

30 September 2009

Mary Lavery
Energy Division
Department of Enterprise,
Trade and Investment
Netherleigh
Massey Avenue
Belfast
BT4 2JP

Dear Mary

Re: New Strategic Energy Framework (SEF) for Northern Ireland

Thank you for providing firmus energy with this opportunity to respond to the above.

We recognise that it is 5 years since the Department of Enterprise, Trade and Investment published its last Strategic Energy Framework which aimed to reduce energy costs, build competitive markets, enhance sustainability and maintain reliable energy supplies.

We also acknowledge that the expansion of the Northern Ireland gas network, the Single Electricity Market and the increased use of renewable energy are cited as key achievements of the 2004 SEF and we appreciate that the 2009 Strategic Energy Framework aims to achieve a competitive, sustainable and long-term future for energy in Northern Ireland.

These objectives are commendable when set against a background whereby;

- 70% of households still use oil as their primary source of home heating, and
- 47% of carbon emissions come from heat production

We feel much has been achieved, but more could and should be done. We believe that a key focus for energy policy should be;

- continued promotion of the natural gas industry in Northern Ireland in particular by optimising existing network infrastructure and seeking to extend that network where it is deemed economically viable
- to drive competition, especially within the domestic sectors, in both electricity and the Greater Belfast gas market
- to ensure that natural gas continues to play a central role towards reducing Northern Ireland's dependency on heavy carbon fuels
- to take account of the impact that fuel choice and energy prices has on fuel poverty
- to begin to take account of the large number (70% of households) that are offered no form of price or consumer protection by the oil, coal or LPG industries

- to promote energy efficiency and encourage CHP, particularly with regard to the potential for micro generation in homes and small businesses

firmus energy has only responded where we feel best placed to do so.

Chapter 2: Competitiveness

Before we can strive to encourage more companies to enter gas and electricity supply markets, we need to create conditions that will facilitate customer switching. firmus energy has written to the Utility Regulator on a variety of issues which must be addressed urgently in order to promote greater levels of retail competition in both gas (Greater Belfast) and electricity.

firmus energy is keen to understand what role the Regulator intends to take in addressing and overcoming each of the detailed issues which are necessary to enable new suppliers to compete on a level playing field.

Only by addressing these issues will suppliers want to actively participate in the market and in turn offer choice to consumers.

firmus energy feels that a strategy to incentivise gas connections and increase gas uptake should be adopted by both DETI and the Utility Regulator. Customers will not switch from their existing heating or hot water systems to natural gas without switching incentives. firmus energy would welcome increased collaboration between DETI and the Utility Regulator to promote the benefits of natural gas and to challenge policy makers to choose natural gas as a low carbon alternative to coal and oil, where it is available.

firmus energy intends to make proposals to both the Department and Government in early October 2009 on funding mechanisms, along the lines of the Reconnect programme for Renewable solutions, which can drive the availability and up-take of natural gas along the route of the NW & SN transmission pipelines.

The proposed incentive scheme will deliver a number of benefits:

- Reduce heating costs for owner occupied households
- Reduce carbon emissions where natural gas is available
- Increase gas availability for small businesses, reducing fuel bills and carbon emissions in the private sector
- Reduce cost and CO₂ emissions within the public sector estate

The costs of an incentive scheme for owner-occupier homes could be met via a partnership between firmus energy, the Northern Ireland Sustainable Energy Programme, coupled to Government funding support.

Unique to Western economies, oil is still a dominant energy player across Northern Ireland. Given the lack of formal regulation, consumer protection and indeed energy efficiency targets placed on the coal and oil industry, firmus energy would call upon DETI to undertake an evaluation as to what the energy mix in Northern Ireland needs should be.

That is to say:

- what percentage of homes and businesses do we wish to heat through oil compared to natural gas or renewables?

- where can we economically extend the natural gas network to deliver such an ambition for gas penetration?
- should Northern Ireland maximise gas penetration across the licensed areas, promoting renewable heat solutions in areas which are “off the gas network”?
- how can the Public sector play its part in driving down running costs and carbon emissions within its own estate by connecting to natural gas where available?

