



SPC20: Price Control for SSE Airtricity Gas Supply (NI) Ltd

Final Decision
4 November 2019



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

This document sets out the UR's final determination for the price control on SSE Airtricity Gas Supply (NI) Ltd in the Greater Belfast gas supply market. The control will come into effect on 1 April 2020 until 31 March 2023.

This paper outlines the UR's decisions in relation to the main areas within the SSE Airtricity control: structure and form; scope and coverage of regulated tariffs; duration of control; operating costs levels and allocations; and allowed margin.

Audience

Industry, consumers, and their representative bodies and statutory bodies.

Consumer impact

The price control will protect customers by setting a maximum limit on the average price that SSE Airtricity can charge its price regulated customers for gas in the Greater Belfast and the West areas. This ensures that customers only pay for the efficient cost of the gas they receive and a fair profit margin.



Contents page

Glossary	1
1. Introduction	2
2. Background	3
3. Scope and Duration	4
4. The Regulated Tariff	5
5. Network Costs	9
6. Supply Operating Costs	10
7. Gas Costs	24
8. Margin	26
9. Reconciliation	28
Annex 1.....	30



Glossary

Name	Definition
CAPEX	Capital Expenditure
CCNI	Consumer Council for Northern Ireland
CMA	Competition and Markets Authority
DfE	Department for the Economy
EUC	End User Category
FES	firmus energy (Supply) Ltd
FTE	Full Time Employee
GB	Great Britain
HMRC	Her Majesty's Revenue & Customs
IT	Information Technology
I&C	Industrial and Commercial
LBE	Latest best estimates
NI	Northern Ireland
OPEX	Operating Expenditure
PAYG	Pay As Your Go (Pre-payment meter)
PSL	Phoenix Supply Limited
Power NI	Power NI Energy Ltd
Q	Quarter
REMM	Retail Energy Market Monitoring
RPI	Retail Price Index
SGN	SGN Natural Gas Limited
SNIP	Scotland-Northern Ireland Pipeline
SPC17	Supply Price Control 2017-2020
SPC20	Supply Price Control 2020-2023
SSE Airtricity	SSE Airtricity Gas Supply (NI) Ltd
UR	Utility Regulator

1. Introduction

- 1.1. The principal objective of the Utility Regulator (UR) in relation to gas is “to promote the development and maintenance of an efficient, economic and co-ordinated gas industry in Northern Ireland” while having regard to “the need to ensure a high level of protection of consumers of gas”. To help meet this objective we retain price controls on dominant, former monopoly, gas and electricity suppliers.
- 1.2. This document sets out the decisions and principles that form the basis of SSE Airtricity’s Supply Price Control 2020 – 2023 (SPC20) and provides background information on the Greater Belfast gas market.
- 1.3. The new control will apply from 1 April 2020 for SSE Airtricity until 31 March 2023.
- 1.4. This final determination follows the UR’s Consultation Paper published in July 2019 which set out our proposals for SPC20 for SSE Airtricity. We received two responses to this consultation which are published alongside this final determination and addressed where relevant within this consultation.
- 1.5. We consider that our approach has been consistent with the principles of better regulation which the UR continues to apply: transparent, consistent, proportionate, accountable, and targeted.
- 1.6. All costs presented are in October 2018 prices. These prices will be adjusted within the tariff for inflation as discussed in Section 9
- 1.7. As SSE Airtricity changed their accounting period from 1 January to 1 April for the current price control (SPC17), any references to a year within this document relate to the period 1 April – 31 March.

2. Background

- 2.1. In Northern Ireland (NI) there are three separate distribution areas for natural gas. These are the Greater Belfast area, the Ten Towns area and the West area. The Greater Belfast area is served by Phoenix Natural Gas Ltd (PNGL) and the price-regulated supplier is SSE Airtricity. The Ten Towns area is served by Firmus Energy (Distribution) Ltd and the price regulated supplier is Firmus Energy (Supply) Ltd (FES). The West area is served by SGN Natural Gas Ltd (SGN) and the price-regulated supplier is SSE Airtricity.
- 2.2. The Greater Belfast market includes Belfast, Newtownabbey, Carrickfergus, Larne, Carryduff, Newtownards, North Down and East Down. There are approximately 218,000 connections to the network (comprising of 211,521 domestic and 11,192 I&C connections) in this area¹. Currently there are five active suppliers in the market. Only two of these companies supply to domestic customers; SSE Airtricity and FES.
- 2.3. The West market includes Coalisland, Cookstown, Dungannon, Magherafelt, Omagh, Enniskillen, Strabane and Derrylin. There are approximately 476 connections to the network (comprising of 455 domestic and 21 I&C connections in this area³. There are now 3 active suppliers in the West area, namely SSE Airtricity Gas NI as the commissioning domestic supplier, with Electric Ireland and Flogas active only in the I&C market.
- 2.4. The current SSE Airtricity price control applies for the period from 1 April 2018 to 31 March 2020, in line with their accounting period.
- 2.5. SSE Airtricity is a subsidiary of SSE plc, a UK-listed energy company with operations and investments across the UK and Ireland. SSE is involved in the generation, transmission, distribution and supply of electricity, the production, storage, distribution and supply of gas and in the provision of energy-related services.

