



Commission for Energy Regulation

An Coimisiún um Rialáil Fuinnimh

Fuel Variation Tariff (FVT) Structural Element Review Final Decision

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CER – Information Page

Abstract:

This paper sets out the Commission's final decision following a review (CER/09/055 & CER/09/087) of the structural elements of the Fuel Variation Tariff (FVT) as established in the Commission's decision paper CER/07/097.

Target Audience:

Gas Customers, Suppliers, Shippers and Producers.

Related Documents:

- CER/09/087 – FVT Draft Decision Paper
<http://www.cer.ie/en/gas-retail-market-current-consultations.aspx?article=1eb00752-2bfb-4231-8bb8-31fbe20a1e2f>
- CER/09/055 – FVT Background Note and consultation paper
<http://www.cer.ie/en/gas-retail-market-current-consultations.aspx?article=1eb00752-2bfb-4231-8bb8-31fbe20a1e2f>
- CER/09/034 – CER decision on BGES FVT charges: 1 March 2009 – 30 September 2009
<http://www.cer.ie/en/gas-retail-market-current-consultations.aspx?article=0b9546c9-e18d-4831-9c18-21ebd2d378e7>
- CER/07/097 – Decision on BGES Tariff structure for larger NDM Industrial and Commercial customers (The 'Fuel Variation Tariff')
<http://www.cer.ie/en/documents-by-year.aspx?year=2007>

For further information on this final decision paper, please contact Stuart Coleman (scoleman@cer.ie) at the Commission.

Executive Summary

This decision paper outlines the Commission's final decision with respect to the structural elements of the FVT regime. Following consultations with industry, which involved the publication of consultation papers in April and June 2009 and also subsequent meetings with respondents, the Commission has decided to retain the FVT regulated pricing mechanism in its current form with change only to the Booking window. The Commission has decided to approve a change to the booking window on the FVT contract offered by BG Energy to enhance the flexibility offered to customers. The Commission has also decided that the BG Energy FVT tariff fixed charge will be subject to review on the 1st March and 1st October each year in order to reflect market and commodity changes.

The Commission also makes clear its view that the FVT regime should be seen as a transitory measure and will be removed when the Commission is of the view that competition can function effectively in this segment of the market.

Summary of Decision

- The FVT regulated pricing mechanism will remain in place.
- From 1st October 2009 onwards BG Energy contract quotations will be open for 1 day (opening at 9:45 a.m. on day D and closing on day D+1 at 9 a.m., however, on Friday the booking window will remain open until 15:00 only). The booking window will be open for 4 days.
- Capacity discount will remain at 10%.
- BG Energy FVT tariff fixed charge will be subject to review on the 1st March and 1st October each year
- The Commission will keep the case for retaining, or removing, the FVT regime under regular review.

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1.0 Introduction

1.1 Legal Background

Under section 23 of the Gas (Interim) (Regulation) Act, 2002, the Commission for Energy Regulation (“the Commission”) is responsible for regulating charges in the natural gas market, including supply tariffs to final customers.

1.2 Purpose of this paper

The purpose of this paper is to outline to the gas industry and associated stakeholders the Commission’s decision in respect to the structural elements of the Fuel Variation Tariff offered by Bord Gáis Energy (BG Energy).

1.3 Comments Received

The Commission received three responses to the consultation paper (CER/09/087). One of the parties requested that their submission remain strictly private and confidential. The remaining two submissions were received from the following organisations:

- Bord Gáis Energy
- Viridian Power & Energy Limited

These responses are available to view on the Commission’s website. The Commission would like to thank those parties for contributing to its consultation process and ensure them that all comments were considered and given due consideration in the Commission’s final decision.

1.4 Background Information

On the 16th July 2007 the Commission published a decision (CER/07/097) with respect to the implementation of a price regulation regime (a Fuel Variation Tariff) for Non-Daily Metered (NDM) gas consumers of BG Energy with a Supply Point Capacity above 3,750kWh and consumption level > 73,000kWh gas annually. The resulting regime came into effect on the 1st October 2007. The aim of the FVT regime is to provide a transparent tariff which reflects the underlying cost of procurement and delivery of Gas to BG Energy's larger NDM customers. It was also hoped to provide the opportunity for customers to choose a tariff that is suited to their individual preference.

