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Dear Fergus, Barbara

RE: Retail Tariff Structure Review

Bord Gáis Energy (BG Energy) welcomes the Regulatory Authority's (RA's) retail tariff structure review in the context of enhancing the development of competition in the Irish and Northern Irish retail markets.

On a general point of principle, tariffs are typically designed to provide appropriate signals to customers relating to their consumption and to ensure that the tariffs charged are reflective of the costs incurred. The Queensland Competition Authority¹ in its recent review of retail tariff structures has stated that price signals depend on "cost reflectivity and not cost recovery". This is an important distinction if tariffs are to be suitably transparent to provide for the development of competition in a market. Ultimately, competition is the best medium of ensuring that appropriate tariffs and tariff structures are provided to meet market needs. Therefore, BG Energy is of the view that the RA's should focus their efforts on those areas which continue to inhibit competition; such as liquidity and transparency; and allow the subsequent competitive forces to determine the prevailing tariff structures in the market.

The remainder of this response focuses on the specific aspects and questions raised by Pöyry in their report to the RAs.

¹ 'Review of Electricity Pricing and Tariff Structures – Stage 1', Queensland Competition Authority, August 2009.

1. Existing PES Tariff Structures and Cost Allocation

Pöry's report clearly reflects the inputs to the tariff setting process and highlights where differences between the two jurisdictions exist. However, the narrative fails to highlight the volatility and lack of transparency which mars the current regulated tariff process and hinders the development of competition in the market. This is a market barrier similar to liquidity and other issues referred to in section 3 of the report which BG Energy believes should be addressed if the regulatory tariff regime is to have the effect of delivering benefits to customers.

2. Market Structure Proposals

2.1 CfD Liquidity

BG Energy welcomes Pöry's recognition of the importance of increased wholesale liquidity for suppliers seeking to offer customers cost reflective tariffs. BG Energy has fervently contended since the beginning of the Single Electricity Market (SEM) that further liquidity in the wholesale market is required if effective competition is to emerge in the Irish market. The merits of implementing more frequent contracts (quarterly, monthly and weekly) include the reduction of market risks, the promotion of competition and ultimately a reduction in prices for end-users.

This level of liquidity is likely to be best achieved through an on-line broker screen. However if it is to be effective and marketable to users, the broker must demonstrate its independence and ability to provide tradeable contracts on a long and short term basis to the market. BG Energy participated in and helped instigate this year's online CFD auction trials in conjunction with Tullett Prebon. The NDC & PSO auctions being carried out online this year, was a good opportunity for market participants to familiarise themselves with this online CFD trading process. BG Energy is keen that continued progress and commitment is made to create a liquid SEM market through participants trading CFDs online.

2.2 Global Aggregation

Given the increasing levels of competitive activity in the market, the suggestion that all suppliers are treated equally with respect to the allocation of distribution loss factors and unallocated consumption seems reasonable, in theory. However, moving to global aggregation in the current market is not practically viable as it will increase forecasting volatility and risks for independent suppliers. The existing wholesale market is not sufficiently liquid to enable participants to trade out their positions at short notice, thereby compounding the risks faced by independent suppliers. For this reason, BG Energy cannot support the implementation of global aggregation at this time.

2.3 Metering

Metering is a seminal aspect of this review as the types of meters and level of information provided by meters limits the scope for changes in tariffs and the level of information provided to the market. The current meters for domestic and a large proportion of small and medium enterprises are not sufficiently advanced to support more complex tariff structures. Previous analysis by the CER indicated that lowering the threshold for profile metering down to customers with a MIC of greater than or equal to 50kVa was economically justified. This was not implemented but may be worth revisiting on an all-island basis.

For those customers with an MIC of less than 50kVA, BG Energy is aware of the ongoing Smart Meter Pilot Project and will refrain from commenting at this stage on the detail or merits of smart metering. However, if the outcome of the pilot project is that smart metering is not economically viable, a less costly alternative should be considered; for example a four-dial meter replaced on a passive replacement basis may be worth considering.