Given the current economic climate, natural gas has a key role to play in reducing the costs of living for householders, increasing bottom line profitability for businesses and providing efficiency cost benefits for the Public sector.

Natural gas has historically been the lower cost fuel for homes and businesses across GB, the Republic of Ireland and the rest of Europe and firmus energy’s “guaranteed cheaper than oil” price pledge ensures that customers looking to switch to natural gas can avail of the lowest possible costs for heating and hot water compared to other fuels.

Q. Are there particular or more radical actions which can be taken to accelerate greater competition in our retail energy markets – both electricity and gas?

Ans.

Greater Belfast Gas market:

Commercial barriers to competition (large IC contract sector)

Given our experience in tendering for large industrial and commercial (IC) businesses - i.e. gas customers using >25k therms p.a. - in the greater Belfast market, firmus energy is concerned at the lack of regulatory oversight on the incumbent and their resultant ability to meet, and indeed block, new supplier entrants.

This regulatory freedom is in stark contrast to the market opening experience in both GB and the Republic of Ireland, where the respective regulatory authorities ensured that the incumbent supplier(s) adhered to both Regulated pricing mechanisms and Codes of Conduct in the years immediately following market opening. On this basis, new supplier entrants were able to gain the necessary footholds in the large IC contract sector which could support full participation in the SME and domestic retail markets. firmus energy has already submitted, to both the Department and the Regulator, a dossier of activities which highlight the current deficiencies in competition arrangements in the IC contract sector and we would welcome an early response to these issues, for the benefit of all customers in Greater Belfast.

These deficiencies not only relate to the ability of the incumbent supplier to effectively price discriminate across its customer portfolio to enable it to retain market share, but also relate to the incumbent’s use of its existing contract terms to unduly delay, and at worst block, customer switching (for example, 90 day notice periods). firmus energy believes there should be greater regulatory oversight of the incumbents’ commercial offers whereby termination periods should be limited to a maximum of 60 days (or down as far as 30 days, as is the case on the Republic of Ireland) and that the incumbent should not be allowed to lock new entrants out of the market by offering contracts more than 12 months in duration. Both of these remedies were used for the benefit of gas customers at market opening in the Republic.

We also feel that all contract offers should be quoted using a standard template clearly separating out Transmission, Distribution, Gas costs, Supply costs, other costs (shrinkage, Moffat costs etc.) and Supply margin. Customers could then more accurately compare competitor quotes without fear of 'hidden charges' and new suppliers could have more confidence in the incumbent's inability to cross-subsidise its supply business.

To summarise, effective regulation of the large IC (contract) sector is critical if new suppliers are to be able to obtain a foothold in the Belfast gas market, develop a balanced portfolio for gas purchasing, and have the critical mass to operate in the smaller business and domestic sectors.

Systems arrangements

Currently only 25 - 50 meter points are able to be switched per week by Phoenix Distribution. This is wholly unacceptable.

In GB, more than 10 years after market opening 100,000 customers - equivalent to 0.5% of households - still switch their energy provider every week. If the equivalent pro rata numbers of customers in Greater Belfast were to switch gas suppliers, the Phoenix systems would need to cope with 550 switches per week. Currently they can cope with a maximum of 50, that is to say 9% of that number. firmus energy believes that in the first year or so of full domestic competition, the required number of switches could be *twice* that of the current, established % run rate in GB, necessitating a switching system capable of over 1000 switches per week.

Clearly, the ability for new suppliers to enter the market, particularly those looking to enter with a dual-fuel offering, is greatly restricted by the current gas switching systems. Without doubt there is cost-benefit analysis to be done in terms of the costs of implementing a new switching system within Phoenix Distribution and, on this issue, firmus has a number of suggestions.

firmus energy is of the opinion that the GasMaP system used in RoI could be used to facilitate market competition quickly and at least cost. Given the absence of existing automated systems or processes in PNG, no backward integration or process re-engineering would be necessary.

firmus energy is also of the view that it's own proposal to NIAUR in 2007 on a 'point-of-sale' switching mechanism using PayPoint should be investigated further as a way of facilitating efficient switching within the PAYG sector. This option could offer real benefits to a small market such as Northern Ireland and ensure that those fuel poor customers, who need it most, can benefit from a quick and effective form of competition.

