



UCC newsletter

utility consumers consortium
www.ucceurope.com
november 2007



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Water competition rules must change

Competition for water supplies to customers in England and Wales using more than 50 megalitres (MI) has been possible since December 2005. In all that time, we're not aware of a single customer that's changed supplier.

Ofwat say this failure is mainly due to a combination of the Costs Principle set out in legislation and the high 50MI threshold. In response to the recent Ofwat consultation, UCC strongly endorses Ofwat's analysis and attributes most of the difficulty to the Costs Principle.

There is a fear that domestic water consumers could be disadvantaged by competition for business customers but UCC points out that this wasn't the case with domestic electricity and gas consumers in the 1990s. Long before they were able to buy competitively themselves, domestics had gained from the improvements achieved through business competition. Huge cost reductions had been made through greater efficiency, and suppliers had recognised the advantages of providing good service standards.

With this in mind, there shouldn't be a narrow-minded view of avoided costs in looking to replace the existing retail-minus approach in water. UCC believes that for retail competition, the approach should employ average accounting costs, which would be a much closer fit with existing Ofwat regulation than the current regime.

UCC argues that avoided costs are much more relevant in the area of common carriage where a new supplier is seeking to provide an alternative water source. This would mean that the deferment or cancellation of a major new investment (say a new reservoir) by the water undertaker would be fully recognised in access prices. Under current 'rules' let's suppose that such a deferment/cancellation did not occur until 15 customers had switched. In this case, it would not be the

first customer who got the advantage of innovation but rather the 15th! This situation is clearly unsustainable and changes must be made – although a reduction in the 50MI threshold might help to alleviate the problem.

Ultimately, all 1.25m businesses should have choice but as a practical way forward and to alleviate fears and uncertainty, an interim threshold of 5MI should be employed, enabling 27,500 large businesses to buy competitively.

Legal advice appears to confirm that the threshold could be reduced fairly simply but a change to the Costs Principle requires primary legislation. Even if DEFRA can be persuaded to take this forward, will the Government as a whole allow Parliamentary time? The UCC very much hopes so.

Spot price surge challenges the assumptions for winter

Despite calm weather, spot gas and power prices surged in September

This surge seems to turn the logic of wholesale pricing on its head. Day-ahead gas prices hit a high of 41.9p/therm on 2 October, their highest since early November last year. And day-ahead power prices had reached £46.50/MWh a day earlier – again their highest levels since November 2006.

There have been knock-on effects for wholesale prices in to winter, with the price for gas in October closing September over 33p/therm, 20% more than the level it had been trading at four weeks earlier. Prices for the fourth quarter of this year rose 14% to just over 40p/therm during September.

EC proposes 3rd package of legislation

The energy proposals in September are intended to put consumer choice, fairer prices, cleaner energy, and security of supply at the centre of its approach.

Commission president José Manuel Barroso said: “An open and fair internal energy market is essential to ensure that the EU can rise to the challenges of climate change, increased import dependence, and global competitiveness. This is about getting a better deal for consumers and business and making sure that third country companies respect our rules.” The proposals include:

- Network ownership “unbundling”— separation of production and supply from transmission networks. As an alternative, the commission also proposed the “independent system operator” to allow existing vertically integrated companies to retain network ownership but with the assets operated independently;
- Safeguards to ensure companies from 3rd countries wanting to acquire a “significant” interest in an EU network would have to comply with the same unbundling requirements as EU countries;
- The creation of an Agency for the Co-operation of European Regulators, with binding decision powers to complement national regulators and ensure the correct handling of cross-border trade;
- Measures to strengthen and guarantee the independence of national regulators; and
- Measures to improve market transparency on network operation and supply.

The commission will work with the European Parliament and the EU Council to develop its proposals further. UK ministers hope the legislation will be adopted by all member states by June next year, approved by MEPs next autumn and implemented in early 2009. But there is likely to be much debate over the proposals.

