



Commission for Energy Regulation

An Coimisiún um Rialáil Fuinnimh

**Final Direction on Bord Gáis Energy Supply Revenue  
For Domestic and small Commercial and Industrial Customers  
(Non-Daily Metered Market)**

**1 October 2006 to 30 September 2007**

**8<sup>th</sup> September 2006**

**CER/06/169**

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## **Executive Summary**

### **Commission Direction**

The Commission for Energy Regulation (the Commission) today (8th September 2006) publishes the Final Direction in relation to the allowable revenues, for Bord Gáis Supply (BGS) to supply gas to its Non-Daily Metered (NDM) Customers from 1<sup>st</sup> October 2006 to 30<sup>th</sup> September 2007 and the resulting NDM natural gas tariffs.

In its formal submission to the Commission, BGS requested an average revenue (and tariff increase) of 38.34% which equates to a revenue requirement of €728.09 million. Following a detailed examination of the BGS submission the Commission has approved the recovery of NDM revenue of €706.37 million, which equates to an average increase of 33.8% in NDM tariffs.

Unfortunately the increasing cost of fuel worldwide has led to a significant and direct impact on energy prices for customers in Ireland. While any tariff increase to customers is highly regrettable, the main cause for the price increase relates to international wholesale prices of fuel which is outside the control of the Commission.

The largest contributor to the 33.80% increase is due to the significant increase in the BGS gas procurement costs which has increased by approximately 50% over last year. This is largely driven by two factors. The rising trend in recent years in international wholesale gas prices and the expiry of the BGS long term “in the money” contracts.

BGS has to import the vast bulk of its gas supplies from international markets and does so through contracts in the UK. This makes BGS a net importer of natural gas and therefore exposed to the prices faced in international wholesale markets. The small share of indigenous natural gas production that contributes toward the overall consumption requirements in Ireland means that Ireland remains a price taker for gas prices set in international markets. Wholesale gas prices in the UK and worldwide have increased significantly and these have resulted in a direct effect on the BGS gas procurement costs. The key reasons for the increase in UK prices over the last year 12 months appear to be: significant increases in oil prices directly influencing continental and in turn, UK gas prices, uncertainty over security of supply for winter 2006/07 and Geopolitical risk in oil producing countries. These factors have also affected some of the largest suppliers in the UK.

Another factor that has contributed to the increase in gas costs faced by BGS is the expiry of their favourably priced long term contracts. In the past BGS customers have benefited from favourably priced long term gas contracts, which shielded customers from the full impact of international market price increases. As these contracts are due to expire this year, BGS is increasingly required to procure its natural gas requirements at prevailing wholesale prices. The expiry of these favourable long term contracts accounts for over half the increase in BGS's own gas procurement costs.

The Commission has examined how Irish gas prices compare with other countries. It has been observed that increases in wholesale gas prices have

also affected some of the largest gas suppliers in the UK. They too have faced significant price increases in 2006. The six largest UK gas suppliers have now increased their gas tariffs twice since January 2006. A table of the cumulative increases are between 47.3% and 30.8% and details are shown in appendix 3 of this document.

In approving the natural gas supply tariffs Bord Gáis Energy Supply (BGS), can charge its NDM customers, the Commission first examined the BGS submission on costs of service to determine its revenue requirement for the 2006/07 gas year. This method of revenue control provides BGS with full pass through of allowed transmission, distribution and gas procurement costs. It also indexes the BGS own supply costs to growth/decline in numbers of BGS customers and GWh sales and correction factors to enable adjustments for divergence between forecasts and actual costs and revenues incurred. The NDM tariffs are then set to recover the approved revenue requirement.

The Revenue Control Formula (RCF) determines the revenue that BGS is permitted to earn each year from the NDM customers. This formula has been used to determine these revenues since 2004 and will operate until 30<sup>th</sup> September 2007; therefore the Commission will shortly commence a full and comprehensive review of the RCF, to determine the management of BGS revenue and tariff regulation in the future.

