Gas distribution price control review

response to Ofgem consultation 123a/06 by the National Consumer Council

About the National Consumer Council

The National Consumer Council (NCC) makes a practical difference to the lives of consumers around the UK.

With changes in provision of services by government and companies, there is apparently more choice, and more talk about meeting consumers' needs. Yet, the rhetoric does not always match people's experience: markets can operate in ways that act against consumer interests; and consumers who are disadvantaged or inarticulate can be ignored.

The NCC uses its insight into consumer needs to advocate change. We conduct rigorous research and policy analysis to investigate key consumer issues, and use this to influence organisations and people that make change happen. We don't just respond to policy discussions, but shape future debate through our groundbreaking thinking.

An open and collaborative organisation, we seek to work with public service providers, businesses and regulators. We hold regular policy forums which provide us with a unique opportunity to exchange views and test our thinking.

Our relationship with the Department of Trade and Industry – our main funder – gives us a strong connection within government. But we are ready to challenge any organisation, public or private, that does not give consumers a fair deal.

We have linked organisations in Scotland and Wales, and a close relationship with colleagues in Northern Ireland. We play a leading role within European and worldwide consumer groups, ensuring that cross-border consumer issues are tackled and the consumer voice is heard within global institutions.

Please check our website at www.ncc.org.uk for our latest news.

We can often make our publications available in braille or large print, on audio tape or computer disk. Please contact us for details.

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1. Introduction

The National Consumer Council (NCC) uses its insight into consumer needs to advocate change, working with public service providers, businesses, regulators and Government. NCC conducts rigorous research and policy analysis to investigate key consumer issues, and uses the results to influence organisations and people that make change happen. NCC receives the bulk of its funding through the DTI.

NCC is committed to the principal of universal access for essential goods and services, including gas and electricity. This is defined as 'availability and continuous accessibility and affordability of goods and services at a specified minimum quality for all consumers'. In particular, NCC has a remit to promote the interests of disadvantaged consumers. These are people who - for example, because of low income, living in a deprived area, or a disability - are excluded from adequate provision of everyday essential goods and services or are obliged to pay more for them than better-off consumers.

NCC's strategic objectives for 2005-08 are:

- to put users at the heart of public services
- to make markets work for consumers
- to ensure that disadvantaged and vulnerable consumers get a fair deal
- to achieve more sustainable consumption.

These are in line with the Government's energy policy objectives, two of which are:

- to put the UK on a path to cut its carbon dioxide emissions by some 60% by about 2050, with real progress by 2020, and

- to ensure that every home is adequately and affordably heated.

NCC is also conscious of Ofgem's statutory duties. These include its duties: to take account of the interests of all consumers, present and future, including those on low incomes and residing in rural areas; to be aware of the effects of its actions on the environment; to promote the efficient use of electricity and gas; to contribute to sustainable development and to have regard to social and environmental guidance issued from time to time by the Secretary of State for Trade and Industry.

NCC therefore welcomes the opportunity to comment on Ofgem's Gas Distribution Price Control Review consultation (123a/06), particularly those aspects of it that relate to network extensions to non-gas communities.

2. Network extensions to non-gas communities - background

Some 20% of households do not have access to the gas network[1]. Whether a household has access to the network or not is largely a historical accident. Many diverse factors influenced where the gas mains where built with the result that there are some strange anomalies. Some communities have no access to gas, despite being surrounded by others that do; others that are relatively remote have access to gas while there are pockets in urban areas that do not. There is thus no transparent economic rationale for the extent of the present gas network[2].

It is widely accepted that natural gas provides the greatest degree of thermal comfort within a home, is energy efficient, emits less carbon than other and represents good value for money[3]. For these reasons, access to a gas supply is a highly-prized asset. Newly-built homes will almost always have access to gas provided. Those buying such homes consider a gas supply to be a pre-requisite. Newly-built homes account for the majority of homes that have been connected to the gas network since 1980.

A household with access to the gas network will have many fewer carbon emissions than a household without.

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[1] Data presented in 'UK Energy Sector Indicators 2001' (DTI) suggests that roughly 80% of households have gas central heating, 10% of the remainder have coal, oil, or electric central heating and the remaining 10% are unclassified. It is highly possible that some of the remainder will be using focal point fires.

[2] Work by Tansco for the DTI showed that there were 4,600 clusters of communities with 50 homes or more within 2 km of the existing gas network, but not connected to it.

[3] Over the past year, electricity, oil and LPG prices have risen in line with gas prices, and so the ranking of cost-efficient fuels has not changed, though the absolute fuel costs have.

This is because by far the most efficient means of heating water and space is by gas. Space heating is responsible for 61% of domestic fuel consumption. The Building Regulations 2005 (Part L) now require a condensing boiler to be fitted in all new homes, and when older boilers are replaced in existing homes. Gas condensing boilers are 91% efficient whereas oil-fired boilers are typically 75% efficient.

