

FLOGAS RESPONSE -CONSULTATION PAPER – REVIEW OF NON DAILY METERED RETAIL GAS MARKET CER 12/164

Q1. Respondents are invited to comment on the CER’s proposal outlined in this section to define a national market for the retail supply of natural gas to Non-Daily Metered residential customers. Are you in favour of this proposal? Outline your reasons for agreement or disagreement.

Flogas believes that the “relevant product market” is the NDM Residential gas market in ROI. Residential Natural Gas customers cannot easily switch to electricity as they have already invested heavily in a gas burning boiler and associated equipment. There is very little evidence of Natural Gas customers switching to electricity irrespective of supply price movements. Clearly Natural Gas is not a substitute for electricity. Consumers cannot power their television or currently provide lighting requirement using gas.

Some customers may prefer to purchase their electricity and gas from one supplier and others may prefer to purchase their electricity and gas from different suppliers. Consumers may elect to purchase their weekly groceries in one store or in a number of stores. These are simply consumer choice issues and choice is good. It is clear that gas and electricity cannot be considered to be the same product market.

At present the conditions of competition are significantly different in ROI and NI. This may of course change in the future.

Q2. Respondents are invited to comment on the CER’s proposal that BG Energy’s market share is presumptive of dominance, pending the examination of other economic factors. Outline your reasons for agreement or disagreement.

It is clear that BG Energy still holds a dominant market share of the residential NDM Market. Competition Law generally assumes that any market share in excess of 50% gives the holder a dominant position. The risk remains that should the market be prematurely deregulated then anti-competitive practices could occur.

BG Energy Supply is shedding customers at a reasonable rate and hence their market share will become less dominant over time.

Q3. Respondents are invited to comment on the CER's assessment of wholesale market liquidity. Outline your reasons for agreement or disagreement.

Flogas does not consider access to wholesale market liquidity to be a significant barrier to entry.

Q4. Respondents are invited to comment on the CER's assessment of economies of scale and of scope. Outline your reasons for agreement or disagreement.

Economies of scale are an issue in supplying the residential gas market. There is a minimum level of cost involved in being active in the market. This makes it more difficult for new entrants to compete with the incumbent.

Economies of scope do exist. However, such economies do not relate solely to the provision of dual fuel (gas and electricity offerings). Where a supplier has other business interests, synergies can be achieved here also.

Flogas believe that certain aspects of the current Revenue Control Formula applying to BG Energy Supply have the effect of artificially reducing BG tariffs and consequently the customer switching rate is decreased.

Q5. Respondents are invited to comment on the CER's assessment of the extent to which customer switching constitutes a barrier to entry or expansion. Outline your reasons for agreement or disagreement.

It is extremely easy for consumers to switch from one supplier to another. No barriers exist in this regard. Flogas would argue, however, that the level of bad debt arising due to debt hopping is unsustainably high and that the CER needs to amend the regulatory system to help deal with this issue.

Q6. Respondents are invited to comment on the CER's assessment of the impact of dual fuel Offerings on competitive conditions in the retail gas market. Outline your reasons for agreement or disagreement.

Flogas is of the view that BG Energy Supply still holds a dominant position in the residential market (with a market share of between 65% and 70%). We do not believe that the retail electricity and gas markets are the "same" product market. The markets for residential gas is clearly competitive at the current time with a relatively high level of customer switching.

In order to preserve a competitive market over the longer term, it is important that:

- (a) Previous monopolists are not permitted under their licence to sell below cost.

- (b) Companies offering dual fuel offerings should not be permitted under their licence to penalise “electricity only” customers i.e. electricity consumers who are on the Natural Gas grid should be able to purchase their electricity at rates no less preferential to the most favourable electricity rates available to consumers who are off the Natural Gas grid.

Q7. Respondents are invited to comment on the CER’s assessment of the significance of branding as a barrier to entry and expansion. Outline your reasons for agreement or disagreement.