On 21<sup>st</sup> July 2006 the Commission published its Proposed Decision on Bord Gáis Energy Supply Revenue for Domestic and Small Commercial and Industrial Customers (CER/06/127). In reaching its final direction, the Commission has considered a number of comments submitted in respect of the Proposed Direction CER/06/127. These are discussed in Appendix 2 of this document.

In making this Final Direction the Commission has been mindful of its legal functions under section 6 of the Interim Gas Regulation Act, these include:

- Protection of the interests of final customers
- Promotion of competition in the supply of natural gas and
- Ensuring continuity, security and quality of supply of natural gas

## The Revenue Control Formula Components

The table below provides a summary of the approved level of allowable revenue for the period that may be recovered from NDM customers through increases in tariffs.

**Table 1 Allowed NDM Revenues for tariff year 2006/07<sup>1</sup>**

| 2006/07 BGES Revenue Control Formula |                                     |     |        |
|--------------------------------------|-------------------------------------|-----|--------|
| <b>Rev = P+T+D+M+S+Y+K+RK</b>        |                                     |     |        |
| P                                    | Forecasted Gas Procurement costs    | €'m | 437.05 |
| T                                    | Forecasted Transmission Costs       | €'m | 71.24  |
|                                      | Less Interbook ICS                  | €'m | -4.30  |
|                                      | Less: External ICS                  | €'m | -2.60  |
|                                      | Less: Inch Benefit                  | €'m | -1.29  |
| D                                    | Forecasted Distribution Costs       | €'m | 159.91 |
| M                                    | Supply Margin                       | €'m | 8.85   |
| S                                    | Forecast of BGES own cost of supply | €'m | 32.86  |
| Y                                    | Exceptional Costs                   | €'m | 0.40   |
| K                                    | Expected under-recovery for 2005/06 | €'m | 4.26   |
| R                                    | Total Revenue Requirement           | €'m | 706.38 |

The following sections describe each of the components of the Revenue Control Formula, (RCF), and sets out the Commission's Final Direction for allowed revenue in each case.

### *Total revenue (R)*

The Commission has approved the recovery of NDM revenues totalling €706.38 million for the period 1<sup>st</sup> October 2006 to 30<sup>th</sup> September 2007. This represents an increase of 33.80% in NDM tariffs.

This increase differs from that proposed in CER/06/127 (33.84%) due to the following:

- The K Factor for 2005/06 has increased from -€12.242 million to -€14.242 million due to a re-calculation of revenue from Interruptible Capacity Sales, and
- The revenue of €1.69 million from the standing charge on the Gas Card tariff, which the Commission has decided to retain, has been included in the Revenue Control Formula.

### *Gas procurement costs (P)*

The Commission has approved recovery of €437.05 million in gas procurement costs based on the IPE price of 12<sup>th</sup> July 2006. This reflects the Commission's direction that

- the peaking provision of €8 million is to be excluded and that
- all WACOG benefit is to be allocated to the NDM sector

### *Transmission Costs (T)*

<sup>1</sup> Figures are rounded to 2 decimal places

The Commission has approved recovery of €63.05 million of Transmission Costs. This comprises €71.24 million less expected Interbook ICS of €4.30 million, expected External ICS of €2.60 million and expected Inch benefit of €1.29 million.

*Distribution Costs (D)*

The Commission has approved recovery of €159.91 million of Distribution Costs.

*Supply Margin (M)*

The Commission has approved recovery of an €8.85 million Supply Margin

*Own Supply Costs (S)*

The Commission has approved the BGS calculation of €32.86 million in allocated operating costs under the RCF, which takes account of customer numbers, gas volumes, inflation and efficiency improvements.

*Specific Recoverable Costs (Y)*

The Commission has approved recovery of €0.40 million in Specific Recoverable Costs for IT related expenditure capitalised and depreciated over 10 years.