¹ UR Quarterly Transparency Report (Q2 2019): https://www.uregni.gov.uk/sites/uregni/files/media-files/2019-08-30%20-%20Transparency%20Report%20Q2%202019%20Final_1.pdf

3. Scope and Duration

Scope

- 3.1. The SPC17 Final Determination stated that the control would apply to one distinct End User Category 1 (EUC1) – all domestic customers and those businesses using less than 2,500 therms (73,200 kWh);
- 3.2. Due to the continued dominance of SSE Airtricity in the EUC1 category, for SPC20 we proposed to retain the scope of the control at domestic and low-consumption business customers using up to 2,500 therms (73,200kWh) per annum.

Duration

- 3.3. In the November 2018 Information Paper we stated that we considered a three year period to be the most appropriate duration for the price controls as it balances the resource implications of carrying out a control with the ability to forecast accurately over the medium term.
- 3.4. Therefore, it was our proposal in the consultation to apply the control for a period of three years; from 1 April 2020 to 31 March 2023.

Response to Consultation

- 3.5. SSE Airtricity supported the UR's proposal in its response to the consultation.

Final Determination

- 3.6. It is the decision of the UR that the scope and duration of SPC20 for SSE Airtricity will remain structured as it was in SPC17; as is laid out in the consultation.

4. The Regulated Tariff

4.1. The gas supply licence confers on the UR the power to control charges if deemed necessary:

2.4.1 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 Premises² shall not exceed the maximum price calculated”

4.2. A price control is the mechanism that the UR uses to determine the costs which make up the maximum average price per therm that a price regulated gas supply company can charge.

4.3. In granting consent we review the maximum average price to ensure that it is constructed in line with the provisions within the price control.

4.4. This price control sets out the treatment of each cost element which makes up the maximum average price. These are:

- Network Costs;
- Wholesale Gas Costs;
- Supply Operating Costs; and
- Margin

K Factor

4.5. In addition to the costs outlined above the maximum average price will also include a k factor adjustment.

4.6. In the consultation paper, we proposed that some costs should be treated as retrospective costs. Some of the retrospective costs will be pass through costs, meaning that the company is allowed to recover the actual levels of costs incurred; whereas other retrospective costs will be subject to a retrospective adjustment to calculate the level of allowed cost based on pre-determined factors.

4.7. The costs which we have proposed in this price control to treat as retrospective costs are listed in the table below along with our proposal for

² Regulated Premises means premises supplied by the Licensee in the Greater Belfast and the West areas at which the normal annual consumption of gas is reasonably expected not to exceed 73,200 kilowatt hours.

the determination basis of each cost.

Retrospective cost line	Determination Basis
Network costs	Pass through cost
Wholesale gas costs	Pass through cost
Prepayment transaction costs (within Billing costs)	Retrospective adjustment
Bad debt (within Billing costs)	Retrospective adjustment
Meter reading costs (within Billing costs)	Retrospective adjustment
Customer information processing & postage (within Billing costs)	Retrospective adjustment
Safety inspections and meter exchanges (within Operations Costs)	Retrospective adjustment

- 4.8. Within the tariff we will include a forecast for these retrospective costs based on historical performance and latest best estimates. Each year a reconciliation is carried out to calculate the actual allowed costs based on pass through cost, or the retrospective adjustment as appropriate.
- 4.9. The k factor is the difference—whether positive or negative—between all of the pass through and retrospectively adjusted actual costs incurred, and what was forecast for them. This difference will then be taken off or added to the next tariff revenue requirement respectively at the next tariff change.
- 4.10. It is our intention to maintain the k factor at a minimum level through the use of regular tariff reviews and a trigger mechanism to monitor the tariff closely and thus minimise the impact of the k factor on the tariff.
- 4.11. At each tariff change the UR will publish the k factor to allow for transparency.

Tariff Review

- 4.12. A tariff review is the process of analysis and discussion of the tariff to consider if a change to the tariff is needed, and to decide the magnitude and timing of any change.
- 4.13. We review the gas tariffs on a bi-annual basis. In addition we will be able to

initiate a tariff review under the trigger mechanism as discussed below. We consider that regular reviews minimise the impact of k factor on the tariff and can help mitigate tariff volatility for consumers.

- 4.14. We have established a process in consultation with the SSE Airtricity, the Consumer Council for Northern Ireland (CCNI), and the Department for the Economy (DfE) which sets out the timescales and information required in setting the tariff.
- 4.15. The tariff review process is a consultative one where all parties bring their expertise and opinion in relation to the needs of the gas supplier, the needs of the consumer, and the wider impact on the economy. Therefore, it is important that all parties are aware of and in agreement with the formal process.
- 4.16. This process provides a robust procedure, which is in line with the requirements of the licence to ensure that all parties are consulted in a timely, prescribed, and comprehensive manner for both anticipated and unanticipated tariff reviews.

Trigger Mechanism

- 4.17. In addition to the bi-annual tariff reviews we establish a trigger mechanism within the price control. The aim of this trigger mechanism is to initiate a tariff review should the cost of wholesale gas purchased by the gas supplier vary significantly from the cost forecast within the tariff.
- 4.18. The trigger mechanism will operate to allow the UR to initiate a tariff review should the tariff costs change between review periods, either increase or decrease, so as to change the tariff by 5%.
- 4.19. We consider the 5% level to be an appropriate level, any level under this and volatility in the wholesale market could necessitate a number of tariff reviews in a year. Tariff reviews can be costly and complex for the company.
- 4.20. Where a review is initiated by the trigger mechanism, the tariff review group will look at a number of factors including:
 - Volatility in the wholesale gas market;
 - Time since last tariff review;
 - Level of k factor; and
 - Amount of gas purchased by the supplier
- 4.21. The UR also retains the flexibility to initiate a review at any stage it considers is in the interest of customers.