The Bord Gais brand is extremely strong and has been built up over a very long period. It clearly provides major benefits to the incumbent with many consumers unwilling to switch from a brand/entity with which they are comfortable. The Bord Gais health and safety advertising reinforces this loyalty effect. Either Bord Gais Networks or Bord Gais Energy Supply need to change their brand. If BG Energy Supply wish to retain the brand, then the market share deregulation threshold should reflect this.

Q8. The CER is proposing that BG Energy remains dominant in the relevant product market for the retail supply of natural gas to Non-Daily Metered residential customers, due to its continuing high market share and the absence of factors which would significantly reduce its market power. The CER recognises that dual fuel supply may potentially mitigate market power to some extent. Respondents are invited to comment. Outline your reasons for agreement or disagreement.

All relevant factors indicate that BG Energy Supply still holds a dominant position in the NDM residential gas market. We do not see that dual fuel mitigates this dominant position in the gas market.

Q9. Respondents are invited to comment on the CER’s proposal that the overall criteria taken to define a competitive market are still valid. Outline your reasons for agreement or disagreement.

Flogas believes that the criteria currently in place for assessing when deregulation should occur are still relevant and valid.

Q10. Respondents are invited to comment on the CER's analysis of the relationship between branding and market share.

Flogas believes that the BG retail division and the Network division should be separately branded. A single branding situation causes confusion with customers. For example when Flogas mention to customers that Bord Gais Networks is the pipeline provider customers frequently think that our retail competitor provides the pipeline capacity to Flogas customers. This is obviously unhelpful.

The Bord Gais brand is extremely strong and has been built up over many years. It is unfair to new entrants who have to invest in their brand that the incumbent would hold such a benefit. The Bord Gais brand is a powerful tool in ensuring customer retention. Logically if BG Energy supply is to retain the Bord Gais brand then the market share threshold for deregulation should be correspondingly lower.

Q11. Respondents are invited to comment on the level of BG Energys market share, which when combined with the other competition criteria, could be considered to define a competitive market.

The Bord Gais brand is extremely strong and has been built up over many years. Logically if BG Energy supply is to retain the Bord Gais brand then the market share threshold for deregulation should be correspondingly lower. We would suggest that if BG Energy supply was to rebrand then an appropriate market share threshold would be 60%. On the other hand if it was decided that BG Energy Supply was to retain the Bord Gais brand (and Networks change theirs) then a threshold of 50% to 55% would be more appropriate.

Q12. Respondents are invited to comment on the CERs identification and assessment of three regulatory options. Outline your reasons for agreement or disagreement.

Logically, it makes no sense to propose the removal of price regulation when the criteria required to define a competitive market have not yet been met. Flogas believes that it is appropriate to retain the current form of price regulation until such time as the criteria for a competitive market are achieved. It is however important that the Revenue Control Formula be fully reflective of all the costs involved in serving the NDM residential gas market. If tariff are not fully cost reflective newer entrants may be forced to withdraw from the market. This would of course hinder competition in the longer term.

Flogas strongly opposes the concept of a singular price cap. If there is validity in the argument for a price cap then by definition there should be a price floor also. Presumably in this case the price floor would be the current regulated tariff price. A poorly thought out approach here would be detrimental to longer term consumer interests in a competitive market. The likely impact of a price

cap approach would be to delay deregulation, perhaps indefinitely. Below cost selling by the incumbent should in all cases be prohibited under the licensing arrangements.

Consumers can quite easily compare the various Suppliers tariff offerings. Clearly some Suppliers offer customers additional non-tariff benefits also. Supplier tariff options are clear and transparent to any consumer who has the interest to consider the issue. This is substantiated by the current high switching rate of in excess of 15%. We are strongly against suppliers being forced to construct or present their tariffs in a uniform way. It is important that Suppliers be encouraged to create tariff options which meet a variety of consumers preferences. Uniformity was considered a good thing in communist Russia but has little place in a consumer orientated market economy. Independent energy cost comparison web sites provide an additional valuable tool to consumers. Restricting choice cannot be a good thing for consumers.

Until such time as deregulation occurs Bord Gais Energy supply should not be permitted to discount gas below the regulated level. This would delay the achievement of deregulation. Discrimination and below cost selling should be prohibited under the BG licensing arrangements.