



SSE Airtricity Gas Supply Northern Ireland Ltd.

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

Consultation Response

September 2019

Introduction

SSE Airtricity welcomes the opportunity to comment on the Utility Regulators (UR) consultation on the SPC20: Price Control for SSE Airtricity Gas Supply (NI) Ltd.

SSE Airtricity is the second-largest provider of energy and related services operating across Ireland with almost 740,000 customers served across both electricity and natural gas markets. In Northern Ireland, SSE Airtricity is in a unique position of being the largest competitor to the incumbent electricity company, while also being the incumbent gas supplier in the Greater Belfast area. We are committed to the development of competition in the Northern Ireland and Irish energy markets and to presenting our customers with choice and quality customer services.

Table of Contents

Introduction	2
Table of Contents.....	2
1. Overview	3
2. Scope and Duration.....	4
3. Key areas of challenge	4
Manpower.....	4
Contingency	5
Bad Debt	5
Customer Engagement	6
4. Impact of change in approach to replacing the billing system	6
Manpower efficiencies.....	7
IT Cost of Capital	7
IT Operation Costs.....	8
Bill Print Vendor Costs	8
5. Conclusion.....	8

1. Overview

The Utility Regulator (UR) published its SPC20 approach document for consultation in November 2018. Since then SSE Airtricity Gas Supply Northern Ireland (SSE Airtricity) has been engaging with the regulator in the price control review process. SSE Airtricity made its initial submission to the UR for the allowances required to run the business in SPC20 period in January 2019. SSE Airtricity has engaged with the UR during the Draft Determination (DD) development stage seeking to ensure the regulator fully understands the requirements of the business and its objectives over the SPC20 period.

The UR published its consultation on SPC20 in June 2019 which set out its view and position on the costs being sought by SSE Airtricity. We welcome the recognition in the consultation that significant changes are required to our existing billing systems. SSE Airtricity has engaged with the Utility Regulator over the last few months and has proposed modifying its approach to this project and as a result procurement will not be completed in advance of the SPC20 price control determination.

SSE Airtricity cannot reconcile some of the proposed allowances with the overall costs of the business or the proposals made. Unfortunately, this means there are significant shortfalls in proposed allowances in several areas which are business critical. This paper therefore sets out additional challenges to the proposals set out in the consultation paper in addition to the changes in resources required to continue to operate the HiAffinity billing system during the SPC20 price control period.

SSE Airtricity has met with the UR to set out the impact modifying the approach to changing the billing system, which impacts on both the consultation proposals and any final determination. Over the course of the consultation period we have provided clarification and additional information on our submission as well as further information following the publication of the consultation paper. We consider that the evidence we have provided during this process supports changes to the proposals in the consultation and that it would be unreasonable to expect SSE Airtricity to otherwise operate in absence of these required allowances to deliver both its regulatory and customer obligations.

We have proposed a number of other changes to the consultation proposals to reflect the operating costs and capital costs for retaining the existing billing system during the price control period as well as reinstating several efficiencies that had been assumed to be realised within the price control period.

SSE Airtricity welcomes the UR's recognition that a regulated business needs to make an adequate return on its investment, however we are disappointed that the UR has not increased this return above the 2% allowed in the SPC17 period and 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. It is important that the UR recognises that Northern Ireland retail energy businesses need to remain sustainable, and furthermore, attractive to investors in the long run.

While the UR's consultation paper is supportive in general of the changes made by SSE Airtricity, given the increasing customer base, increased customer service opening hours and regulatory changes expected over the next price control period, SSE Airtricity is of the opinion that some of the assumed efficiencies, particularly in respect of manpower and bad debt, are not justified. SSE Airtricity provides additional confidential information to this response to demonstrate the relevant business needs over the SPC20 price control period.

2. Scope and Duration

The UR set the price control period for the next control to 3 years. This means the next price control will be in place from 1 April 2020 – 31 March 2023.

SSE Airtricity support the proposed price control period and the customers bands to which it will be applied.

3. Key areas of challenge

Section 4 of this paper sets out how we have adjusted the proposals from the consultation paper to exclude any changes that were directly as a result of a proposed new billing system implementation which had been incorporated into our original SPC20 submission. We have assumed this as our revised baseline for this consultation response.

This section outlines where SSE Airtricity has serious concerns with the proposals put forward in the UR's consultation and where change is needed to ensure sufficient allowances are available to effectively operate its business, to deliver best in class for customers, and fulfil license obligations.

Manpower

One of the biggest challenges facing the business is the adequacy of resources to support a growing customer base which has grown significantly in the current price control period and is forecast to grow by a further c20% from 18/19 to the end of SPC20.