Finally, the Networks business should be asked to publish their Distribution charges for each gas year to *all* gas suppliers at least 28 days prior to the 1st of October, in order that competitor tariffs can be developed.

Business separation (unbundling)

firmus energy remains concerned at the apparent lack of unbundling evident in the incumbent gas business in Greater Belfast. This has been evidenced by the recent "Lower gas prices are around the corner" and "Natural gas prices are being turned down" advertising messages used, and funded by the regulated Distribution business (PNG), in apparent support of the unbundled Supply business (PSL).

firmus energy recognises the requirement in a small market such as Northern Ireland for companies to optimise their efficiencies across the corporate group, for the benefit of customers. However the current lack of unbundling means that new supplier entrants are operating on an uneven playing field. Marketing activities undertaken by the Network Operator in Greater Belfast should be undertaken without prejudice or favouritism to any one supplier, rather it should simply positively position natural gas as a fuel of choice.

firmus energy argues that a more effective unbundling of Phoenix's Supply business from its Network Operation is critical if new entrants are to be able to compete on an equitable basis.

Electricity:

Commercial arrangements:

The regulated tariff should be reviewed, together with the k-factor, to ensure that all domestic suppliers are operating on a level playing field in terms of risk and margin headroom.

The current NIE Energy retail margin, together with the existing k-factor arrangements, does little to encourage new supply entrants.

Systems arrangements:

On the basis of our arguments on gas switching, firmus energy fervently believe that the late 2011 / early 2012 "go live" date for the 'Enduring Solution' is wholly inadequate. NIE T&D must implement a system capable of delivering 15-20,000 switches per month as quickly as possible. In line with the experiences in GB, firmus energy believes that a market opening campaign by a new supplier in Northern Ireland could result in at least 3,300 switches per week, double the maximum which can be currently realised using the existing NIE legacy systems.

Again, based on an assumption of only 15% of customers switching from NIE Energy in the 12 months following a new supplier entering the market, we are concerned that the existing legacy systems would be exhausted (based on NIAUR's recent confirmation of a maximum 125,000 switches in total). This does not include the fact that, whilst approximately 30% of NIE Energy's domestic customer base uses a keypad or pay-as-you-go meter, the current switching systems allow only a maximum of 10% of switches to be keypad customers.

Clearly, whilst the switching systems evident in NI electricity are vastly superior to those in the Greater Belfast gas market, they still do not allow for efficient market entry with minimal customer dissatisfaction.

In terms of the non-domestic sectors, to ensure a more open market for customers, lists of customers by sector should be available for all second tier suppliers – or at the very least, NIAUR / Consumer Council should write to all eligible customers advising them of the new suppliers active in the market place.

It would also be helpful for NIE T&D to publish usage profiles for sample SME's (split by commercial sector, e.g. hotels, restaurants, pubs) and domestic users to help new entrants profile consumption and cost data.

Q. Is greater availability of natural gas the most effective means of delivering greater fuel choice, security of supply and lower carbon emissions?

Ans.

Given that the natural gas availability in Northern Ireland is at least 20 years behind the rest of the UK and Ireland, there is an opportunity for the Province to more quickly realise its carbon reduction commitments than other areas of the UK, through the conversion from heavy carbon fuels to natural gas.