Green groups quit new nuclear consultation process

The Government’s consultation on whether to build new nuclear power stations has suffered a blow from the withdrawal by a number of environmental lobby groups. In early September Friends of the Earth, Greenpeace, WWF-UK, CND and the Green Alliance all ended their participation. Friends of the Earth said it had made its move because:

- There was a lack of clear non-nuclear options to facilitate informed public debate;
- There was a failure to provide adequate information about the wider dangers of nuclear power;
- The consultation being rushed in five months over the summer period with the NGO stakeholder group participation also suffering from timing constraints; and
- The government appears to have decided already to proceed with a new nuclear programme.

Subsequently Berr secretary of state John Hutton said he was “very disappointed” by the groups’ decision to withdraw, adding: “We made every effort on the day to make sure the opinions of Greenpeace and other organisations were put accurately put to the public.”

Climate change levy has been mixed success says NAO

Although the climate change levy (CCL) and supporting climate change agreements (CCAs) have increased energy efficiency and reduced carbon emissions in business, the National Audit Office (NAO) said recently in a report that their effectiveness is hard to measure. The NAO said that although the CCL helped refocus attention on energy use in the period after 1999 – when it was first mooted for introduction from April 2001 – and led to improvements in energy efficiency and emissions reductions, its subsequent impact “is harder to discern”. In particular, its effect on energy prices has been limited, and the results of an NAO survey “suggest it is no longer seen as a major driver of new energy efficiencies.” The survey found that most companies do not view the CCL as “a major decision driver” when it comes to energy costs.

New gas distribution charges show very significant increases

New charges took effect from 1 October and costs in all bar one of the eight charging regions rose significantly – those in London up by nearly two thirds!

Charges for using the national transmission and regional Distribution Networks typically account for 10-20% of business gas bills. They're regulated by Ofgem and set by the respective pipeline operators. Since the sale of four of eight gas Distribution Networks (DNs) by National Grid in 2005, charges have become more variable as the new operators have developed their own rates that reflect their local costs.

Charges effective at 1 October 2007 for all bar one of the eight DN's (the exception is the East of England) see significant increases, averaging at least 20% on a year ago. There are two reasons for this. Firstly, under the 2007-08 one-year price control, Ofgem allowed the gas DN's an increase in average revenue of 11.5%. Secondly, warmer than average weather meant the operators earned less last year

than they were allowed to and are entitled to charge this shortfall plus interest in the current year. Much the most significant changes are being levied by National Grid Gas's London DN. But in all DN areas outside the East of England, customers should prepare for increases of at least 20% in their transportation costs. Such changes could push customers' bills up by 5% or so.

Indicative changes in gas transportation charges (p/therm)

Type of business	Rates at	GB average	Lowest region	Highest region
SME (614 therms/yr)	01/10/2006	15.43	13.41	17.41
	01/10/2007	19.36	17.41	22.07
	Change (%)	25.5%	29.9%	26.8%
Commercial firm (20,000 therms/yr)	01/10/2006	9.35	8.21	11.01
	01/10/2007	11.57	10.18	13.46
	Change (%)	23.7%	24.1%	22.3%
Industrial firm (200,000 therms/yr)	01/10/2006	5.02	4.39	5.77
	01/10/2007	6.35	5.67	7.34
	Change (%)	26.5%	29.1%	27.2%

No change to interruption regime yet

Interruptible users can expect transportation increases of similar magnitude to those experienced by firm industrial users. But, for this year, at least they will continue to pay around a third less for transportation than the equivalent firm use. In return, they cede the right for the Distribution Networks (DNs) to cut supplies, normally for up to 15 days, to manage the pipeline network. In practice, DN's have not interrupted on this scale of late. New arrangements are, though, on the table involving DN's seeking bids from large users to provide specified volumes and locations of interruption. All users – even network sensitive loads currently obligated to be interruptible – will be deemed firm unless they bid successfully. Thus, the days of a flat discount for interruptible transportation with minimal chance of supply cuts will be over. Current thinking is that these new arrangements should be in force by 2010.

Gas distribution charges to become capacity-based?

Ofgem has decided, for the time being at least, not to implement a proposal by the gas Distribution Networks, which would change the structure of their charges, as it carries out an impact assessment. The gas Distribution Network operators have proposed changing charges so they're 95% capacity-based and 5% volume-based compared to the current 50:50 split. Making this change would increase the fixed element of transportation charges and could lead to a move away from simple volume related pricing.

industry news

National Grid confirms view of "a less tight" winter for gas

National Grid's final Winter consultation report 2007-08 reflects a higher expectation of gas import availability, partially offset by lower supplies from storage. The forecast for gas supply, including storage at 546 mcm/d, is 15% higher than last year's base case assumption. The company said for electricity, the outlook "appears less uncertain than that for the gas market," with power station capacity at similar levels to last winter.