To maintain a high quality, compliant service, we need to ensure that resource capability is scaled appropriately to manage demand growth. A summary of the changes needed for the continuation of the HiAffinity billing system as well as the additional resource requirement is set out separately in the attached manpower paper. These additional requirements are separate to the proposal in regard to the manpower efficiencies which had originally been attributed to the new billing system set out in Section 4.

Our approach is to deliver our services and obligations with a suitable staff level, whilst acknowledging that all costs need to be justifiable. As a regulated business, we are mindful of the impact that increased operating (and specifically manpower costs) can have on consumers.

However, we are also a business with responsibilities regarding our employees and those customers who choose to be supplied by us. There is a balance to be struck between efficiency of costs (since our costs are borne by our customers) and being able to attract and retain the calibre of skills and experience necessary, to deliver service excellence and to meet our regulatory obligations.

We were disappointed that the URs SPC20 consultation has used limited comparators to benchmark our resourcing requirements. It is not clear from the consultation paper that the UR has fully considered the enhanced opening hours of our call centre, which operates for 25% more hours per week than the company we have been benchmarked against. This drives a higher resource requirement.

SSE Airtricity does not agree that the resourcing levels proposed in the SPC20 consultation are sufficient when taking into consideration the additional operating hours and increasing customer numbers.

However, given the increased customer numbers since the last price control estimates, SSE Airtricity is of the opinion that there is justification for additional resources in relation to back office and credit control operations for each year of the price control period to help manage the increased activity associated with increasing customer numbers along with disproportionate increases to meter exchanges and change of tenancies etc.

We have set out our view on the allowance separately, however we would like to highlight that a sustained reduction in Bad Debt at a time when customer numbers are increasing can only happen with adequate resourcing to manage the manual credit processes. In the absence of appropriate resourcing SSE Airtricity will be penalised as a result of increasing customer numbers if it cannot maintain the final level of Bad Debt set out in the final determination.

Contingency

SSE Airtricity is concerned that its current manpower allowance, does not provide the capacity to backfill heads during periods of prolonged absence or support normal ongoing commitments which a business would usually face in a diverse employee population (maternity cover, workload gap rising from Long Term Sickness in post and force majeure absence). SSE Airtricity has previously provided additional supporting evidence in respect of maternity and sickness costs and believes that it is reasonable for an appropriate level of these costs to be recovered to enable it to be able to maintain its services to customers and compliance with licence conditions.

Bad Debt

SSE Airtricity has previously submitted substantial information in relation to its bad debt costs as part of its initial submission. Within this paper we have highlighted a number of key risks that justify a bad debt allowance of 0.7%.

- We have demonstrated that on average the cost of bad debt is around 0.64%, the proposal of 0.45% set out by the UR in the consultation paper is based on the best year SSE Airtricity has ever had. It is unrealistic to expect SSE Airtricity to sustain this low level of bad debt for the three-year price control period, particularly given the uncertain future economic environment, increasing customer numbers and no substantial increase in manpower to support the maintenance of the allowance at this level
- We are already experiencing challenges as a result of new engagement measures associated with the increased time consumers are taking to clear their bills (on average 30 days longer)
- Rising levels of revenue protection incidents up over 25% from 2017 - 2018

Furthermore, we do not feel that the Utility Regulator has considered the impact of proposed regulatory changes to the market in respect of back billing, codes of practice for energy theft, and the potential impact of the consumer protection programme currently being developed by the Utility

Regulator. SSE Airtricity also consider that continued work to reduce LTNA will only increase bad debt due to further detection.

Finally, there are potential significant risks arising out of a no-deal Brexit and the impact of this on UK/NI economic prospects.

We are therefore requesting a bad debt allowance based on the average bad debt over the last 3 years.

Customer Engagement

SSE Airtricity requested an allowance to support customer engagement to increase awareness of its services and obligations around energy theft, vulnerability (and awareness of energy care register) and energy efficiency. SSE Airtricity initially proposed a frequency of two postal communications, on average, per year to customers.

SSE Airtricity does not agree that the proposal 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.) is sufficient to raise awareness of our services and obligations.

SSE Airtricity requests that the UR consider revising the proposals from the SPC20 consultation to allow for one additional communication to go out with bills and one further communication, including stationery & postage costs to facilitate a timed communication outside normal billing inserts. The proposals put forward in the consultation paper would restrict our ability to target a number of key communications that have been discussed with the UR for example: a further communication with each bill to quarterly credit customers regarding payment methods aimed at helping to reduce bank charges on card payments as per direction given in SPC20 Consultation.