*Out-turn adjustment for under-recovery in 2005/06 (K)*

The Commission has approved the inclusion of an under-recovery of -€4.26 million in the RCF for 2006/07, which comprises -€0.91 million under-recovery in respect of 2003/04, €11.57 million over-recovery in respect of 2004/05 and an expected under-recovery of -€14.92 million in respect of 2005/06.

The K Factor has changed from -€2.26 million to -€4.26 million since the Proposed Decision, CER/06/127, was published. The Commission has allowed for the inclusion of a further recovery of -€2 million in respect of 2005/06, i.e. from -€12.26 million to -€14.26 million, which is due to a recalculation of revenue from Interruptible Capacity Sales.

## **1. Introduction**

Under the Gas (Interim) (Regulation) Act, 2002, the Commission for Energy Regulation (“the Commission”) is responsible for regulating charges in the natural gas market. This takes in the functions of gas transmission, distribution and supply to the BGS customers<sup>2</sup>.

On 21<sup>st</sup> July 2006, the Commission published its Proposed Decision on Bord Gáis Energy Supply, BGS, Revenue for Domestic and Small Industrial and Commercial Customers as CER/06/127. This document sets out the final Direction to BGS on its allowable revenues for the period October 2006 to September 2007.

In reaching its conclusions the Commission has balanced a variety of factors. The Commission is conscious of the need to act in a manner that is in the best interests of customers and the impact record increases in gas prices have on end customers.

The Commission considered submissions made in respect of the Proposed Decision. These are discussed in Appendix 2 “Response to Comments Received on CER/06/127”

The Commission received comments from the following:

- General Public
- National Consumer Agency
- Irish Business and Employers Confederation, IBEC
- Bord Gáis Networks
- Bord Gáis Supply

In exercise of the powers conferred on the Commission as amended by Section 23(2) B(vii) of the Gas (Interim) (Regulation) Act, 2002, the Commission hereby directs that Bord Gáis, in its capacity as natural Gas supplier Bord Gáis Supply, in relation to Residential and small Industrial and Commercial customers (or the NDM sector)<sup>3</sup>, may increase the natural gas tariffs by 33.80%. These tariffs shall apply for the period 1<sup>st</sup> October 2006 to 30<sup>th</sup> September 2007. The tariffs that shall apply to each customer category are set out in Appendix 1 of this Direction.

## **2. Revenue Control Formula**

This section sets out the methodology the Commission used for calculating the BGS revenue in the Residential and I&C market sectors.

The Retail Control Formula, (RCF), is described algebraically below (all terms expressed in €). The RCF provides BGS with a full pass through of allowed gas procurement, transmission and distribution costs. It also indexes the BGS own supply costs to the growth/decline in numbers of BGS customers and in GWh sales.

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<sup>2</sup> Under Section 2(6) of the Gas (Amendment) Act, 1987, as amended by Section 23 (2) (b) (vii) of the Gas (Interim) (Regulation) Act, 2002.

<sup>3</sup> For clarity the Non Daily Metered Sector (NDM) includes non-eligible customers, domestic, and eligible customers, Industrial and Commercial, consuming below 180,000 Therms per annum.

The approved revenue is then recovered through NDM tariffs. These tariffs increase to the extent that approved revenue increases (and vice versa).

|   |                   |
|---|-------------------|
| $R = (P + T + D + S + Y + K + I) \times (M) + RK$ | <b>Equation 1</b> |
|---|-------------------|

Where:

- R = Allowed revenue
- P = Gas procurement costs
- T = Transmission costs
- D = Distribution costs
- S = BGS's own costs of supply (staff, rent, IT, etc)
- Y = Pass through of specific exceptional costs (e.g., business separation costs)
- K = Out-turn adjustment for under-/over-recovery in the previous year
- I = Initial, special correction factor (*not required in 2006-07*)
- M = Allowed profit margin of 1.3%

The following sections describe each of the components of this formula, sets out the BGS submission in each area, i.e. the costs it believes are appropriate, reviews these and describes the Commission's direction for allowed revenue in each case.