Tariff Structure

- 4.22. The domestic credit tariff for SSE Airtricity is made up of two charges; a higher charge for the first 2,000 kWh used per annum and a second charge for any usage above 2,000 kWh per annum³.
- 4.23. Pay as You Go (PAYG) customers pay a flat tariff for each unit used.
- 4.24. Industrial and commercial customers using less than 73,200 kWh (2,500 therms) are charged a two tiered tariff; with different charges for usage up to 2,000 kWh per annum, and between 2,001 kWh and 73,200 kWh per annum⁴.
- 4.25. At each tariff review we will require the supplier to demonstrate the assumptions used to create the tariff structure in order to ensure that the average weighted price charged to customers is equal to or less than the maximum average tariff.

Response to Consultation

- 4.26. SSE Airtricity made no comment on the structure of the regulated tariff in its response to the consultation.

Final Determination

- 4.27. It is the decision of the UR that the regulated tariff will remain structured as it was in SPC17; as is laid out in the consultation.

³ SSE Airtricity Domestic tariffs: <https://www.airtricitygasni.com/at-home/help-and-advice/tariffs-and-payment-options/>

⁴ SSE Airtricity I&C tariffs: <https://www.airtricitygasni.com/in-business/help-and-advice/tariffs/>

5. Network Costs

- 5.1. Network costs are the charges incurred by SSE Airtricity for their use of the NI gas transmission and distribution systems. These charges are reviewed and approved by the UR.
- 5.2. The costs for the transmission system are those costs involved in bringing gas from Scotland to NI, via the Scotland to NI Pipeline (SNIP), and all the transmission pipelines within NI. These costs are published on the Gas Market Operator for NI (GMO NI) website⁵.
- 5.3. The costs for the distribution system are those costs associated with moving gas throughout the distribution networks area to homes and businesses. These can be found on the Phoenix Natural Gas website⁶ for the Greater Belfast area and on the SGN Natural Gas website⁷ for the West area.
- 5.4. Distribution costs are also subject to price control by the UR. The current price control, GD17, runs from the period of 1 January 2017 for to 31 December 2022.
- 5.5. Within the previous controls for SSE Airtricity, the network costs have been treated as pass through costs. This means that the customer pays for the actual cost of the network charges that SSE Airtricity incur, and no more than that.
- 5.6. Therefore, in the Consultation Paper we proposed that network costs remain as pass through costs, as these are outside the control of the supplier.

Response to Consultation

- 5.7. SSE Airtricity made no comment on the treatment of Network Costs in its response to the consultation.

Final Determination

- 5.8. It is the decision of the UR that network costs will remain pass through costs for SPC20.

⁵ GMO NI charges: <http://gmo-ni.com/tariffs/explanatory-notes>

⁶ Phoenix Natural Gas network charges: <https://www.phoenixnaturalgas.com/about-us/about-phoenix/network-information/network-charges>

⁷ SGN Natural Gas charging statements: <https://sgnnaturalgas.co.uk/index.php/publications/>

6. Supply Operating Costs

- 6.1. Supply operating costs are those costs which relate to the day to day operation of the SSE Airtricity gas supply business; and include among other things salaries, IT costs, metering costs, rent and rates, consultancy/legal fees and bad debt.
- 6.2. In November 2018, the UR provided SSE Airtricity with an initial information request for the operating costs wholly incurred by the gas supply business in the provision of gas to customers within all the gas distribution areas: Greater Belfast, West, and Ten Towns. This included the total operating costs for serving both price controlled and non-price controlled customers using more than 73,200 kWh per annum.
- 6.3. The submission requested historical actual costs, Latest Best Estimates (LBE) of current costs, and a forecast of costs for the three years of the price control period. We stated that we would welcome any evidence to support the figures given in the submission. Additionally, the information request was clear that the burden of proof rests with SSE Airtricity to justify the cost base set out in the submission.
- 6.4. In January 2019 the supplier presented its initial submission to the UR. Over the next five months we engaged with SSE Airtricity to understand this submission through meetings and various additional information requests. We have analysed the forecast cost figures against historical costs and previous determinations and benchmarked information against other companies where appropriate. We have also engaged consultants to review specific elements of the submissions (e.g. IT required spend).
- 6.5. In July 2019 we published the consultation paper which set out our proposals for the price control. SSE Airtricity and CCNI submitted responses to the consultation in September 2019.
- 6.6. In the following section we set out our final decisions for the supply operating costs for SSE Airtricity. These decisions are shown against the requested costs of the companies and the draft determination.
- 6.7. In reaching our final determination we have considered the responses made by SSE Airtricity and CCNI to the consultation, requested additional information and engaged further with SSE Airtricity in order to arrive at our final position.
- 6.8. The costs shown throughout this paper are the total SSE Airtricity gas supply business costs (i.e. including SSE Airtricity's unregulated gas supply business in all three distribution areas). The apportionment allocation of costs determines the appropriate level of costs to the tariff sector (i.e. the

price regulated sector of SSE Airtricity). This ensures there is no cross-subsidisation between the tariff and non-tariff businesses. In order to calculate the apportionment, each cost line is apportioned on the basis of the most appropriate cost driver and these apportionments summed to provide the overall percentage. A list of the apportionment cost drivers can be found in Annex 1.

- 6.9. We consider that the allowances set is an efficient allowance, and given the relatively short duration of the Control we determine that an efficiency factor of 0% is appropriate for the duration of the control.
- 6.10. Table 1 below shows the total (price regulated and non-price regulated) costs for the SSE Airtricity total supply business. We present here the costs summarised into three main cost categories; **Manpower**, **Operations**, and **Billing**. It is not our intention to provide a line-by-line budget for the supplier to spend, but rather to provide an efficient overall allowance, derived from a reasonable assessment of the various cost requirements, for it to spend running the price regulated supply business.

