charge between themselves on an arms-length basis.

Yours faithfully,

Gerard McIlroy

Gerard McIlroy
Director