By email only

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Dear Ljuban,

Classification of premises for the purposes of the standard conditions of the gas supply licence

I am writing in response to David Hunt's 12 October letter giving Ofgem's 'minded to' position on this issue.

My letter of 31 January in response to the original consultation set out in detail our views against the change proposed; in summary:

- There are no compelling arguments in favour of change; the current framework is coherent and has operated satisfactorily since privatisation;
- The change would introduce complexity and uncertainty to the existing regulatory architecture;
- The proposal did not fulfil the principles of better regulation, since it introduced a change for a small number of cases where there did not appear to be an issue.

The details of the 'minded to' letter, which has not led us to change those initial views, leaves a number of unanswered questions that might pertain in specific cases, leading to situations of uncertainty rather than the present clarity; for example:

- What does 'non-commercial collective purchase' mean in practice? Your letter defines collective purchase as applying to the "limited case of owners and tenants having direct control over the entity that is collectively purchasing the energy".

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Elsewhere, the example you give is of customers in domestic apartment blocks where their gas is “bought collectively by a wholly tenant-owned non-commercial residential management company on a not-for-profit basis for the purpose of providing heat.”

However, the detailed arrangements of these situations are likely to be complex and may not in all cases satisfy your definition.

For example:

- if some of the members of the management company are owners who have sublet the property and do not actually live there themselves then this would appear to fall outside your definition. It seems to us that the members of the management company must be the people in residence.
- unless the members have the right to appoint the directors of the management company so that it is fully within their control we could not be sure that it is a not-for-profit company, as directors may be extracting profit in the form of above market rate salaries.

- What happens if the supply to the premises also supplies activities that are not domestic; for example café, restaurant, swimming pool or gym? It would be difficult to work out whether the supply was being used ‘wholly or mainly’ for domestic purposes.

These examples demonstrate how the change proposed will remove the clarity of the present situation and bring uncertainty into our dealings with some of our customers.

Above all, such a change could introduce unacceptable regulatory risk for suppliers in respect of the licence conditions in section B of the supply licence which would now apply to such supplies; I note this was pointed to by several suppliers in responses to the original consultation.

The conditions take a number of forms: those relating to payment, including debt; and those relating to customer protection. A number of the payment terms are clearly not relevant in these circumstances, as they envisage a relationship with individual dwellings; and as we have no contractual relationship or knowledge of individual tenants several of the customer protection conditions would be problematic; this is particularly so for those applicable to vulnerable customers. We would have no legal means to discharge our obligations as any contract would not be with the final consumers of energy.

You say that in these cases you would expect the supplier may need to enter into a bespoke domestic contract "for the Domestic Customers to receive the same protections as envisaged with a standard domestic residency structure." Leaving aside the question of how this would work under tariff simplification, if these arrangements are to be considered as domestic, we would argue that as the contractual counterparty is the management company it is the management company that is the domestic customer for the purposes of the licence and not the occupants of the individual apartments. The supplier should be able to discharge any obligations (for example, information provision) through its dealings with the management company, whose responsibility it would be to keep up-to-date information about any of the tenants' special needs. To regard the individual tenants as our domestic customers would mean having to rely on the management company to help us fulfil licence conditions; this would be undesirable as it would introduce additional risk. What would happen if the management company did not keep to its side of the agreement and for some reason we were found to be in breach of one of the licence conditions? It is likely that we would still be held responsible; and what would be the sanction for the management company?

If Ofgem goes ahead with this interpretation, at the very least there should be an immediate review of section B of the supply licence in order to ensure that the conditions related to supply to individual premises do not apply to this new set of 'Domestic Customers'

Your letter asks a number of questions to try to identify any unintended consequences of your proposal. The questions and our responses are below.

Question 1: How do you currently treat multiple tenancy sites with single gas boilers with a small number of Domestic Customers?

Question 2: How do you currently treat multiple tenancy sites with a single meter point serving a large number of Domestic Customers whose combined consumption is significantly above that of a traditional single domestic residence?

In both cases these supplies would be procured by a third party and so it would be treated as non-domestic supplies.

Question 3: How many customers with whom you have a contract would be affected by the clarification described above?

Not known.

Question 4: What would be the impact on your business of the clarification described above?

As pointed out, we consider that this change would introduce significant confusion and regulatory risk.

Question 5: In principle, would it cost more for high consumption Domestic Customers as described above to be supplied with a bespoke domestic contract for gas rather than a non-domestic contract.

All contracts are priced to include the costs and risks of supply. Therefore, in principle, and all other things being equal, a bespoke domestic contract should not cost more. However, it is not clear what environmental/social obligations suppliers would face in respect of sites/supplies of this nature and, therefore, how for example CERT would be costed in to such contracts. Clarification would be welcomed.

The bespoke contract would also need to envisage what would happen in relation to pricing in situations where the customer has: (a) given notice to leave at the end of the fixed term but has not transferred supply; or (b) simply failed to respond to a contract renewal invitation.

In conclusion, it is not clear to us what Ofgem is seeking to achieve here for what we envisage would be a relatively small number of cases. The proposal will lead to confusion within the industry and the need for a review of the licence. Therefore, we would argue strongly for the status quo, which has operated well for over ten years.

Please contact me if you want to discuss any of the points above.

Yours sincerely

Gerald Jago