Table 1: SPC20 submission and consultation Decisions

Tariff Costs	SSE Airtricity Submission			UR Consultation			UR Decision		
	2020	2021	2022	2020	2021	2022	2020	2021	2022
Manpower Costs	2,945	2,987	2,931	2,700	2,699	2,604	2,700	2,699	2,698
Operations Costs	1,841	1,730	1,737	1,596	1,465	1,453	1,190	1,208	1,225
Billing Costs	2,480	2,578	2,725	2,246	2,284	2,366	2,311	2,352	2,436
Total Costs	7,266	7,295	7,393	6,542	6,449	6,423	6,202	6,259	6,359

- 6.11. The following section discusses each of these three main cost headings above in greater detail to explain the basis for the finals decisions.

Manpower Costs

Table 2: Manpower costs

Tariff Costs	SSE Airtricity Submission			UR Consultation			UR Decision		
	2020	2021	2022	2020	2021	2022	2020	2021	2022
Salaries	2,304	2,342	2,288	2,081	2,080	1,990	2,081	2,080	2,079
Staff Engagement	12	12	11	11	11	10	11	11	11
Training	51	50	47	44	44	42	44	44	44
Labour Recharge	528	534	539	517	517	517	517	517	517
Travel and subsistence	50	49	47	47	47	44	47	47	47
Total	2,945	2,987	2,931	2,700	2,699	2,604	2,700	2,699	2,698

Salaries

6.12. Salaries make up the vast majority (93%) of the manpower cost submission along with some other smaller items of manpower cost. In its initial submission for manpower costs SSE Airtricity requested an increase from an actual level of 67 Full Time Equivalents (FTEs) in 2018 to 78.5 in 2020; in order to support customer growth and business change.

6.13. Following extensive analysis and benchmarking, we determined that the increase of 11.5 FTEs requested by SSE Airtricity was excessive. We therefore proposed an increase of 6 FTEs in 2020. This comprised of:

- **+1.5 Customer Service Advisor** to maintain the current level per 1,000 customers;
- **+1.5 FTE Credit Control** to maintain current level per 1,000 customers, and also assist with new Theft CoP compliance;
- **+1 FTE Back Office Analyst** in line with customer growth;
- **+0.5 FTE Quality Monitor** to manage customer service regulatory compliance issues;
- **+1 FTE Business Assurance Analyst** to allow for increased regulatory training and reporting to enhance regulatory compliance; and
- **+0.5 FTE Regulation Specialist** to ensure regulatory compliance against Codes of Practice;

6.14. In addition, we disallowed the provision of an allowance equivalent to 3 FTEs

to provide cover for long term sickness and maternity which was consistent with the treatment of other regulated companies.

- 6.15. We also proposed reducing the FTE count by 4 in the third year of SPC20 in anticipation of resource efficiencies due to the implementation of the new billing system.

Response to Consultation

- 6.16. SSE Airtricity asked that a further 1 Back Office FTE and 0.5 Credit Controller admin FTE for each year of the price control. The supplier stated this would provide sufficient resources to manage customer growth and associated debt.
- 6.17. As the upgrade of its billing system is not proceeding as planned (see paragraph 6.32), the supplier requested that the 4 FTEs removed in year 3 of the control be reinserted, as the assumed efficiencies in that final year will now not be realised. The supplier also asked that additional efficiencies of 2.5 FTEs (PPM Head and Credit Controller Admin) be reinstated.
- 6.18. SSE Airtricity asked that the UR reconsider its position on the disallowance of cover for long term sickness and maternity, and requested instead than an allowance of c.£30k per annum be provided. The supplier stated that in a business with very small staff numbers, there is little scope to cover the cost of absent employees during times of extended sick or maternity leave. When required, the supplier said that these positions are regularly filled with agency staff, meaning the position is being paid for by the business twice.
- 6.19. CCNI questioned whether salaries for the FTEs were broken down by different grades or salary bands. The consumer body also recommended that the UR benchmarks SSE Airtricity's manpower costs with a reasonable pool of comparable efficient suppliers in GB and ROI to identify whether there are opportunities to achieve further efficiencies in manpower costs.

Final Determination

- 6.20. It is the decision of the UR to maintain that the 6 additional FTEs proposed by the UR in the consultation are sufficient to manage customer growth and the associated debt; and that these levels benchmark comparably with other regulated NI suppliers. As the supplier has provided little additional evidence on head count requirements, the additional Back Office and Credit Control Admin FTEs requested will not be allowed for under SPC20.
- 6.21. We accept that the forecasted efficiencies resulting from the new billing system will now not be realised, and have therefore reinstated the 4 FTEs that were removed in year 3 of SPC20. However, there were no efficiencies factored in for PPM Heads or Credit Controller Admin, and therefore the

requested 2.5 FTE increase will not be allowed.

- 6.22. Consistent with the consultation, we maintain that long term sickness and maternity will not be provided for under SPC20. The UR cannot sufficiently quantify this cost or verify how suppliers have managed any absences. This is consistent with the treatment of FES, and suppliers will need to manage resourcing under the allowance provided.
- 6.23. Addressing CCNI's comments, we can provide assurance that the UR fully scrutinises each FTE allowance, and this includes a complete breakdown of grades and salary bands. However, the UR does not have the information required to make reliable benchmarks beyond the NI energy market.

