CER Information Note

GNI Allowed Revenues for PC4
(From 2017 to 2022)

Summary Information Note

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Regulating Water, Energy and Energy Safety in the Public Interest

The Exchange, Belgard Square North, Tallaght, Dublin 24, Ireland
+353 1 4000 800  |  info@cer.ie  |  www.cer.ie
1. Introduction

1.1. The Commission for Energy Regulation

The Commission for Energy Regulation (CER) is the independent economic regulator for the natural gas, electricity and water sectors in Ireland. Our mission is to regulate water, energy and energy safety in the public interest.

Part of the CER’s responsibilities involve setting the level of revenue which GNI in its role as the gas network operator can recover from its customers. The CER does this by reviewing the GNI business and setting appropriate revenue allowances for operating costs\(^1\), capital costs\(^2\) and other items. One of the CER’s goals in this area is to protect the current and future interests of consumers, while ensuring a stable environment for GNI to obtain finance from investors.

The CER is now issuing its decision regarding the level of revenue that GNI will be allowed to recover to run its business for the period October 2017 to September 2022 (known as PC4). In reaching this decision, the CER has sought to protect the gas customers by ensuring that GNI only recovers efficient costs while delivering improvements in performance and service over time.

The process followed by the CER in completing this review mirrors that used in the three previous gas price controls and is in line with those carried out by other utility regulators worldwide.

This information note summarises the key points set out in the CER’s decision papers (CER/17/259 and CER/17/260).

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\(^1\) Operating costs are the day to day running costs of the utility. These costs are made up of line items such as staff costs, customer operations, insurances and licences amongst others.

\(^2\) Capital costs relate to GNI’s physical assets i.e. the gas network, vehicles, IT systems aswell as the upgrade, repair and maintenance of the existing network.
1.2. Public Impact Statement

The CER’s role is to protect gas customers by ensuring that GNI spends customers’ money appropriately and efficiently to deliver necessary services. The CER does this through what is called a Price Control which is carried out every 5-years, the next 5-year period starts on the 1st of October 2017 (PC4).

- A Price Control is an important process because the CER must carefully consider the level of money GNI needs to safely operate, maintain and invest in the gas network for the next 5 years.

The CER will continue to monitor GNI’s performance and will challenge GNI to become more efficient over PC4. The benefits to gas customers will be:

- A gas network that is operated to the highest safety standards, ensuring safe supply of gas to customers;
- A reliable and secure supply of gas to homes and businesses;
- The efficient management of the gas network resulting in stable tariffs; and
- A high standard of customer service at all times with timely resolution to complaints.

As a result of the PC4 transmission and distribution decision documents, the average annual residential customer’s\(^3\) bill will rise by €2.89. The estimated percentage effect is an increase of less than half a percent.

\(^3\) As per CER/17/042 the average domestic consumption for gas is c.11,000kWh. Based on these figures the average annual gas bill is approx. €760 for a standard plan.
Security of Supply
✓ Meet 1 in 50 obligations
✓ Emergency planning
✓ Reliable and secure supply of gas to homes and businesses

Innovation
✓ CNG
✓ Biomethane
✓ Power to gas

Safety
✓ Emergency response
✓ Gas network operated to the highest safety standards
✓ Carbon monoxide awareness
✓ Dial before you dig

PC4 Total Revenue Allowance 2017-2022
€1.9 billion

Transmission Revenue
€924m

Distribution Revenue
€990m

Impact on Customer Bill
€2.89

Customer Service Metrics
✓ Call Centre Response
✓ High standard of customer service at all times
✓ Complaints Metric
✓ Customer Survey

Incentives
✓ New connections
✓ Defer investment
✓ Reduce costs
✓ Stable tariffs

4 Image Credits: Latysheva Phil Smith AnanthTomas Knopp, Anil Setyo Ari Wibowo
1.3 Key Points

- **Total Revenue** - The CER has decided to allow GNI a total revenue of €1,913.3m (2015/16 prices) over the period of PC4 (2017-2022) with a Weighted Average Cost of Capital (WACC) of 4.63%. This represents a saving of €264.4m when compared to GNI’s request.

- **PC4 Tariffs** - Given the forecast gas demands CER’s decision will lead to a 2.30% increase in 2017/18 distribution tariffs (15/16 monies) and a 3.83% decrease in 2017/18 transmission tariffs. This will result in the average annual residential customer’s bill rising by €2.89 which is an increase of less than half a percent.

- **Ongoing Efficiency** - As with previous price controls the CER has set an annual ongoing efficiency to be applied to GNI’s transmission and distribution business. In this case, this is a 1% improvement in efficiency each year.

- **Catch-up efficiency** - Following a review of GNI’s relative efficiency to other gas network distribution operators the CER has decided on annual catch-up efficiency target of 0.75% to be applied to GNI’s distribution business.

- **WACC** - The CER has set a WACC of 4.63% pre-tax real. This is intended to cover the financing cost associated with capital expenditure. The WACC is used to derive a fair return for GNI on its efficiently incurred capital investments.

- **Customer Service Incentive** - Earlier this year, the CER published a decision paper on a number of customer performance indicators against which GNI will be incentivised over the course of PC4. The CER has decided that 0.25% of allowed revenue used for this incentive.