In the Commission's decision paper CER/09/034 the Commission stated it would conduct a full review of the structural elements of the FVT and its effects on wider competition in the FVT customer sector in the second quarter of 2009. Following comments/responses received on consultation documents CER/09/055 and CER 09/087 the Commission sets out below its final decision regarding the FVT.

2.0 FVT Structure

The FVT is a price regulated formula consisting of four elements: a gas commodity charge, a fixed rate charge, a site charge and a shrinkage gas charge. The tariff is designed to provide a transparent tariff which reflects the underlying cost of procurement and delivery of gas to those customers with an SPC greater than 3,750kWh.

Each customer's monthly invoice consists of four components:

- The **Gas Commodity Charge** (c/kWh) reflects the monthly unit cost of wholesale gas at the UK NBP. The level of commodity charge faced by any particular customer for a given month will depend on which pricing option the customer has chosen. Customers may elect to contract for a 'monthly' floating price' or 'fixed price'. The 'monthly floating price' is calculated as an arithmetic average of the last five ICE daily settlement prices for month M-1 as published on the European Spot Gas Markets. The 'fixed price' is calculated as the published ICE settlement price for the day immediately prior to the booking window.
- The **Shrinkage Gas Charge** (c/kWh) reflects the monthly unit cost of transmission shrinkage gas costs incurred by BG Energy in respect of the FVT volumes. The rate varies each month but it is charged equally to all customers regardless of which gas commodity option the customer has chosen.
- The **Fixed Rate Charge** (c/kWh) incorporates those costs which depend on the volume of gas supplied where the appropriate rate of cost recovery (per kWh consumed) remains constant through the gas year and does not vary between customers. This charge consists of transmission commodity tariffs, distribution commodity tariffs, UK transportation costs, swing flexibility and an approved margin on total costs.
- The **Transport Capacity and Own Supply-Cost Charge** (€/month) incorporates those costs which are largely independent of the gas volume consumed by a customer. These consist of transmission and distribution capacity tariffs and the administrative cost of running BG Energy's business. The transportation capacity costs are site-specific, being based on the individual capacity booking requirement for each customer.

3.0 Comments Received

On the 12th June 2009 the Commission published CER/09/087 Fuel Variation Tariff, Draft Decision Paper¹. The Commission invited comments from interested parties by 10th July 2009. The Commission received a number of comments on various aspects of the FVT. This section summarises those comments and outlines the Commission's response. The Commission appreciates comments received from respondents. The Commission's responses are in italics.

Fixed Charge

Comments by respondents:

- CER has been reticent in divulging the detailed calculations for justifying the fixed rate charge
- These changes should be at fixed dates e.g. 1 October and 1 April. To date these changes have been ad hoc at best.
- Swing premium – believe that in this sector of the market an upward sliding scale for swing should be applied over a 12 month period, ranging from 2p to 12p/therm, risk premium needs to be built into forward prices.

The Commission does not accept the claim that the CER have been reticent in divulging the calculations of the fixed charge. All elements of the fixed charge are transparent.

The Commission agrees that changes to the fixed rate charge to date have been ad hoc. Movements in commodity and currency markets over the course of a gas year can account for volatile movement in prices. To recognise this, the Commission has therefore decided the BG Energy fixed charge will be reviewed/changed twice a year on the 1st October and on the 1st March each year.

The Commission has taken account of the comment in relation to swing premium and conducted a full examination of the cost of swing. This examination involved analysis over the period '07 – '08 and from Oct '08 to Jul '09. The Commission carried out swing analysis over the FVT book as a whole and examined BG Energy's own figures for the corresponding time period. Both sets of analysis concluded that the swing premium of 1p/therm is appropriate to BG Energy's risk

¹ For details on previous consultation comments see CER/09/087.

of providing this in their product. The Commission has therefore decided to retain the existing price of 1p/therm for swing.

Capacity Discount

Comments by respondents:

- does not agree with certain suggestions that the capacity discount provision confers a competitive advantage to the incumbent relative to other competitors in the market.
- the discount of 10% over-charges BG Energy's customers.
- do not agree with the 10% capacity discount to BG Energy customers.
- alternative would be to distribute the discount via the network charge to help mitigate the effects of competition i.e. so that all customers in this bracket may benefit.