Other Manpower Costs

- 6.24. Staff Engagement - We proposed to accept SSE Airtricity's submission as it is in line with HMRC recommendations and SPC17.
- 6.25. Training - We proposed to set this cost at the LBE rate per FTE for the duration of the price control.
- 6.26. Travel and subsistence (including Fleet Costs) – We proposed to allow the proposed rate per FTE as there is a decrease in spend due to more training activity in Belfast rather than Dublin.
- 6.27. Recharges – SSE Airtricity requested an annual increase of 1% above inflation, which we proposed to disallow as allowances are already inflated annually by RPI as with other salaries. SPC20 recharges will be set at the level incurred in 2018.

Response to Consultation

- 6.28. SSE Airtricity made no comment on these allowances in its response to the consultation.

Final Determination

- 6.29. It is the decision of the UR to maintain these costs at the level laid out in the consultation.

Operation Costs

Table 2: Operation Costs

Tariff Costs	SSE Airtricity Submission			UR Consultation			UR Decision		
	2020	2021	2022	2020	2021	2022	2020	2021	2022
Office Costs	377	384	390	377	384	390	377	384	390
Rates	48	49	51	48	49	51	48	49	51
Professional and Legal Fees	143	143	142	143	143	142	143	143	142
Insurance	27	27	27	27	27	27	27	27	27
Information Technology	830	682	653	830	682	653	418	418	418
CAPEX	23	23	22	22	22	21	22	22	22
Licence Fee	2	2	2	2	2	2	2	2	2
Network Maintenance	143	154	166	86	94	104	86	94	104
Customer Engagements	248	266	286	61	63	65	67	69	71
Total	1,841	1,730	1,737	1,596	1,465	1,453	1,190	1,208	1,225

IT

- 6.30. In SPC17, SSE Airtricity was provided a CAPEX allowance to upgrade its existing billing system, which was deemed no longer fit for purpose. This project was originally planned for implementation during SPC17. However, the billing system's owner was subject to a takeover and the proposed upgrades were deemed to be no longer efficient or the best option for the long term interests of customers.
- 6.31. During SPC17, SSE Airtricity notified the UR that it was scoping an upgrade to a new billing system. At the time of the SPC20 consultation, the UR was still liaising with SSE Airtricity on the required CAPEX for the new billing system and the cost was therefore excluded from the consultation. However, the expectation was that the new system would be implemented early in SPC20.

Response to Consultation

- 6.32. Due to changes in the approach to replacing the billing system, SSE Airtricity proposed retaining the existing billing system for an additional two years. This would allow SSE Airtricity to undertake a full procurement and ensure that the best value for money for current and future customers is obtained.
- 6.33. The supplier proposed that the IT CAPEX allowance will be determined

through the E_t term of the price control following completion of the procurement process.

- 6.34. SSE Airtricity proposed to maintain the existing level of IT OPEX for years 1 and 2 of SPC20, as the supplier will still be using its existing system. However, the supplier provided a considerably higher estimate for year 3 of the control (when a new system is expected to be implemented).
- 6.35. In its response to the consultation, CCNI questioned how SSE Airtricity's IT costs had been scrutinised by the UR. However, we would expect these specific concerns would be mitigated by the supplier now undertaking a full competitive procurement.

Final Determination

- 6.36. Whilst a delay in the implementation of the new billing system is not ideal, we accept that it is more preferable than implementing a system that may not represent good value for money for customers.
- 6.37. For IT OPEX, we have determined to maintain the allowance at the existing level for all three years of the SPC20. Whilst the supplier is likely to have a new system implemented in year 3 of SPC20, it is unclear how the IT OPEX costs of a new system will compare to the existing level of IT OPEX and the existing IT OPEX is the only reliable benchmark we have.
- 6.38. For IT CAPEX, we agree that the allowance should be determined through the E_t process following completion of the procurement process. We will engage external consultants to perform an assessment of, and provide an opinion on, these IT costs once they are provided during the SPC20 control period.

Customer Engagement

- 6.39. SSE Airtricity requested an allowance to support customer engagement to increase awareness of their services and obligations around energy theft, vulnerability (and awareness of energy care register), energy efficiency and back-billing. SSE Airtricity proposed a frequency of two postal communications on average per year to customers.
- 6.40. Customer Engagement and Information is important to help ensure customers are aware of the services available. However, we do not believe an increase of over £200k per annum is in the best interests of consumers.
- 6.41. In the consultation, we proposed to allow the cost of print for one additional communication per year which can be added to the existing mailing (bills/PAYG statements/tariff changes/EE Directive etc.). This extra communication will be approved by UR and must not contain references to

other SSE Airtricity services such as Energy Services.

Response to Consultation

- 6.42. SSE Airtricity responded asking for an allowance of c.£176k per year to undertake three communications per year to customers on various matters.
- 6.43. The supplier added that in the consultation, the UR identified the costs associated with some payment methods, and the associated banking charges, as one area where SSE Airtricity have been given a target to reduce costs from their current level. Therefore, the supplier proposed to communicate with credit customers who are paying by debit and credit card to make them aware of other payment methods, which could potentially reduce future banking costs.
- 6.44. In its response, CCNI stated that SSE Airtricity can undertake any such engagement at a low marginal cost if it “*maximises the use of existing scheduled communications and maximises the use of low cost online and digital technologies and tools*”.