Northern Ireland has an opportunity to roll out the gas network, in the same manner as was delivered in GB and the Republic of Ireland, so that the economic, social and environmental benefits of natural gas can be realised by as many homes and business as possible. It is no coincidence that 21 out of the 23 worst performing council areas in the UK, as benchmarked by the Energy Saving Trust in 2007, were in Northern Ireland, and all of these areas were either relatively new gas areas or non-gas areas. As a proven technology, with a reliable and well-regulated supply chain, natural gas offers Northern Ireland a readily accessible and affordable opportunity to lower fuel costs for homes and business whilst at the same time reducing the Province's carbon footprint. The conversion to natural gas offers homes and businesses the opportunity to improve energy efficiency by up to 30% (from 60%+ for an existing 10-15 year oil fired boiler to 90%+ for a high efficiency gas boiler), reduce their fuel bills and, through the use of pay-as-you-go meter technology, make the payment for fuel more manageable.

However, whilst these benefits have been quickly realised by the Private sector, the objectives relating to the benefits of the extension of the gas network to the SN and NW towns have not yet been fully realised. Gas *availability* alone cannot in itself deliver benefits to the local economy or local consumers, rather policy is required to ensure that Northern Ireland PLC can maximise the benefits espoused at the inception of the NW & SN gas pipeline projects.

Delays and/or non-conversion of key public sector buildings within the new gas areas, together with the lack of traction around the NI Housing Executive heating replacement programme, which to date has converted less than 10% of the public sector housing stock in the NW & SN towns from solid fuel, Economy 7 or room heaters to natural gas, is effecting gas availability for private sector homes and businesses in the 10 towns.

firmus energy believes that there are significant realisable carbon reduction opportunities by converting the public sector estate to natural gas, where gas has already been made available. These conversions are proven and affordable ways of reducing carbon emissions by over 25%, whilst at the same time ensuring cost savings for the public purse, and we would urge Government to support the realisation of these benefits as soon as possible.

Q. How important are common arrangements between Northern Ireland and the Republic of Ireland to ensure continued investment in the gas industry and to develop competition and longer term security of supply?

Ans.

We would welcome a discussion with DETI and the Utility Regulator to consider regulatory approaches and energy policy direction that could be tailored to Northern

Ireland's energy market needs. We do not believe that comparisons with GB regulatory structures are the most appropriate for Northern Ireland's gas market.

As an energy company which has an all-island presence, both in gas and more recently in electricity, we would welcome the chance to explore opportunities to maximise regional cooperation and efficiencies across the island of Ireland, for the benefit of customers.

Q. How can the job creation potential of the renewable energy sector be maximised?

As indicated in the Green New Deal proposals for Northern Ireland, there are significant employment benefits in looking at opportunities to invest not only in renewable technologies but also in "lower carbon fuel switching" at both a domestic and commercial user level. There are some 705,000 dwellings in Northern Ireland and despite improvements over the past decade, over 90% of houses still fall some way short of the best energy performance standards. Domestic space and water heating is responsible for over 40% of energy consumed in Northern Ireland along with associated emissions.

As a proven, reliable technology, natural gas central heating systems can not only deliver improvements of up to 30% in energy efficiency for homes and premises converting from oil or other heavy carbon fuels, but can also deliver an immediate 25%+ savings in CO₂ emissions. As part of a comprehensive conversion programme of the existing housing stock in Northern Ireland, the inclusion of natural gas as a key element of home energy efficiency improvements presents an opportunity for thousands of jobs* both within the construction sector (civils works) and private sector downstream gas installers.

firmus energy would be keen to work with Government on the optimal ways to realise this opportunity as quickly as possible.

[* up to 15,000 new jobs. Source: Green New Deal, Housing Package 2009]

Chapter 3: Security of supply

We understand that DETI and the Utility Regulator are investigating options for additional gas storage capabilities in Northern Ireland with a number of interested parties, including BGE.

firmus energy, BGE Transportation and the Utility Regulator also undertook a storage product trial using spare capacity within the NW and SN transmission pipelines. firmus energy would be keen to discuss how this trial could be reinstated until such times as an Inventory Storage Service (delivered as part of the CAG project) is offered on an all island basis.

firmus energy also welcomes the current smart metering trial in Northern Ireland and is pleased to be an active participant in the study. As a pre-requisite to any final rollout of smart metering, firmus energy would advocate the implementation of dual fuel meters (gas and electricity) which can best ensure customer management of the total energy requirements.