### **3. RCF Components**

#### ***a) Gas procurement costs***

The Commission has examined the BGS request for gas procurement costs of €445.05 million and has decided to approve an estimated gas procurement cost of €437.05 million as part of its total revenue requirements for the coming gas year.

The Commission has disallowed an estimated peaking provision of €8 million, which the commission considers to be a contingent cost rather than an actual cost. Should the peaking costs materialise they may be factored into the K Factor calculations in 2007/08.

Condition 17 of the BGS supply licence requires BGS to procure natural gas at the best effective price and to act prudently and reasonably in the interests of its customers in its gas procurement approach. The extent to which the Commission considers gas procurement costs to be allowable and therefore recoverable in tariffs is subject to BGS satisfying this test. The Commission has reviewed and will continue to review the level of the BGS gas procurement costs that are considered to be allowable revenue and included in tariff prices.

In its 2006/07 NDM revenue submission, BGS calculated a weighted average cost of gas (WACOG) for the NDM portfolio, taking into account the contractual purchase commitments already made and the quantity of gas as yet uncontracted. For the uncontracted quantities BGS assumes that gas will be purchased at the IPE monthly forward prices as published in European Spot Gas Markets on 12<sup>th</sup> July 2006.

The BGS submission also included a calculated market cost of gas for its NDM portfolio. This represents what the gas would have cost BGS if no previous contractual commitments had been made and all of the gas was to be purchased at the monthly forward prices published on 12<sup>th</sup> July. The difference between the BGS WACOG and the Market Cost is referred to as the Mark to Market (MTM) Value, or alternatively as the WACOG Benefit.

The Commission directs that all WACOG benefit (100%) should accrue to NDM customers, both residential and I&C.

The Commission directs that BGS allocates all benefits, both commodity /capacity, that are delivered through arrangements for natural gas from the Inch pipeline to the NDM sector.

Due to the seasonal usage in this sector there may be periods during the summer when there is more 'cheap' gas that the NDM sector can consume. BGS may sell this excess gas, to the Non-NDM sector at market related prices. The Commission directs that all financial benefit thus gained, must be fully credited to the NDM sector as a reduction in the revenue requirement.

#### ***b) Transmission charges (T)***

The Commission approves the recovery of a net figure of €63.05 million of Transmission Charges. This includes the financial benefit of the following:

- Interbook Transfers of €4.31 million, net of a BGS margin of 5.1%,
- External ICS of €2.6 million, net of a BGS margin of 5.1% and
- Gas capacity and commodity benefits at Inch of €1.29 million,
- The Commission directs that all 100% of the Inch Benefit shall apply to the NDM sector.

#### ***c) Distribution Charges (D)***

The Commission approves the recovery of €159.91 million of Distribution Charges as requested by BGS.

**d) Supply Margin (M)**

The Commission has reviewed the calculation of the supply margin figure of €8.85 million and approves this amount for recovery from the NDM customers.

**e) BGS own cost of supply**

The “S” component of the Revenue Control Formula represents the allowed own operating and capital costs for BGS. The details for the calculations of the “S” component are set out in CER/04/286.

For the gas year 2006/2007, BGS has estimated its supply costs to be in the order of €32.86 million, which is approved by the Commission.

**f) Exceptional Costs (Y)**

The BGS submission included exceptional costs of €1.19 million in relation to IT related capital expenditure. The €1.19 million includes €0.79 million in costs to fully separate Bord Gáis integrated IT systems. BGS expect that the costs to separate these IT systems will be in the region of €15 million.