Final Determination

- 6.45. As in the consultation, we do not believe that SSE Airtricity’s proposal of a significant increase of customer engagement costs is in the best interests of consumers. We expect the allowance provided will adequately support SSE Airtricity’s communication program.
- 6.46. However, we acknowledge that in the consultation paper we proposed a card payment cost glide path, diminishing across the three years of the control which is designed to incentivise SSE Airtricity to take steps to encourage customers to use more efficient payment methods. Therefore, we have allowed the additional cost of print for one communication to those customers per year (+£6k) which can be added to existing mailing.

Other Operations Costs

- 6.47. Office Costs (including stationery, telephone and postage) – SSE Airtricity’s submission was in line with previous annual increases which we proposed to allow.
- 6.48. Rates – SSE Airtricity applied a nominal 3% uplift above inflation (as per the last price control) and proposed rates to be a pass through cost. We proposed to allow these costs as submitted.
- 6.49. Professional and Legal Fees - Legal and company secretarial charges are fixed service charges. Payroll recharges are allocated by headcount and tax recharges have been agreed at 18/19 costs subject to inflation. We proposed

to accept SSE Airtricity's submission as the costs are at the current level.

- 6.50. Insurance – SSE Airtricity's submission forecasted a decrease for the 2020-2023 price control period. Insurance and interest charges decreased slightly and we proposed to allow these costs.
- 6.51. CAPEX (non-IT) - We proposed to allow the amount of £300 per FTE for the duration of SPC20.
- 6.52. Licence Fee – We proposed to allow the costs for licence fees.
- 6.53. Network Maintenance (including safety inspections) – Following assessment by the UR, SSE Airtricity resubmitted these costs as its original submission included costs in excess of licence obligations. We proposed to accept SSE Airtricity's re-submission as the unit rates for maintenance items and safety inspections are set by the network company and the volumes are retrospectively adjusted.

Response to Consultation

- 6.54. SSE Airtricity made no comment on these allowances in its response to the consultation.

Final Determination

- 6.55. It is the decision of the UR to maintain these allowances at the level laid out in the consultation.

Billing Costs

Table 3: Billing Costs

Tariff Costs	SSE Airtricity Submission			UR Consultation			UR Decision		
	2020	2021	2022	2020	2021	2022	2020	2021	2022
Bad debt	300	312	325	193	201	209	201	210	218
Paypoint costs & credit check costs	505	521	538	505	521	538	505	521	538
Bank and Interest Charges	274	287	301	274	232	185	274	232	185
Meter reading	783	797	855	783	797	855	783	797	855
Customer Information P+P	580	617	657	453	491	530	510	549	591
Tracing costs	33	35	37	33	35	37	33	35	37
Text alerts	6	8	12	6	8	12	6	8	12
Total	2,480	2,578	2,725	2,246	2,284	2,366	2,311	2,352	2,436

Bad Debt

- 6.56. The SPC17 SSE Airtricity price control included a bad debt allowance of 0.9% of tariff credit revenue. This was much higher than FES as the historical situation inherited by SSE was a poor record with debt management.
- 6.57. For SPC20, SSE Airtricity requested a bad debt rate of 0.7% of Credit Tariff Revenue. It stated this level will offer a degree of protection to the supplier against the market changes and risks to recovery that they are currently experiencing.
- 6.58. However, in our consultation we noted that significant improvements have been made to their processes which has delivered substantial outperformance of the current target in SPC17. The actual levels achieved are well below the current allowances and we therefore proposed a rate of 0.45%, which is the current LBE level.

Response to Consultation

- 6.59. SSE Airtricity stated that it was concerned that the UR had not adequately considered the impact of proposed regulatory changes to the market in respect of revenue protection, back billing, codes of practice for energy theft, and the potential impact of the consumer protection programme currently being developed by the UR.

- 6.60. The supplier requested that a bad debt allowance of 0.64% of tariff credit revenue be set for the forthcoming price control. This is based on the supplier's average bad debt costs between 2015 and 2019. The effect of this is a request for an additional c.£256k over the three-year price control period.
- 6.61. In its response, CCNI stated that SSE Airtricity Gas Supply's Bad Debt SPC20 allowance should be no higher than the current target of 0.45%. CCNI added that UR should benchmark the bad debt rate with the level set for energy suppliers in GB and ROI, as well as FES in NI.

Final Determination

- 6.62. We do not believe that an average of 2015-2019 is an appropriate level to set for the supplier's Bad Debt. SSE Airtricity's Bad Debt has fallen consistently year-on-year resulting in a significant outperformance. An average of the last 4 years will not reflect the improvements the company has made toward its resourcing, processes, and current levels of Bad Debt.
- 6.63. However, the bad debt allowance for FES was calculated using an average of the last two years. Therefore, in order to maintain consistency between the two regulated gas suppliers we recalculated the SSE Airtricity's bad debt percentage in line with this methodology.
- 6.64. Therefore, a rate of 0.47% of tariff credit revenue will be used to calculate SSE Airtricity's Bad Debt for SPC20.

Bank & Interest charges

- 6.65. Since the SPC17 determination there have been significant changes to bank charges and card fees for SSE Airtricity which they claimed were been wholly outside the control of the business. They have experienced an increase in banking charges of approximately 80% to date during the current Price Control.
- 6.66. SSE Airtricity stated that bank charges have increased for a number of reasons; including merchant fee rate increases, customer growth and online payments and changes in payment arrangements due to EU Payment Services Directive 2 which came into effect on January 2018, and prevents charges from being passed through to customers paying by credit card. The main reason for the increase in bank charges is the increase in the costs of card payments.
- 6.67. However, we believe SSE Airtricity could do more to minimise these costs. For example, its website offers card payments overtly on their homepage and its call centre hold message advises customers of the website card payment option rather than more cost effective collection methods such as

Direct Debit or Paypoint card.

