



Public Utilities Access Forum

Founded in 1989, the Public Utilities Access Forum (PUAF) is an informal association of organisations, which helps to develop policy on the regulation of the public utilities providing electricity, gas, communications and water services in England and Wales. PUAf facilitates the exchange of information and opinions between bodies concerned with the provision of those utilities to consumers with low incomes or special service needs, such as the elderly and people with mental and physical disabilities. It draws the particular problems of such consumers to the attention of the industries, the regulators and other relevant bodies, promoting the adoption of policies and practices that cater for their needs, exchanging information about service provision and promoting research.

Gas Distribution Price Control Review Consultation October 2006

Response from PUAf

1. PUAf is concerned by the proposals for increases in gas distribution prices in the Consultation paper. This is particularly so as the increases will come on top of substantial gas price rises over the past 18 months. Although gas distribution costs make up only a proportion of the bill, for PUAf's constituency of low income and vulnerable households the increases will add to the hardship many are facing and therefore need to face a high hurdle of reasonableness. In PUAf's view, the paper does not make a convincing case that increases at the level proposed are justified.
2. There are two areas of particular concern – the allowances for overspend on CAPEX and REPEX and the allowances for pensions.
3. In the case of pensions, whilst it is reasonable to allow the GDNs to recover the cost of ongoing pension contributions, the costs of previous under-funding and to repair deficits should have been taken into account when the current owners purchased the GDNs and reflected in the purchase price. Problems with under-funding of pensions have been well known for some time and one would expect companies buying businesses of this sort to have paid particular attention to this in the due diligence process. PUAf is not convinced it is reasonable for customers to pay these costs, which amount to almost 50% of the allowance for pension costs.
4. In the case of CAPEX and REPEX overspending, the new GDN owners should also have taken this into account in the price they paid. Furthermore, the consultation document acknowledges significant difficulties with information relating to CAPEX and REPEX. Therefore to err on the side of

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Chair: Dr Gill Owen. **Secretary:** Neil Ritchie. **Treasurer :** George King
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the companies in the split of exposure to costs seems unreasonable. Whilst it may be reasonable for customers to pay for some of the overspending, a more justifiable split might be 40% customers and 60% GDNs.

5. Apart from the specific impacts of these items on the prices that customers will be expected to pay there is a general point of principle here. Making allowances for liabilities and costs that should have been reflected in the price paid when the companies were sold could act as a perverse incentive for future such transfers of ownership. The seller gets a higher price than the buyer is happy to pay because customers will foot the bill – so shareholders in both companies benefit and customers are the losers.
6. Two other factors in the proposals reinforce PUAF's concerns. Firstly, that Ofgem proposes to maintain a cost of capital for distribution that exceeds its latest proposal for the transmission price control. Secondly, that as the new owners are aiming for greater cost savings than those envisaged by National Grid, the price control proposals could have contained a tougher efficiency incentive for reductions in controllable OPEX. These factors add to the sense that customers are not getting a fair deal in these proposals.
7. PUAF recognises that setting price controls requires judgements about whether allowances are over-generous and penalise customers or under-generous and increase risk and hence cost of capital, which is also not in the long term interest of customers. In a balanced price control proposal PUAF would expect to see some judgements that seemed to err in favour of companies and some in favour of customers. However, too many of the judgements that have been made in these proposals seem to be too generous to the GDNs, resulting in a proposed price increase that will see customers – including millions of low income households - paying higher charges than are necessary.
8. Ofgem said that there would be benefits to customers when National Grid sold the gas distribution companies. PUAF therefore would urge Ofgem to revise these proposals to give a better balance between customers and the companies. PUAF would also hope to see a better reflection of customer interests in the 5 Year price control.

20.10.06

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