



*Campaigning for Warm Homes*

## **NEA NI**

### **Response to Consultation Paper by the Northern Ireland Authority for Energy Regulation –**

### **The Proposed Acquisition of East Surrey Holdings plc by Kellen Acquisitions Limited – Implications for Phoenix Natural Gas Limited**

**June 2005**

NEA is the national energy action charity working to eradicate fuel poverty in Northern Ireland. Around one third of Northern Ireland's households experience fuel poverty with more being at risk if energy prices were to increase.

In light of the recent offer by Kellen Acquisitions for East Surrey Holdings incorporating Phoenix Natural Gas, it is NEA NI's opinion that the proposed regulatory agreement needs to be reviewed. Our reasons for this include:

The offer appears to value Phoenix Natural Gas (PNG) at a sum above that assumed by the NIAER for regulatory purposes; this implies a level of confidence in investing in the NI natural gas market higher than that previously assumed by NIAER and, accordingly, the permitted rate of return on that investment should be decreased to reflect the apparent decreasing risk of investment.

It should also be noted that two factors involved in assessing risk are within control of PNG themselves; consumer certainty and expectations of investors. For example, the debacle in early 2004 over PNG's proposed 20% price increase will have damaged consumer certainty as to the attractiveness of natural gas as an alternative to fuel oil; this uncertainty in turn could impact on the overall growth of the natural gas market and this was recognised by the regulatory authority at the time. This increased consumer uncertainty and consequential potential impact on the development of the natural gas market will have

increased the risk for potential investors in the natural gas industry in Northern Ireland. Thus potential investors will have been expecting a higher rate of return on their investment. In short, PNG's own behaviour may well have resulted in higher prices for consumers so investors made an acceptable return on their investment; it is unfair that consumers should pay for such irresponsible behaviour and NEA NI is of the opinion that PNG should be strongly encouraged to behave in a more responsible fashion in future and consumers be protected where an organisation acts irresponsibly. It is also NEA NI's opinion that perceived risk is exacerbated by unreasonable expectations of investors; this potentially creates a vicious circle where high levels of perceived risk create expectations of high returns on investments and these in turn create more unreasonable expectations on the part of investors. Again, halting this spiral is not within the gift of consumers and consumers should not be expected to pay for unreasonable demands for unfair returns on investment.

Whilst NEA NI has welcomed the development of the natural gas industry in Northern Ireland, it must be remembered that 'the development and maintenance of an efficient, economic and co-ordinated gas industry in Northern Ireland' does not have any intrinsic worth. It only has value if it provides benefits to individual consumers and to the wider economy. The 'interests of consumers' is not subsidiary to development of the gas market - it is the rationale for market development. This raises another issue. NEA NI wants to take this opportunity to ask what the fallback position is in the situation where PNG becomes unviable without exorbitant prices and/or Government subsidy; the GB competitive market regulations embody the principle of supplier of last resort where an existing supplier, for example, withdraws from the market. NEA NI asks if NI consumers are protected in a similar fashion, particularly in light of investment in the natural gas industry by individual consumers and Government and its agencies such as NIHE.

In light of potential savings to customers, NEA NI supports the mutualisation of the natural gas distribution network however, the inter-relationship between the various components of the proposed regulatory agreement mean it is paramount that the whole agreement be reviewed. We would also take this opportunity to ensure that information relating to NI Energy Holdings be made more accessible to the public at large through normal sources of information and that it is ensured that consumers be equitably represented on its board.

Regarding licence modifications, NEA NI is of the view that as many modifications are made as required to protect the interests of consumers. Whilst we understand that many of the proposed modifications are dealt with within current company law legislation, we support the Authority in ensuring that the natural gas licence held by PNG is clear and precise as to their responsibilities and limitations. It is therefore our view that such licence modifications are necessary in order for the NIAER to carry out its responsibilities and duties, independent of, for example DETI, or any other body with responsibility for enforcing company law generally.

We look forward to hearing NIAER's conclusions regarding all the issues raised within the consultation.