Small businesses get raw deal from their electricity suppliers

Energywatch surveyed levels of service provided by the Big Six to their small business electricity customers. It claims none scored a "satisfied" rating. Even so, two-thirds perceive the service is about the same as from suppliers of other goods and services.

UK energy production and demand fall

Total UK energy production in the second quarter of 2007 was 46.5mn tonnes of oil equivalent (mtoe), 5.4% lower than in the second quarter of 2006, the latest official statistics show. Total inland consumption on a primary fuel input basis was 227.7mtoe in the second quarter of 2007, 1.2% lower than a year ago.

Time to make things more competitive

Customers, energy managers and user groups are becoming increasingly more frustrated by the lack of competitive opportunities within the SME market sector – so make sure you check YOUR small print.

Their concern, and in many cases annoyance, is aimed at the antics of the suppliers who are precluding customers from being able and free to search on a realistic basis for an alternative supplier.

Restrictive clauses

Members of the Federation of Small Businesses, Association of Conservative Clubs, Federation of Fish Fryers and many others are complaining that legislation does not seem to deter suppliers from incorporating restrictive clauses which prevent change at contract end. Further concern is expressed at the fact that neither Energywatch nor the regulator appear to be interested in this worsening situation.

Notice periods

Contract terms are being massaged to provide the customer with an obligation to give notice. Such notice is demanded in a variety of forms:

- Ninety days before end of contract but not before 120 days; and/or
- 30 days before the anniversary of the start date.

Few customers realise that notice needs to be given in month eight of the contract period, where a one year contract prevails and few customers will be aware of the start date which is significantly different from the contract signed date.

Managers of multi-sited contracts have also found that these unfavourable clauses

have been slipped in and not detected until too late.

Some suppliers seem to be suffering unfairly in terms of undelivered mail and claim not to receive termination letters unless sent by recorded delivery!!

Expensive penalties

The resultant effect of not giving timely notice can be expensive. Penalty Charges and Excess Period Rollover Charges are becoming commonplace. Objections are raised in the event that a consumer wishes to change supplier whilst in Contract Rollover Period being deemed as "In Contract" and should the customer insist on leaving, Penalty or Early Termination Fees are threatened as a deterrent against proceeding with the change.

The situation at this point can worsen. The customer, having signed a valid contract with a new supplier, that is binding on both sides, finds it's financially impracticable to proceed and therefore cancels the new contract. The new supplier is then entitled to impose an Early Termination Fee as a threat against not fighting the objection and proceeding with the switch.

Price rises at end of contract

In other cases the customer has found that upon contract end, prices have risen without notification by a staggering amount. In haste to do something about it

a change of suppliers is urgently sought. Immediately the registration commences the customer is contacted and offered a refund of the excess charges and a more realistic rate for continuing for a further period. This practise is unethical and against the best interests of the spirit of competition.

Many small businesses whether part of a multi-sited contract, member of a user group or simply an individual trying to manage his own affairs are totally disenchanted with the situation that has developed within this market sector.

Hidden terms

The impetus has changed from one of true competition in terms of tariff structure and price to one of protecting market share by customer default resulting from hidden terms and conditions which frequently are not explained or disclosed at the initial sign up.

Such a situation is not in the best interests of the un-initiated SME user and is a very poor reflection upon the UK energy market.

This situation is not easy to guard against. It is as always a case of buyer beware.

Hopefully the promised code of conduct between suppliers will be considered as an urgent need and the regulator will become involved in some performance monitoring to ensure speedy resolution to this problem.

UCC 2007 meeting dates

The last UCC meeting of the year will be held on Wednesday 12th December at The Chamber of Shipping, Carthusian Court, 12 Carthusian Street, London EC1M 6EZ. Meeting are FREE for UCC Members and £90 each for guests.

Keep a look out for next year's meeting dates, they'll be posted on www.ucceurope.com

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