In its Domestic Energy File, 2006, BRE sets out in detail the various factors responsible for reductions in carbon emissions from the housing stock between 1970 and 2001[4]. The greatest decrease in emissions occurred during the 1970s when 'the most important factor reducing carbon emissions was the structural changes in domestic energy use (as the use of natural gas increased rapidly whilst the use of solid fuel and town gas fell).' This accounted for a reduction of 7 MtC. In the 1980s heating system efficiency improvements, followed closely by insulation, were the most important factors (accounting for a reduction of 4 MtC), while in the 1990s the most important factor was the rapid shift to electricity generated by gas-fired plant from coal-fired plant (which also accounted for 4 MtC)[5].

A household with access the gas network will be more energy efficient than a household without central heating. In 1970 centrally heated dwellings had average space heating

[4] See Appendix 3, 'An Analysis of the historical changes to housing stock carbon emissions', in Domestic Energy Fact File (2006): Owner occupied, Local authority, Private rented and Registered social landlord homes, J.I. Utley and L.D. Shorrock, BRE, Energy Saving Trust and Defra. http://projects.bre.co.uk/factfile/TenureFactFile2006.pdf

[5] These reductions in carbon emissions from the housing stock have been offset by a rise in overall energy demand with resultant carbon emissions.

efficiencies of 59% compared with 45.8% for non-centrally heated dwellings. In 2004, the equivalent figures are 74% and 53.7%[6]. The Energy Efficiency Commitment (EEC), administered by Ofgem, accredits energy savings to an energy supplier if they provide financial assistance to allow electric heating to be replaced with gas-fired heating in recognition of the improved efficiency. (Typically, this would be in partnership with local authorities or other Registered Social Landlords who are replacing a heating system.)[7]

Importantly, however, there have also been rises in average internal temperatures in centrally-heated homes. In 1970 the average internal temperature in properties with central heating in 1970 was 12.1 degrees C, while in 2004 it had risen to 18 degrees C. Half those households without access to the gas network do not have central heating, among whom there is a high concentration of fuel poor households. Low internal temperatures are a contributory factor to a range of chronic illnesses, including pneumonia and respiratory conditions. In dwellings without central heating, it is very hard to maintain a constant internal temperature. Individual warm pockets are the norm, for example in the kitchen or living room, with the rest of the dwelling, including the bedroom, much colder.

From the foregoing, it can be seen that there are important social, environmental and economic reasons why domestic households connected to the gas network are in a much more favourable position than those that are not.

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[6] BRE, op.cit.
[7] Energy Efficiency Commitment, 2005 - 2008, Technical Manual, November 2004, Ofgem.

3. Recommendations

Other than for newly-built homes, the small number of existing homes connected to the gas network since 1990 has largely been as a result of infill. However, these conncections have also tended to occur in a haphazard manner: Independent Gas Transporters (IGTs) who are connecting industrial sites to the gas supply, for CHP for example, have been prepared to connect domestic households at the same time, provided that they are on the route of the planned connection, and that there is enough take-up to make it worth their while. One company in particular has been active in carrying out this work.

Such schemes have been successful in some areas, where there were households in fuel poverty alongside other households. In these, funds have been leveraged from the EEC (see previous section), as well as from regional, EU and other diverse sources in order to reduce the costs of connection for fuel poor households. Nonetheless, these schemes are labour-intensive and complicated to co-ordinate, and funding sources are very difficult to access. (The consultation document states that very few additional homes have been connected since the amendment to the IGT licence in 2004.)

It is likely that some households who have access to the network, as a result of an extension, will opt to connect at a later date. For example, this could be when a new kitchen is being fitted, the home is being redecorated or when the property changes hands (on average every seven years). The option to connect becomes a valuable asset,

rather as planning permission for a building extension can be.

As regards the additional costs to consumers of a connection, for households on benefits, the Warm Front Programme, and its devolved equivalents, will fund the central heating system, while the EEC will fund the insulation and contribute to the new appliances required.

Proposed options

NCC considers that this is a unique opportunity for Ofgem to establish a robust, workable mechanism that will incentivise the extension of the gas network in a rational and consistent manner.

NCC cannot support Option 1 since we do not agree that the current situation is satisfactory. NCC does not consider that Option 2 would make enough of a difference to the economic proposition for householders to achieve significant additional connections. As regards Option 3, NCC could support the setting up of a incentive scheme to reward high standards of customer service, but not to incentivise gas network extensions. Compared with the total revenue of the GDNs, a fund on an equivalent scale to the electricity networks one described would not be sufficient to achieve the sort of step change that is required or command the necessary management attention.

Between the two remaining options, NCC strongly favours Option 5. This is a straightforward, open mechanism which would be robust enough to achieve the desired increase in connections, by setting a clear incentive to extend, where it makes sense to do so, rather than merely 'allowing' extensions to take place in a reactive manner. It also recognises that there are potential benefits for the GDNs in the longer term, as well as for the households in question, now and in the future.

In taking this position, NCC stresses that the environmental, social and economic benefits of connection to the gas network need to be fully recognised and valued. For many homes, situated close to the gas network but not connected to it, mains gas will continue be the most sustainable fuel source. In those situated far from the gas network, other options, including renewable fuel sources, will be more viable, although targeted grant assistance is likely to be required to install central heating.