The Commission has concluded an examination of the capacity discount. The Commission has examined forecast and actual outturn data and is satisfied that a discount of 10% can be allowed. The Commission has decided the capacity discount will remain at 10% until the end of the gas year '09/'10. The Commission does not see any objectively justifiable reason for allocating the benefits of this discount to all network customers as opposed to BG Energy's FVT customer base as other competing suppliers should be able to match this discount.

Booking Window

Comments by respondents:

- Believe the extended period of five days is not merited. An expansion of the current arrangements to two days would be more appropriate. Two days of booking windows, as opposed to a two day booking window, represents a 100% improvement on current arrangements.
- Ask the CER to extend the closing time of the booking window until 9am of the following morning. This ensures that the gas price is open for less than one 24hr period (9.45 a.m. on day D until 9.00 a.m. on D+1) minimising the risk to suppliers but again enhancing the flexibility offered to customers.
- Would have preferred no change. The Commission should ensure the booking window runs only from Monday to Thursday (i.e. 4 days) and only on business days.

Following response to the Commission's proposed option of a 5 day booking window (CER09/087) concern was raised with keeping the booking window open for long periods (particularly over the weekend, which can allow for large price differentials) and with making changes to the FVT, which is a relatively new product. Responses also indicated there was no compelling argument for such a change to the structure of the booking window. After careful consideration and following discussion with suppliers, the Commission has decided that the booking window will be altered from the current two day (48hr period) booking window to four² booking days (each booking window will be open for less than 24 hrs)³. The new arrangement of the booking window should minimise risks faced by independent suppliers and BG Energy and in turn give customers greater flexibility in their purchasing requirements.

End Goal of FVT

Comments by respondents:

- Comments that the FVT will be removed once 'competition can function effectively' are not helpful to the development of the overall market and serves to highlight once again the dangers of operating in the Irish retail gas industry, where regulatory risk is higher than it ought to be.
- Segments cannot be viewed in isolation.
- Constraining competition and competitive rivalry is not the role of regulation.
- Suggest a further review point in 18 months time, thus providing the market with a greater degree of regulatory certainty and a more stable platform for competition to develop.

The Commission has always stated that the FVT should be seen as a transitory measure to enable competition to develop and will be deregulated in time. The Commission believe each market segment must be analyzed in its own right and within the wider market to gain a better understanding to how the market operates. A full and thorough analysis will be completed before any market segment is deregulated, this will of course be carried out in consultation with the gas industry.

² Booking window opens on a Wednesday following a bank holiday. The booking window following a bank holiday will remain open for 3 days only.

³ See Appendix A for details on booking window.

The Commission reiterates that the FVT would appear to be some way off being deregulated⁴ as there is insufficient evidence to demonstrate sustainable and effective competition. The first half of 2009 saw more competition emerge in the FVT sector. This demonstrates that competition is beginning to emerge, but further shows that the FVT is not ready for deregulation.

The Commission will keep the principles of the FVT under review. In any event, in order to give regulatory certainty the Commission gives notice that the FVT will not be deregulated without giving significant notice to the market.

CHP Opt Out

Comments by respondents:

- does not agree with the assertion that allowing a CHP opt-out for FVT customers would fragment the sector.
- Unfair and unjustified to discriminate between different sizes of CHP generators.

The Commission has given due consideration to the respondents comments and arguments in relation to a CHP opt-out. However, the Commission has decided there will be no CHP opt-out allowed in the FVT sector.

With competition increasing in the FVT sector, fragmenting the sector further could be detrimental. There are four active suppliers in the FVT sector, three of which are unregulated; therefore the Commission believes there is reasonable choice available to customers.

Other Comments by Respondents

- disappointed not all responses were published. This does not help a fully informed debate to take place.

The Commission agrees with the respondent, and would urge all respondents to make their responses open for general viewing as this enables a more open and honest discussion relating to the issues at hand. The Commission respectfully requests that respondents to consultations make their submissions open for publication to the wider public. Any points/data a respondents feels is of a

⁴ BG Energy market share by AQ @ 83% (data taken April '09).

confidential nature should be presented as part of an appendix which the Commission will not publish.