- **Growth Incentive** - The CER is mindful that continued utilisation of the gas network continues so that customer tariffs can be contained. With this in mind decided to introduce an incentive mechanism to challenge GNI to reach their original proposed connection targets for PC4. This will be reviewed in the last year of PC4 and will carry a reward /penalty for GNI. There will be a cap on the amount of money, which will be the subject of the reward or penalty, this will be €4m.

- **Innovation** - The CER has decided to allow funding of €20.0m for innovation over PC4. The CER will ensure that GNI report annually on the outputs and outcomes of the innovation funding and benefits it will bring to gas customers. This funding is provided

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5 CER/17096 GNI Customer Performance Indicators Decision Paper.
against the backdrop of the decarbonisation of the economy by 2020 and with a view to ensuring that the gas network will continue to be utilised to the benefit of gas customers.

2 Allowed Revenue

2.1 PC4 Distribution Revenues

The CER has decided to allow €989.6m to GNI for distribution over the period of PC4 with a Weighted Average Cost of Capital (WACC) of 4.63%. GNI sought revenue of €1.1bn based on their proposed WACC of 4.96%, over the period.

Table 2.1: PC4 allowed distribution revenues

<table>
<thead>
<tr>
<th>Revenue Allowance</th>
<th>GNI Request</th>
<th>CER Decision</th>
<th>Saving</th>
</tr>
</thead>
<tbody>
<tr>
<td>Total PC4 revenue</td>
<td>€1,122.6m</td>
<td>€989.6m</td>
<td>€133.0m</td>
</tr>
</tbody>
</table>

2.1.1 PC4 Distribution Capex

GNI requested a Capex Revenue Allowance of €529m\(^6\). The CER has decided to allow €332m. This is 37% lower than GNI’s request for distribution Capex. The CER is of view that the growth strategy, which includes GNI’s forecast for new connections, is overly ambitious and has as a consequence reduced the number to a more prudent number, which is slightly above the actual number of connections that took place in PC3. A summary of GNI’s distribution Capex\(^7\) over PC3 and the CER’s decision on allowed Capex for PC4 relative to GNI’s request is shown in Figure 2.1 below.

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\(^6\) This figure is net of customer contributions.

\(^7\) Net of customer contributions.
2.1.2 PC4 Distribution Opex

GNI Requested an Opex Revenues Allowance of €385m\(^8\). The CER has decided to allow €340m\(^9\). The CER has reduced the allowance in this area to 11.6\% less than GNI requested but still above the allowance in PC3. The CER has decided on a number of reductions in GNI’s requested Opex as stated in their business plan, including challenging efficiency targets where the CER consider there is scope for GNI to improve during PC4. A summary of GNI’s distribution Opex over PC3 and the CER’s decision on allowed Opex for PC4 relative to GNI’s request is shown in Figure 2.2 below.

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\(^8\) This is controllable Opex.
\(^9\) This is controllable Opex.
2.2 PC4 Transmission Revenues

The CER has decided to allow c. €924m to GNI for transmission over the period of PC4 with a WACC of 4.63%. GNI sought revenue of c. €1.05bn based on their proposed WACC of 4.96%, over the period.

Table 2.2 PC4 allowed transmission revenues

<table>
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<tbody>
<tr>
<td>Total PC4 revenue</td>
<td>€1,055.1m</td>
<td>€923.7m</td>
<td>€131.4m</td>
</tr>
</tbody>
</table>

2.2.1 PC4 Transmission Capex

GNI requested a Capex Allowance of €271m\(^{10}\). The CER has decided to allow €236m. The CER has not accepted the full work programme requested by GNI which is reflected in the CER’s decision being 13% lower than GNI’s request. This is mostly due to the disallowance of a Capex funding request for renewable gas injection facilities and a reduction in the pipe refurbishment and replacement work programme. A summary of GNI’s actual (outturn) Capex over PC3 and the CER’s proposed Capex for PC4 relative to GNI’s request is shown in Figure 2.3 below.

![Figure 2.3: Total net transmission capex over PC3 and PC4](image)

\(^{10}\) This figure is net of customer contributions.
2.2.2 PC4 Transmission Opex

GNI requested an Opex Allowance of €424m. The CER has decided to allow €385.5m. The CER’s Opex allowance is 9% lower than GNI’s Opex request. The CER recognises that delivering quality outputs for lower Opex allowances will be challenging. The CER is committed to continuing to ensure that GNI operates as efficiently as possible and therefore has set challenging efficiency targets for GNI over the PC4 period. Ensuring that GNI operates efficiently helps contain tariffs for consumers. These efforts to reduce costs must, however, be balanced against the requirements to deliver a reliable and safe service. A summary of GNI’s actual (outturn) Opex over PC3 and the CER’s proposed Opex for PC4 relative to GNI’s request is shown in Figure 2.4 below.

![Figure 2.4: Total controllable transmission opex over PC3 and PC4](image)

Further information regarding the CER can be viewed on [www.cer.ie](http://www.cer.ie). For further information on the above please see the CER’s decision paper (CER/17/259 and CER/17/260).