- 6.68. SSE Airtricity submitted additional information which indicates that over a third of all payment transactions for credit customers who are not on direct debit are card payments, which benchmarks very poorly versus Power NI and FES.
- 6.69. For card payment costs we proposed a glide path, diminishing across the three years of the control which will allow SSE Airtricity to take steps to encourage customers to use more efficient payment methods.
- 6.70. The other cost items that make up the total bank charges we proposed to allow as they move in line with customer growth.

Response to Consultation

- 6.71. SSE Airtricity made no substantive comment on this allowance in its response to the consultation.
- 6.72. CCNI stated that SSE Airtricity should have a degree of control over the Bank and Interest Charges that it incurs, and it can promote cheaper payment methods such as direct debit.

Final Determination

- 6.73. It is the decision of the UR to maintain the costs for Bank & Interest charges at the level laid out in the consultation.

Customer Information/Bill Printing and Postage

- 6.74. Bill processing is a cost that is subject to retrospective adjustment relating to allowance for billing statements, tariff review letters, bad debt letters, welcome packs for new customers and any licensed obligations that require writing to tariff customers. The rates for printing and postage of these are set by the UR for the control period and the allowances adjusted for the volumes of letters sent.
- 6.75. In its initial submission SSE Airtricity detailed the expected mailing requirements for SPC20 and then based its forecasts on increasing this cost with customer growth. Rates for print and postage vary slightly across the SPC20 period.
- 6.76. Stationary and postage rate increases are in line with previous trends and we proposed to allow these costs.
- 6.77. The welcome pack issued to new customers and tariff sheets which are issued to all tariff customers following a tariff change contain an advertisement for SSE Energy Services (an unregulated company). We

proposed a reduction of £10k per annum to reflect the benefit to SSE Energy Services.

Response to Consultation

- 6.78. Due to the billing system upgrade not proceeding as planned, the supplier stated that consumers will not be able to benefit from the reduction in stationary costs that were expected for the price control period.
- 6.79. Reverting to its existing prices, the supplier recalculated that its bill print vendor costs for the 3 years will be higher by approximately £176K over the three years when compared with its initial submission.
- 6.80. In its response, CCNI commented on the disparity between allowances and actual spend, stating: “SSE Airtricity Gas Supply spent £257k on stationary and postage compared to an allowance of £521k. The LBE for 2018 of £420k is still significantly lower than the £542 SPC17 FD allowance”.

Final Determination

- 6.81. As this cost line is retrospectively adjusted we can assure CCNI that SSE Airtricity does not benefit from any under spend.
- 6.82. We accept SSE Airtricity’s revised Customer Information / Bill Printing and Postage submission, as the changes to stationary costs represent a continuation of what the supplier is currently paying. Any increase from the consultation is counter-balanced by the lower IT OPEX costs for years 1 and 2 of SPC20.

Other Billing Costs

- 6.83. Paypoint Costs & Credit Check Costs - We proposed to accept the SSE Airtricity submission as the rates are agreed and numbers are retrospectively adjusted.
- 6.84. Meter reading - We proposed to accept the SSE Airtricity submission as the rates are set and numbers are retrospectively adjusted.
- 6.85. Tracing Costs - We proposed to accept the SSE Airtricity submission as the rates are in line with customer growth.
- 6.86. Text Alerts - We proposed to accept the SSE Airtricity submission as cost increases will have minimal impact on the tariff. We believe increased utilisation will benefit customers by improving communications.

Response to Consultation

- 6.87. SSE Airtricity made no comment on these allowances in its response to the

consultation.

Final Determination

- 6.88. It is the decision of the UR to maintain these costs at the level laid out in the consultation.

7. Gas Costs

- 7.1. Gas Costs relate to the cost of wholesale gas as well as the costs for transporting gas through Great Britain (GB) to the SNIP. These transportation costs are published by National Grid⁸. Previous controls have determined that these costs are pass through which means that SSE Airtricity is allowed to recover the actual cost of gas. Therefore, where wholesale gas costs increase or decrease, the difference in costs is passed on to customers.
- 7.2. In the Information Paper, we proposed to allow wholesale gas costs and the related transportation costs as pass through costs. Wholesale gas costs will be allowed as pass through at the level purchased at the National Balancing Point (NBP).

Energy Balancing

- 7.3. In reviewing the gas costs we consider it appropriate to set an additional allowance for energy balancing. The energy balancing amount is a figure included within the tariffs to account for the cost of buying gas within the month as opposed to on the forward curve. The actual wholesale cost of the gas remains pass through, this figure is to ensure the tariff reflects the impact of the timing of purchasing the gas. SSE Airtricity will hedge the majority of their purchases before the month but some gas will remain to be purchased within the month to match the actual consumption profile.
- 7.4. We will set the energy balancing figure in the tariff as follows:
- Where SSE Airtricity has 40% or less of their gas requirements for the month remaining to be secured, there will be a 10% premium applied to the remaining gas to be purchased.
 - Where SSE Airtricity has more than 40% of their gas requirements for the month remaining to be secured, there will be a 10% premium on 40% of the total purchases for the month.
- 7.5. This is in line with the energy balancing figures currently within the SSE Airtricity tariff.

Credit Support

- 7.6. SSE Airtricity submitted details of credit arrangements in place to cover transmission, distribution, and gas costs and other relevant costs. Currently

8 National Transmission System (NTS) charges: <http://www2.nationalgrid.com/uk/Industry-information/System-charges/Gas-transmission/Current-charges/>

credit cover costs are allowed at an agreed pence per kWh.