At this time, the Commission does not propose to approve €1.19 million in relation to this cost in 2006/07; however as part of the revenue approvals for 2006/2007, the Commission will examine and consider the approval of these costs, after receipt of a comprehensive submission relating to IT separation costs.

The Commission approves €0.40 million in relation to depreciation of expenditures already approved in accordance with CER 05/175.

**g) K factor in respect of tariff year 2003-04**

BGS requested €13.83 million through the K factor for losses associated with extending the tariff year by six months in 2003/04.

Following a detailed examination by the Commission of the BGS outturn revenues and costs for the 18 month period from April 2003 to September 2004, the Commission is of the view that a portion of these losses, €2.91 million including accrued interest, which constitute an economic loss, should be immediately recoverable through the K factor mechanism, the rest being a contingent cost which may subsequently be crystallised by future events.

In its review of the 2005/06 BGS NDM tariff (CER/05/175) the Commission decided to allow for a provision of €2 million for economic losses in 2003/04.

The Commission has therefore decided to allow BGS to recover €0.91 million (€2.91m – €2m) through the K Factor for 2003/04.

**h) K factor in respect of tariff year 2004-05**

BGS has provided an outturn revenue over-recovery of €23 million in relation to the 2004-05 gas year. The Commission decided to net €12.4 million of this over-recovery against the BGS revenue requirement for gas year 2005/06 (CER/05/175). The remaining €11.57 million, including accrued interest, has been netted against BGS revenue requirement for 2006-2007.

***ij) K factor in respect of tariff year 2005-06***

BGS forecasted an under recover approximately €14.92 million in its required revenues in the 2005-2006 gas year. This is largely due to a combination of higher than expected gas costs faced by BGS in the year, lower sales of interruptible secondary capacity than forecasted in the 2005/06 RCF and lower sales volume overall.

After examination of the BGS submission, the Commission has decided to allow BGS to recover €14.92 million through the K factor for 2005-06 as a revised forecast. The Commission will consider the total correction amounts arising from the 2005/2006 gas year, when outturn results for that year are known in full, in 2007/08.

The Commission has therefore included a K Factor of -€4.262 million in the RCF for 2006/07, i.e. -€0.91 million in respect of 2003/04, €11.57 million in respect of 2004/05 and -€14.92 million in respect of 2005/06.

**4. NDM tariffs for 2006/07**

Appendix 1 below sets out the Bord Gáis Supply gas tariff rates for their Non-Daily Metered Customers based on an increase of 33.80%, which are to apply from 1<sup>st</sup> October 2006.

There are a variety of BGS tariffs available to customers dependent on their gas consumption and whether they are Domestic or Industrial and Commercial customers. Some of these tariffs have two separate parts, Standing Charges, which are fixed and Commodity Charges in c/Therm, which vary with the amount of gas consumed.

The Commission has decided to freeze the level of the standing charge on the Gas Card tariff at last year's rate, for the 2006/07 gas year, to assist vulnerable customers on this tariff rate.