It should be noted that Northern Ireland is well ahead of other areas in the UK and Ireland in terms of the efficient use of pay-as-you-go meters which have a proven effect both in terms of helping consumers manage their consumption and avoiding

fuel debt issues. Northern Ireland electricity and gas suppliers have lead the way in ensuring the pay-as-you-go meter users pay the lowest possible tariff, a situation not mirrored in the rest of the UK.

Chapter 4: Sustainability

firmus energy is generally supportive of DETI facilitating the development and deployment of renewable technologies.

That said, many councils and businesses in the NW and SN towns lobbied Government for many years to have access natural gas which would enable them to reduce their carbon footprint, allow businesses to remain competitive and to ensure the delivery of cost and environmental benefits to householders.

Given that firmus energy continues to invest *customer monies* in extending its gas network to new areas, Government and policy makers need to be mindful the role that natural gas can play in the local economy and its ability to offer immediate, long-term and sustainable financial / environmental benefits.

We therefore feel that natural gas *and* renewables need to be embedded within the overall energy policy in Northern Ireland and both should be core to addressing the issues around reducing Northern Ireland's historic dependence on oil and delivering against environmental policy targets.

Chapter 5: Infrastructure

firmus energy believes that the gas industry as a whole needs to encourage a shift from domestic dependence on oil from home heating to natural gas.

Customers will not switch from their existing heating or hot water systems to natural gas without a "switching incentive". firmus energy would welcome increased collaboration between DETI and the Utility Regulator to promote the benefits of natural gas and to challenge policy makers to choose natural gas a low carbon alternative to coal and oil, where it is available.

firmus energy intends to make proposals to both the Department and Government on funding mechanisms - along the lines of the Reconnect programme for Renewable solutions (see Competitiveness section above).

We welcome the current review of gas extensions to new areas in Northern Ireland. Any expansion would need to consider an economic appraisal of the investment infrastructure required to service any new towns and this analysis set against Government policy objectives such as delivering lower fuel costs for homes and businesses in those areas and the CO₂ reduction which could be realised through a reduced reliance on oil. Given firmus energy's experience in bringing natural gas to rural towns across Northern Ireland, we would suggest that 3 key elements must be true to ensure that any investment in gas infrastructure is viable in new towns for consideration:

- available private sector industrial & commercial conversions
- full conversion of Public sector buildings in the locality
- early and full conversion of NIHE homes in the locality

We also understand that DETI and the Utility Regulator are investigating options for additional gas storage capabilities in Northern Ireland with a number of interested parties, including our parent company, BGE.

Q. How important is it to have natural gas more widely throughout Northern Ireland? If gas is not available in certain areas, what support, if any, should be provided for alternative energy sources in certain areas to help shift usage away from oil?

Ans.

There are sound economic and environmental reasons for extending “the reach” of natural gas.

Natural gas continues to play an integral role in helping to reduce the carbon footprint in Northern Ireland. Indeed, we have seen a reduction of around 98k tonnes of CO₂ by homes and businesses in the NW and SN towns, since our licence was awarded in 2005.

The licences granted for the 10 towns are different to those granted for Greater Belfast, firmus energy is keen to propose options to increase the gas availability to homes in the SN & NW towns and ensure better choice for homes and small businesses in terms of their fuel usage.

There are significant cost, environmental and energy efficiency benefits in driving natural gas availability and penetration within our current licence areas. The limit of this roll-out will be dictated by Government’s ambition on the % reduction of the number of homes in NI which rely on oil as their primary fuel, from the current 70% level.

It is disappointing that key public sector connections within a number of the new gas towns have not yet been realised, including 3 large hospitals - **Antrim Area** and **Altnagelvin**, which continue to burn coal, and **Craigavon Area** Hospital which continues to burn heavy fuel oil - even though they are readily connectable to our gas network. It should be noted that, in the case of Craigavon Area Hospital, the payback on the costs of conversion are less than 10 months due to the potential for annual cost savings of c£200,000. The connection of hospitals, schools, Council premises and other public sector buildings are not only vital to the economic viability of the new gas network but their conversions to gas are critical in delivering cost and environmental savings.