If retail market competition is to progress on an all-island basis, BG Energy agrees with Pöyry's proposal to harmonise metering codes of practice but would also suggest the standardisation and harmonisation of metering policy. Given the size of the Irish electricity market, BG Energy believes that metering would be more efficiently carried out as a monopoly operation, whereby the network operators own, install and maintain meters for all suppliers and

customers. Standardising this policy will reduce overall costs to the market and support the further development of competition on the island.

3. All-Island Regulatory Proposals

3.1 Profile Load Research and SME Profiles

The accuracy and availability of standard profile data is important for new entrant suppliers in the retail market. It provides critical information for suppliers seeking to purchase energy for and hedge their portfolio requirements. In order for further work on standard profiling to be more meaningful, suppliers will need access to this data on an ongoing basis. Currently, there is uncertainty as to who owns the standard profile data and therefore who has access to it. In reality, the data is only useful to those parties operating the system and supplying electricity for consumption by end users. Therefore it is essential for a supplier of a customer to have access to that data on a frequent and transparent basis.

Potentially, the most appropriate method of providing this service would be through a central web-service controlled and updated by the relevant system operator.

With respect to increasing the number of SME profiles, it would be prudent, as suggested by Pöyry, to firstly conduct an impact assessment on the proposal. Increasing the number of profiles may add a level of complexity for customers and suppliers attempting to compete in the market which may be unwarranted and outweigh the perceived benefits of greater segmentation.

4. PES Regulatory Proposals

4.1 Network Charging Methodologies and Separation of Network and Wholesale Energy Costs

It seems reasonable and in keeping with developments in other more mature markets for network tariffs to be separated from the energy components of a standard tariff. The general view is that this will act to improve transparency

for the customer, allowing them to identify network related costs and the ability of suppliers to offer more products to end users.

The inclusion of the section on geographic cost signals is slightly confusing in the context and scope of this consultation. Since the creation of the electricity network, distribution customers of different sizes have been treated largely on a “postalised” basis. To move away from this process, introducing what appears to be zonal network pricing, and to discriminate between similar distribution customers in different parts of the island would seem illogical, particularly in the context of a small island economy. To be clear, this is not to say that BG Energy is against a level of differentiation of network charges between the Republic of Ireland and Northern Ireland.

4.2 Contract Term and Indexation

As referred to previously, BG Energy is in favour of increased liquidity and transparency, which in turn should enhance competition and provide more robust tariffs and products to customers. To this extent, products and their underlining tariffs should evolve as markets evolve and should not be subject to stringent regulatory scrutiny/approval. Therefore, PES’s and other suppliers should not need “encouragement” to implement choice by the regulatory structure. This will be provided by the market and competitive forces in due time as the market and competition develops. For this reason and potential market closure reasons, BG Energy does not support the proposal to oblige the PES’s to provide 6 month to 2 year contracts to customers at this time.

4.3 Evaluation of Harmonisation Proposals

The evaluation presented in section 4 provides a holistic and detailed view of the impact of the various proposals contained in this review. The merits of this evaluation would be greatly enhanced by an accompanying cost benefit analysis capturing the financial consequences of the proposals, in particular those relating to metering and providing time of use tariffs. From a practical point of view, it is imperative to keep the underlining costs relative to the benefits in mind, especially considering that the aim of these changes is to improve the level of cost reflectivity to the customer.

5. Conclusion

BG Energy is in agreement with the principles of this review, which calls for more transparency and cost reflectivity in the tariffs charged to end-users. However, from a policy perspective BG Energy believes that competition rather than regulated structures are best placed to direct the structure of tariffs in the future. For this to be realised, a number barriers which inhibit competition, such as; wholesale liquidity and the provision of standard profile data, must first be addressed by the RAs and the system operators. The resulting developments in competition should then provide the level of flexibility and cost reflectivity in products and tariffs sought by the RA's.

In the meantime and until such time as the PES's are no longer the dominant players in the retail market, some form of tariff regulation will be required to restrict the potential for dominant behaviour and protect the interests of the market and customers.

I hope you find the comments above useful to your review. I would welcome an opportunity to meet with you and your colleagues in Pöyry to discuss the content of this response further.

Yours sincerely,

Jill Murray
Commercial Regulation
Bord Gáis Energy

{by e-mail}