The average cost of these proposals is £0.95 per customer, in year one rising to £1 in year 3. This is in line with previous allowances provided by the Utility Regulator for other regulated suppliers such as Power NI.

Please note, while SSE Airtricity is aware of the UR's CPP, at this time the detail of what is proposed in a number of areas is unknown. We have based our submission on customer engagement around known areas of work. In the event the CPP sets out an increased mandatory requirement in this area we will discuss this further with the UR once the details are known.

4. Impact of change in approach to replacing the billing system

At the time of making its submission in January 2019, SSE Airtricity and the UR were of the view that SSE Airtricity would be progressing a billing project to replace Hi Affinity at an early stage of the price control and efficiencies associated with the new system formed part of the original submission. Due to changes in the approach to replacing the billing system there are a number of key changes we are proposing to reflect the costs of operating the business using the existing billing system.

The net effect of retaining the existing billing system for an additional two years in the price control period results in a reduction from the proposed allowance in the consultation paper. Allowances for the capital cost of the new IT systems are proposed to be dealt with using the existing E_t element of the price control formula.

This change in approach has impacted a number of areas including:

- Manpower efficiencies
- IT Cost of Capital
- IT Operation Costs
- Bill Print Vendor Costs

This section explores the impact of removing the costs associated with introducing a new billing system and retaining the existing system for two years of the price control period with a replacement billing system being introduced in year three of the price control period.

There are a number of assumed additional efficiencies in relation to manpower proposed by the UR resulting from the introduction of a new IT system that had been included in the consultation that we have interpreted as being excessive and would result in a significant reduction in operational resources. We are requesting to reinstate a number of these proposed efficiencies to enable the continued efficient operation of the business using the existing billing system. We still expect efficiencies to be derived from deployment and embedding of a new billing system, and future efficiencies will be subject to further engagement with the UR.

Manpower efficiencies

The manpower requirements that were set out in the initial submission were based on the implementation of a new billing system, and had already assumed efficiencies by year 3, the consultation paper has proposed additional efficiencies which, if applied, would have a detrimental impact on the ability to operate the business efficiently, and meet our obligations and deliver a best in class service to our customers.

Given the need to retain HiAffinity for the majority of this price control period the allowances proposed are insufficient to support the necessary staff and their costs for the duration of the price control. In our initial proposal, we had already assumed manpower efficiencies in the years following the introduction of a new billing system.

The original submission made an assumption that there would be no efficiency gains in year 1. The reinstatement of these manpower efficiencies returns the business to the proposed headcount for year 1 of the consultation, which is now rolled forward for years 2 and 3.

IT Cost of Capital

Due to changes in the approach to replacing the billing system SSE Airtricity is proposing to remove this line item. We are proposing that the relevant cost for a new billing system will be addressed through the E_t element of the price control formula.

IT Operation Costs

Due to changes in the approach to replacing the billing system SSE Airtricity is proposing to amend the IT OpEx cost in all years of the price control. The OpEx costs should revert to the HiAffinity costs structure for years 1 and 2.

In year 3 it is assumed that there will be additional OPEX costs associated with a new billing system. This is to allow for any increased licencing, support and maintenance costs associated with a new billing system which have not yet been determined.

Bill Print Vendor Costs

With a change to the approach of replacing the billing system, SSE Airtricity will not be able to avail of the original proposed change in bill print vendor and associated cost savings. SSE Airtricity will be required to retain the existing Bill Print Vendor while it remains on the HiAffinity system. SSE Airtricity has amended its revised submission for the bill print vendor costs with the costs of the current provider.

5. Conclusion

SSE Airtricity and the UR have engaged extensively through the price control review process. This has been a two-way engagement and SSE Airtricity has provided full and detailed information and evidence to support its original submission, any follow up requests for information received and its further submission based on the consultation.

SSE Airtricity is happy to provide further evidence should this be deemed required, however given the level of detail now available to the UR, we believe a fully informed decision can be made to reach appropriate allowances for our business.

The overall objective has been to reach a price control determination where there is clear understanding of the actual costs faced by the business and the return on investment needed to sustain the business.

SSE Airtricity recognises that the change in timing of the procurement exercise for the new billing system has an impact on the proposals in the UR's consultation and requires changes to manpower and IT OpEx and CapEx costs to enable SSE Airtricity to appropriately operate the business over the next 3 years.

We also recognise the support the UR has given to this project which will be progressed over the next price control period.

Separate to the impacts around procurement of the billing system, there are a number of areas where the UR has not allowed sufficient allowances to allow the business to operate in a sustainable way. SSE Airtricity has provided evidence to support changes to proposed allowances and trusts that the UR will consider these and make appropriate amendments in its final determination.