## Appendix 1: Tariff Rates for BGS Non-Daily Metered Customers

**Table 2: Tariff rate for BGS NDM Residential Customers**

| <b>Published Tariff Rates</b>                 |              |                     |                       |
|---|--------------|---------------------|-----------------------|
| <b>Residential</b>                            |              | <b>Current Rate</b> | <b>Increased Rate</b> |
| <b>(Prices are inclusive of VAT at 13.5%)</b> |              |                     | <b>33.80%</b>         |
| <b>Standard tariff</b>                        |              |                     |                       |
| Standing Charge (Bimonthly)                   | €'s per bill | 42.71               | 57.14                 |
| Unit charge                                   | c/kwh        | 3.398               | 4.546                 |
| <b>High Commitment Tariff (16,000Kwh)</b>     |              |                     |                       |
| Standing charge                               | €'s/bill     | 0.00                | 0.00                  |
| Unit charge                                   | c/kwh        | 4.472               | 5.983                 |
| <b>Low Commitment Tariff (8,750 Kwh)</b>      |              |                     |                       |
| Standing charge                               | €'s per bill | 0.00                | 0.00                  |
| Unit Charge                                   | c/kwh        | 5.887               | 7.877                 |
| <b>Reducing Rate</b>                          |              |                     |                       |
| Standing charge (Bimonthly)                   | €'s per bill | 7.93                | 10.61                 |
| <b>Bands</b>                                  |              |                     |                       |
| 0-585 Kwh                                     | c/kwh        | 8.945               | 11.968                |
| 586-1170 Kwh                                  | c/kwh        | 6.705               | 8.971                 |
| >1171Kwh                                      | c/kwh        | 4.741               | 6.343                 |
| <b>Golden Age Tariff</b>                      |              |                     |                       |
| Standing Charge                               | €'s per bill | 0.00                | 0.00                  |
| Unit charge                                   | c/kwh        | 5.887               | 7.877                 |
| <b>Gas Card Tariff</b>                        |              |                     |                       |
| Standing Charge                               | cent/day     | 26.30               | 26.30                 |
| Unit Charge                                   | c/kwh        | 4.472               | 5.983                 |

**Table 3: Tariffs for BGS NDM Industrial and Commercial Customers**

| <b>NDM Industrial/Commercial</b>         |          | <b>Current Rate</b> | <b>Increased Rate</b> |
|--|----------|---------------------|-----------------------|
| <b>(I/C Prices are exclusive of VAT)</b> |          |                     | <b>33.80%</b>         |
| <b>Standard I/C Tariff</b>               |          |                     |                       |
| Standing charge (Monthly)                | €'s/bill | 10.07               | 13.47                 |
| <b>Unit charge</b>                       |          |                     |                       |
| 0-3000kwh                                | c/kwh    | 4.464               | 5.973                 |
| 3001-7500 Kwh                            | c/kwh    | 4.121               | 5.514                 |
| 7501-15000 Kwh                           | c/kwh    | 3.777               | 5.053                 |
| 15001+ Kwh                               | c/kwh    | 3.435               | 4.596                 |
| <b>Demand &amp; Commodity Tariff 1</b>   |          |                     |                       |
| Standing Charge (annual)                 | €'s pa   | 2415                | 3232                  |
| Each Additional Meter Installed          | €'s pa   | 120.80              | 161.63                |
| <b>Unit Charge</b>                       | c/kwh    | 3.023               | 4.045                 |
| <b>Demand &amp; Commodity Tariff 2</b>   |          |                     |                       |
| Standing Charge                          | €'s pa   | 7246                | 9695                  |
| Each Additional Meter installed          | €'s pa   | 120.80              | 161.63                |
| <b>Unit charge</b>                       | c/kwh    | 2.815               | 3.766                 |

## **Appendix 2: Responses to Comments Received on CER/06/127**

On the 21<sup>st</sup> July 2006 the Commission published a Proposed Decision (CER/06/127) on Bord Gáis Energy Supply's supply tariffs to the Non-Daily Metered (NDM) market for the period 1<sup>st</sup> October 2006 to the 30<sup>th</sup> September 2007. The Commission invited comments from interested parties by 11<sup>th</sup> August 2006. The Commission received a number of comments on various aspects of the Proposed Decision. This section summarises those comments and outlines the Commission's response. The Commission appreciates comments received from respondents. In order to preserve the confidentiality of certain submissions, it does not intend to publish the individual responses.

### **1. Standing charge and commodity charge**

The following comments were received with regard to the Standing Charge and Commodity charge elements of the gas tariffs:

- The same increase in the standing charge and the commodity charge makes it difficult for the consumer to reduce their bills by restricting their consumption.
- CER should present information on the breakdown of existing consumer by tariff category. The effect of varying the rate of increase between standing charge and commodity charges should be examined.