- 7.7. The submission for the supplier's credit costs were reasonable when benchmarked to other suppliers in the energy supply industry. We therefore proposed to allow this level of credit cover.

Response to Consultation

- 7.8. SSE Airtricity made no comment on gas costs in its response to the consultation.
- 7.9. CCNI asked UR to specify which suppliers it has benchmarked against and to ensure the list includes suppliers outside NI

Final Determination

- 7.10. The UR has benchmarked SSE Airtricity's Credit Support to NI energy supply companies, as these companies best reflect the conditions faced by the supplier. As stated previously, the UR would not have the in-depth and commercially sensitive information required to develop reliable benchmarks outside of the NI energy market.
- 7.11. We determine that gas costs will remain as pass through costs.

8. Margin

- 8.1. During SPC17, we conducted a complete review of margin in line with the methodology used for the previous Power NI supply price control using a notional supply business capital base and the cost of capital to calculate an appropriate margin.
- 8.2. The SPC17 Final Determination approved a margin of 2% of allowable turnover. This was determined to strike an appropriate balance between the calculations of the CMA, UR external consultants and both SSE Airtricity and FES and their advisors, whilst at the same time taking account of other benchmarks in the energy industry.
- 8.3. We do not believe that market conditions have changed sufficiently to warrant any amendment to this level of margin. SSE Airtricity retains a dominant position in supply to price regulated customers (and is the monopoly supplier to domestic customers in West) in the Greater Belfast area and has associated market power. This is one of the principal reasons for the continuance of the price control, and SSE Airtricity still has more market share and fewer competitors than Power NI had when the 2.2% was set for that supplier.
- 8.4. Given all the above and after due consideration, we are satisfied that the calibration of the margin still reflects the appropriate benchmarks. We informed SSE Airtricity that the UR has no specific intentions to modify this or put in place an alternative level of allowed margin.

Response to Consultation

- 8.5. CCNI agreed with UR's assessment that the regulated retail market conditions in Greater Belfast have not changed sufficiently during the first two years of the SPC17 period to consider increasing the margin. However, the consumer body questioned whether current level of margin was too high.
- 8.6. SSE Airtricity stated that it was disappointed that the UR did not agree to increase the margin, and that it would have preferred to see a consistent approach applied across all regulated energy supply businesses, with a margin of 2.2% being applied to all regulated suppliers.

Final Determination

- 8.7. As stated above, during SPC17 we conducted a complete review of margin to calculate an appropriate level, and we do not believe that market conditions—or SSE Airtricity's dominant position in the market—have changed sufficiently to warrant any amendment to this level of margin.

- 8.8. The margin for the price regulated electricity and gas supply companies differs primarily due to the additional working capital commitments electricity suppliers face due to the payment terms of the Single Electricity Market (SEM).
- 8.9. Therefore, it is the decision of the UR to maintain the 2% margin laid out in the consultation.

9. Reconciliation

9.1. This section sets out how the price control will be reconciled to actual allowed costs on an annual basis.

Reconciliation

9.2. On an annual basis we will reconcile the forecast costs that are allowed in the price control with the actual allowed costs (i.e. the retrospectively adjusted allowed costs) to determine a reconciliation amount. This amount will then form part of the k factor.

9.3. The reconciliation will take into account:

- Billing costs which are retrospectively adjusted
- Ring-fenced allowances (if any)
- Inflation
- Rate of interest applicable
- Possible Other items (to be confirmed)

9.4. In addition to the information required to complete this reconciliation, we will also require from SSE Airtricity annual cost reporting to show their actual costs on a line-by-line basis reconciled with regulatory accounts.

Inflation

9.5. All costs presented in this paper are in October 2018 prices. These costs will be adjusted to account for inflation where appropriate. Inflation will be treated as a pass through. The costs used to make up the tariff at each tariff period will be adjusted to reflect the current price base. For reconciliation purposes the inflation figure will be the average figure for the year being reconciled. The inflation index used will be Retail Price Index (RPI).

Rate of Interest

9.6. In the Consultation Paper, we proposed that any reconciled amounts, whether under or over recovered, will be rolled forward at an interest rate of LIBOR plus 1.5%. The proposed rate of interest reflects the cost to the suppliers of financing the under recovery or the benefits to them of holding any over recovery.

Response to Consultation

9.7. SSE Airtricity made no comment on reconciliation in its response to the

consultation.

Final Determination

- 9.8. It is the decision of the UR that reconciliation will remain structured as it was in SPC17; as is laid out in the consultation.

Annex 1

Apportionment Cost Drivers

Cost	Driver
Manpower	FTEs
Staff Engagement	FTEs
Training	FTEs
Recharges	FTEs
Travel and Subsistence	FTEs
Office Costs including stationery, telephone and postage	FTEs
Rates	FTEs
Professional and Legal Fees	Customer number
Insurance	FTEs
IT OPEX	Customer bills
IT CAPEX	Customer bills
Licence Fee	Load in therms
Network Maintenance including safety inspections	SSE Airtricity Energy Care Scheme customers ⁹
Customer Engagements	Customer number
Bad debt	Credit Revenue ⁹
Paypoint costs & Credit Check Costs	PAYG customers ⁹
Bank and Interest Charges	Load in therms
Meter reading	Customer numbers ⁹
Customer Information Bill Processing and Postage	Customer numbers ⁹
Tracing Costs	Customer numbers
Text Alerts	Tariff only

⁹ This is how this cost line is apportioned for this final determination. This cost is then retrospectively adjusted to actual numbers.