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Dear Bryony

Gas Retail Governance – Further Consultation

Thank you for the opportunity to comment on the issues raised in this document. I am responding on behalf of Contract Natural Gas Limited (CNG), who are retaining me to deal with this matter for them.

CNG is one of the smaller Industrial and Commercial (I&C) shippers and suppliers in the industry. They also successfully ship gas for a number of suppliers and are closely associated with a new entrant to the market, Global Natural Gas Limited. To date, they have chosen to observe developments on this topic, but now feel it is necessary to make direct comment.

The Anti-Competitive Nature of the Governance Framework

We have significant misgivings about the governance framework that is being proposed. We believe that the Supply Point Administration Agreement (SPAA) in its current form is not only biased against smaller suppliers and new entrants, but also anti-competitive. Experience of other industry agreements has shown that active management of the agreements and protocols requires significant resources. The proposals in the consultation that resolutions should be passed on the basis of votes cast and the potential for schedules to be mandatory on licensees will make this agreement particularly onerous for smaller players. Fundamentally, it is anti-competitive that suppliers can force their competitors into adopting particular working practices.

The consultation paper draws parallels with the gas transporters' Network Codes and with the MRA in electricity. These agreements have a key distinguishing characteristic from the proposed SPAA, in that they deal with the relationship between multiple suppliers and a monopolist service provider. In these cases, the value of standardised practices stems from the equitable treatment of competitors by the monopolist. The SPAA as drafted, however, will give suppliers the opportunity to place obligations on their peers and competitors. Regardless of whether any schedules create actual barriers to entry, for example when they are mandatory, the *potential* for the existing players to create mandatory requirements will be a barrier to entry.

We believe that there is one principle of governance missing from the list presented in the document, namely the facilitation of competition. Competition fosters innovation and improvements in product quality and effective governance enables this to happen. However, the proposals in the document are seeking to standardise procedures and will constrain innovation. The effect of mandatory schedules will be to ossify a particular solution to an issue and extend prescriptive regulation, even if Ofgem is not the front-line regulator.

We recognise that there can be value in common approaches to solutions, but do not believe there is a place for mandatory schedules to the SPAA, which would tie new entrants into the approaches adopted by existing players. Instead, each supplier should be free to choose the best solutions for their business. Elective and voluntary schedules are all that is needed to facilitate this and will also enable suppliers to develop new solutions. This has parallels with the approach the FSA are adopting, where guidance is given on how to comply with an obligation, but the company is free to adopt an alternative solution that it considers meets the obligations.

<u>The Scope of the Licence Condition</u>

We believe that the case has not been made for I&C suppliers signing up to the proposed licence condition, that implications for shippers have not been recognised and that the current drafting is far too wide.

The issues that initiated these discussions arose from issues in the domestic market and particularly the advent of metering competition. We note that it is not currently envisaged that the I&C Code will be a part of the SPAA and agree with this. In the domestic sector, the scale of operations and relatively simple metering arrangements mean that common standards can have value. However, the I&C market accounts for less than 2% of the total number of supply points and the volume of transfers is correspondingly lower. Coupled with the more complex metering arrangements in the I&C market, the value of any standardised processes which the SPAA is intended to govern is much lower and it is questionable whether the benefit would outweigh the costs borne by an I&C supplier in administering the governance arrangements. A regulatory impact assessment, including a cost-benefit assessment of this form of governance compared to, for example, bilateral agreements, would be valuable.

We are very concerned that a lot of the drafting of the licence condition assumes that the governance of change of supplier procedures will move out of the Network Codes. Such a move will have significant commercial implications for shippers who are responsible for providing the correct amount of gas into the network and paying the transportation charges that are outcomes from the change of supplier processes. This does not seem to be an issue that has been addressed in the consultation process so far. We would expect there to be full consultation on the implications of separating the governance of system balancing from that for changes of supplier before any licence condition made such a change a fait accompli. The value of including GTs as parties to the SPAA will depend on the outcome of these discussions.

In addition, the current drafting of the licence condition would require licensees to sign on to a document that could expand to cover any obligation under the licence. Far from giving comfort that the scope of obligations will not extend into new and unintended areas, the relevant objectives could allow the SPAA to cover any obligation under the licence.

Procedural Arrangements under the SPAA

Ensuring there are appropriate checks and balances in the arrangements is a key factor in ensuring effective and accountable governance. The ability of suppliers to appeal change decisions is a fundamental contributor to the accountability of the arrangements and we strongly support the approach that issues of unfair prejudice should be determined through a separate appeals procedure.

Similarly, it should be incumbent on the proposer of any change (and any opposers) to secure as wide support as possible for their proposal. Apathy is not the only reason for a non-vote and so the voting regime should not institutionalise a non-vote in such a way. Voting, therefore, should be by reference to the percentage of votes capable of being cast, rather than those actually cast. Any party could then appeal the decision, during which they could use the outcome of any vote to support their case.

I hope you find these comments useful. Please call me if you wish to discuss them any further.

Yours sincerely

Arthur Probert

c.c. Colin Gaines Chief Executive, Contract Natural Gas Ltd