- BG Energy requests a further amendment to the regime which would allow BG Energy to enter into separate contracts with customers during a prevailing contractual period.

Given the late request for this amendment and in the interest of fairness and transparency in giving time for feedback to the gas industry, the Commission, at this time, believes such a change would not be appropriate.

- call upon the CER to direct BG Energy to restrict access to their systems for customers lost to other suppliers. Request the CER to direct BG Energy to desist from sending quotes/prices to end users, when it is aware that a supply contract is in place.

The Commission does not believe restricting access of customers to BG Energy's online systems is warranted. The customer has the right to access information from whichever supplier they want.

The Commission sees no issue with BG Energy contacting an FVT customer to offer a quote and gain business. All other suppliers are allowed carry out this practice and it is ultimately the choice of the customers to go with the suppliers which suits their needs. It should also be noted that BG Energy are restricted in the quotes they can offer as they are price regulated, it is therefore acknowledged that the independent suppliers have more freedom to win customers.

4.0 Decision

This decision paper outlines the Commission's position with respect to the FVT regulated pricing regime. Following consultation with industry, which involved the publication of consultation papers in April and June 2009 and also subsequent meetings with respondents, the Commission has decided to retain the current FVT regulated pricing mechanism but to approve certain amendments to the FVT contract offered by BG Energy such that it improves the flexibility offered to customers. The Commission has also decided that the fixed charge element of the BG Energy FVT tariff will be subject to review on the 1st April and 1st October each year in order to reflect market commodity movements.

Following careful consideration from respondents and examination of the FVT structure the Commission has decided the following:

Summary of Decision

- The FVT regulated pricing mechanism will remain in place.
- From 1st October 2009 onwards BG Energy contract quotations will be open for 1 day (opening at 9:45 a.m. on day D and closing on day D+1 at 9:00 a.m., however, on Friday the booking window will remain open until 15:00 only). The booking window will be open for 4 days.
- Capacity discount will remain at 10%.
- BG Energy FVT tariff fixed charge will be subject to review on the 1st March and 1st October each year.
- The Commission will keep the case for retaining, or removing, the FVT regime under regular review.

Appendix A: Booking Window

The Commission has decided that the booking window will be altered from the current two day (48hr period) booking window to four booking days (each booking window will be open for less than 24 hrs).

The new arrangement will work as follows:

- Four⁵ separate booking days will be open each month; all days will run consecutively (will only run on business days and not over weekend or bank holidays). The four booking days will run at the start of the month and will normally be open; Tuesday, Wednesday, Thursday, Friday.
- Booking window will open at 09:45 on each morning of the booking window on day D, closing at 09:00 on day D+1, except Friday where the booking window will remain open until 15:00 only (opening at 09:45 and closing at 15:00).
- FVT customers will be able to commit to contracts during any day of the booking window.
- The price quoted during each day of the booking window⁶ will be the closing wholesale price of the previous day at close of business.

BOOKING WINDOW ARRANGEMENTS FOR 2009/10

	Mon	Tues	Wed	Thurs	Fri
Oct-09		6 th	7 th	8 th	9 th
Nov-09		3 rd	4 th	5 th	6 th
Dec-09		1 st	2 nd	3 rd	4 th
Jan-10		5 th	6 th	7 th	8 th
Feb-10		2 nd	3 rd	4 th	5 th
Mar-10		2 nd	3 rd	4 th	5 th
Apr-10			7 th	8 th	9 th
May-10			5 th	6 th	7 th
Jun-10			2 nd	3 rd	4 th
Jul-10		6 th	7 th	8 th	9 th
Aug-10			4 th	5 th	6 th
Sep-10		7 th	8 th	9 th	10 th

⁵ Booking window opens on a Wednesday following a bank holiday. The booking window following a bank holiday will remain open for 3 days only.

⁶ The Commission requests BG Energy to have their online booking window updated as soon as possible, current indications suggest this will be early January 2010. In the meantime it is expected BG Energy will facilitate the new booking arrangements by phone and email.