#### ***Commission's response:***

The Commission decided not to have differential tariff increases on the standing charge and commodity charge for the following reasons:

- As the current tariff structure is not fully cost reflective, it means that the standing charge does not fully cover the transmission, distribution and supply costs for providing natural gas. To allow a differential increase at this time, could lead to further deviations from cost-reflectivity of the tariffs and have the effect of requiring further increases in the standing charges in the long term.
- The Commission has decided to carry out a detailed analysis of the current tariff structure in the NDM residential sector with the view to developing a revised tariff structure or tariffs, from October 2007. A transition path to any revised tariffs will be implemented if required.

### **2. Tax applicable to gas charges**

The gas costs for customers are liable to a VAT rate of 13.5%. It was suggested that as a temporary measure, in order to relieve the burden of the increases, at least for domestic consumers, the Government should reduce taxes and that the CER should endorse the recommendation.

***Commission's response:***

The Commission appreciates the comments received with regard to the VAT rates, however the treatment of this lies outside the remit of the Commission.

**3. Mechanisms for increased competition in the supply, transmission and delivery of natural gas**

The following comments were received with regard to supply, transmission and delivery of natural gas:

- Mechanisms should be developed in order to allow for increased competition across all stages of gas supply including transmission and distribution.
- Gas companies would also be more innovative in their tariffs and offer more tariff combinations and make it easier for customers to switch gas supplier. In other countries the process of switching is very easy.
- Consumers should be given the opportunity to fix their gas tariffs for more than one year to allow consumers to budget in advance for the costs over a longer period.
- Consumers should be given more information on reducing their consumption than at present. There are consumer information campaigns on the question of insulation, for instance, but not on the efficiency of appliances, particularly older appliances.
- At times of maintenance consumers should be advised about how their boiler ranks in terms of efficiency and what saving could be made by changing the boiler. The annual inspection and maintenance should include an assessment of the central heating system as a whole and a written report should be given to the consumer.

***Commission's response:***

The Commission appreciates the various comments received in this regard and where possible will take these on board in the "Competition in Supply" review we are currently undertaking.

**4. BGS Gas procurement cost**

The following responses were received regarding the BGS Gas procurement costs.

- The €8 million peaking cost is considered a real and valid cost estimate.
- This cost was excluded from the 2005/06 as part of a suite of "mitigating measures" which BGS and the Commission proposed in an effort to reduce the required tariff increase.

***Commission's response:***

The Commission has based its exclusion of the peaking cost of €8 million on the following reasoning:

- The Commission is of the view that, on balance, excluding peaking costs from the BGS gas procurement costs will not impose a significant financial risk on BGS.
- The Commission considers the peaking provision of €8 million to be a contingent cost that has not yet been incurred.
- The Commission does allow full pass through of BGS gas costs, therefore, should the peaking costs materialise they may be factored into the K Factor calculations in 2007/08.

## **5. Exceptional Costs**

The following comments were received regarding the exceptional costs.

- That a comprehensive submission on the IT separation costs was made to the CER
- The CER had been kept up to date on the project and costs associated with it.
- The total expected cost of the project is €15 million, of which approximately €11.5 million has previously been accepted by the CER as a reasonable estimate of the cost of business separation in relation to the NDM sector.

### ***Commission's response:***

BGS requested €1.19 million in exceptional costs, broken down as follows:

- €0.4 million in relation to depreciation of expenditures already approved by the Commission in accordance with CER/05/175, and
- €0.79 million in relation to depreciation of expenditures on the IT business separation project.

The Commission has decided to exclude the IT separation costs of €0.79 million on the following basis.

- The Commission will approve the appropriate level of costs associated with this project after examination of a comprehensive submission from BGS detailing the costs involved for this project.