Additionally, it is critical that all Government departments play their part in working towards a common energy goal. For example, there are over 100 schools across the NW and SN gas towns which have ready gas availability but have, primarily for short-term funding reasons, not been converted to natural gas. Based on an average conversion cost of c£10,000 per school, the payback on the conversion of these 100 sites to natural gas is around 4 years, with total lifetime savings (based on 15 years on new gas boilers / burners) of nearly £3m for the Education budget. We have already commented on our proposal, which will be formally submitted to Government in October, on the opportunity to convert more homes to natural gas in the new gas areas.

Over and above the requirements for funding mechanisms for households to convert, monies must be made available through the Central Energy Fund (DFP) to enable schools, colleges, hospitals etc. to convert to natural gas. These funds should be made available within a policy context of “going gas” within the Public sector estate where gas is available. Only by doing this, can natural gas availability be increased for the benefit of private sector businesses and homes.

In addition to the consumer and business benefits in increased gas availability, it should be recognised that quick response, gas fired back-up generation may be required to support the realisation of wind generation goals in Northern Ireland. BGE, firmus energy's parent company, has already committed itself to the investigation and subsequent development of open cycle gas generation in the Republic of Ireland, again in support of wind generation targets in RoI. Given the potential for OCGT to support DETI's renewable wind generation objectives, firmus energy would argue that joint collaboration with the natural gas industry is required to help ensure natural gas availability for potential OCGT sites.

It should also be noted that the requirement for transmission or distribution infrastructure support for OCGT sites may enable for a more economic extension of the gas network in Northern Ireland. That is to say, potential OCGT sites may act as anchor loads for new network extensions, making gas availability in rural towns more of an economic possibility.

Q. How essential is strategic energy storage for Northern Ireland? What technologies should be considered?

Ans.

As previously mentioned, firmus energy approached the Utility Regulator in 2006 with plans to run a Northern Ireland Inventory Product. Initially the NI Inventory Product was to be a trial with firmus energy as the Supplier and BGE (NI) the Transporter.

The aim of the Inventory Product service was to buy gas when gas prices were lower and to store this gas in the pipeline for use at peak times when gas prices were likely to be higher. Following consultation in early 2007 the trial was approved.

Business rules were agreed and the trial was operationally successful. firmus energy furnished the Utility Regulator with monthly progress reports. In order to facilitate the flexibility of the service, firmus energy proposed that the business rules should be updated to enable within day nominations and to increase storage capacity within the NW and SN pipelines.

Unfortunately, an extension to the trial was refused by the Utility Regulator on the basis that a storage product was being considered as part of the Common Arrangements for Gas (CAG) workstream.

Given that a storage product is not immediately available, firmus energy would still be keen to run an inventory service trial, using the North West and South North pipelines until such times as an all island service is available. We would be keen to discuss how this opportunity could be realised for the benefit of gas customers.

Chapter 6: Cross cutting themes

Given the cross cutting nature of energy matters in the NI Assembly, firmus energy believes that it is critical to have pan-Executive support for the delivery of NI energy objectives both now and in the future. firmus energy has experienced, first hand, the lack of cohesion between Government departments in terms of realising the benefits of the extension of natural gas to the North West and along the South North transmission pipelines. There are significant gains to be made in the Government taking advantage of the existing gas infrastructure which has been recently developed but the cost and environmental benefits can only be realised through

joining up policy between departments such as DETI, Social Development, Health and Education.

It is therefore crucial that DETI takes the lead in driving forward this cohesion across Government departments to ensure that NI's targets for carbon reduction, energy efficiency and sustainability are delivered alongside the available cost efficiencies which are so greatly needed in these difficult economic times.

Thank you again for allowing firmus energy the opportunity to comment on, what will be, *the* critical policy document for the future of energy policy in Northern Ireland. Should you wish to discuss any of the above, please feel free to contact me on 02894 426840.

Yours sincerely

Michael

Michael Scott
Head of Business Development