## **6. Out-turn adjustment for under-recovery – K Factors**

The following comments were received regarding the K Factor for 2003/04:

- There is dissatisfaction with the Commission's decision to allow full pass-through of a substantial revenue over-recovery in 2004/05 while simultaneously disallowing the pass-through of a similar 2003/04 under-recovery.
- That the treatment of the 2003/04 under-recovery is unacceptable and confirmation is sought that agreed losses will be recovered during future regulated tariff reviews.

***Commission's response:***

The Commission has decided to allow the recovery of €0.91 million through the 2006/07 K Factor, in addition to the €2 million which it provisionally allowed in the 2005/06 K Factor, for the following reasons:

- The Commission adopted its approach because the under-recoveries outlined by BGS may or may not materialise in the future. The Commission's rationale on this has been fully explained to BGS.
- The Commission considers that the K Factor for 2006/07, allowing €0.91 million under-recovery with respect to 2003/04, €11.57 million over-recovery with respect to 2004/05 and an estimated under-recovery of €14.921 million with respect to 2005/06, to be €4.262 million, which has been included in the RCF for 2006/07.

**7. Gas card tariff standing charge**

The following comments were received with regard to the Gas Card tariff standing charge.

- That the standing charge on the gas card tariff be discontinued with the subsequent under-recovery of revenue covered by all other NDM customers.
- This was a valid and reasonable measure in an effort to mitigate the impact of the price increase for those customers who may experience genuine difficulties under the current billing arrangements.
- The removal of the Standing Charge on the Gas Card tariff would have a beneficial financial effect for Bord Gáis Networks as its removal would help avoid customer confusion and the necessity for site visits and telephone calls to the Call Centre.
- A concern was also raised that the Gas Card tariff is only available in the Eastern Region of the country.

***Commission's response:***

After considering the suggestions to remove the standing charge on the gas card tariff, the commission has decided not to remove this charge but rather to freeze any increase on this standing charge for the following reasons:

- At this time it is difficult to distinguish between pre-payment meter customers that require these meters due to fuel poverty and those that require them as a convenience.
- Vulnerable customers with a low gas usage will benefit from this freeze in standing charges.
- As the pre-payment meter is only available in the Eastern Region at this time, it does not offer a complete solution for gas customers in all regions.
- The Commission has recently published a decision paper relating to the policy on the installation, payment, use and tariffs for pre-payment meters. It is expected that new prepayment meters will be available throughout the country within the next year.

### **Appendix 3: UK Gas Suppliers Price Increases during 2006**

Until 2004 Britain was self sufficient in gas, since then it has become increasingly dependant on imports from Europe which presently supplies the bulk of British imports.

In Europe gas prices are traditionally linked to oil prices which have rocketed from approximately \$30 a barrel at the start of 2003 to more than \$70 a barrel today for geopolitical reasons.

Britain also has less storage capacity than its European neighbours and last winter this position was exacerbated when the biggest British storage facility, at Rough, had to shut down due to a fire.

With price rises being driven by the rising wholesale cost of gas in Continental Europe and an unpredictable supply, all six largest UK gas suppliers increased their gas tariffs twice since January 2006. Table 4 below outlines the cumulative price increases in the UK, which are between 47.3% and 30.8%.

**Table 4: Cumulative price rises in UK since January 2006**

| <b>Supplier</b>       | <b>Increase 1</b> | <b>Increase 2</b> | <b>Increase in 2006</b> |
|-----------------------|-------------------|-------------------|-------------------------|
| <b>Powergen</b>       | 24.4%             | 18.4%             | <b>47.3%</b>            |
| <b>British Gas</b>    | 22.0%             | 12.4%             | <b>37.1%</b>            |
| <b>EDF</b>            | 14.7%             | 19.0%             | <b>36.5%</b>            |
| <b>SSE</b>            | 13.6%             | 19.4%             | <b>35.6%</b>            |
| <b>Scottish Power</b> | 15.0%             | 17.0%             | <b>34.6%</b>            |
| <b>npower</b>         | 13.7%             | 15.0%             | <b>30.8%</b>            |