STATES OF JERSEY

GAS TARIFFS: REDUCTION (P.18/2015) – COMMENTS

Presented to the States on 23rd March 2015
by the Council of Ministers

STATES GREFFE

COMMENTS

The Council of Ministers, like many members, is concerned about fuel prices in Jersey and how they impact on the cost of living for Islanders. The Jersey Consumer Council has highlighted that gas prices in Jersey seem to be higher than in Guernsey and the Isle of Man. We do need to understand conditions in the Jersey gas market and what has driven trends in prices and costs, but a unilateral price cut of 5% should be rejected.

The Jersey Competition Regulatory Authority (JCRA) has been asked to commence a full-scale review of fuel supply in Jersey, including the local gas market. Jersey Gas has agreed to co-operate fully with the investigation and has already announced a 3.5% price reduction.

States Members are asked to oppose this proposition for a number of reasons –

1. It fails to understand trends in gas prices in Jersey and the factors affecting the local gas market.

2. There is no justification for such arbitrary price regulation.

3. It takes no account of the risks for the consumers of gas of imposing such price-cuts in the absence of proper analysis. Ministers wish to ensure the long-term efficiency of the gas market before making policy decisions.

4. The Assistant Minister for Economic Development has already asked officials to engage with Jersey Gas to better understand the situation in the local gas market, and has been aware since January that they were working to lower prices. The recent announcement of a tariff reduction of 3.5% with effect from 23rd March 2015 shows that arbitrary price control is not necessary and can quickly be overtaken by events.

5. The new Council of Ministers has given high priority to competition and a programme of work to ensure competitiveness in consumer markets, including gas. The Assistant Minister for Economic Development is finalising with the JCRA a fuel price review that will be conducted in coming months and that will ultimately provide recommendations, where appropriate, on how we can make fuel markets work better in consumer interests. It is encouraging that Jersey Gas has agreed to work on an open-book basis with the JCRA as part of this review to ensure that we have a full understanding of trends in the local market. We need to fully understand the issues in the local market before we can start to prescribe the solutions.

The proposition tries to explain trends in Jersey gas prices through selected quotes from coverage in the Jersey Evening Post. This is insufficient information on which to base a States' decision. A comparison of Jersey and UK gas prices (as included in the Retail Prices Index) shows that since 2000, UK gas prices have risen at a faster rate than those in Jersey. In addition, over the last 3 years, prices in Jersey have risen by 14% and those in the UK by 12%. However, such price trends do need to be treated with caution, given the different nature of gas sold in Jersey and the scale of the local market. Only through more detailed work by JCRA can we really determine whether the market is working in consumers' best interests and whether competition remedies are required.

Comparing price increases in Jersey with those in the UK is not sufficient to form conclusions, as it does not take into account differences in the local gas markets. The attached **Appendix** has been provided by Jersey Gas to explain some of the issues they feel are relevant when looking at trends in gas prices in Jersey. Some of this information has already been shared with the Assistant Minister for Economic Development after his public comments, as covered in the Jersey Evening Post on 16th January 2015. Officers met with Jersey Gas later in January to understand some of the issues facing the business. In particular, Jersey Gas have a hedging policy which means that the relationship between feedstock prices and those for Jersey customers is less straightforward than might first appear.

This information is something that the proposition of Deputy G.P. Southern of St. Helier fails to recognise, and which would have been shared with him if he had engaged with the Assistant Minister for Economic Development, his Officers or Jersey Gas on this matter.

Article 89 of the Jersey Gas Company (Jersey) Law 1989 has been copied by Deputy Southern for States Members' information. Members will see that in making decisions about tariffs, they need to satisfy themselves that the company remains commercially viable. On the evidence available, it would be difficult for States Members to be confident that they are properly taking into account the commercial reality of supplying gas in Jersey.

Deputy Southern states that Ministers are powerless in the face of price increases, but the Assistant Minister for Economic Development has shown that this is not the case by engaging with Jersey Gas at an early stage, and by working with the JCRA to agree a wide-ranging review of fuel prices in Jersey. This review will look at all stages of the fuel supply chain in Jersey to identify whether there are reasonable grounds to suspect markets are not acting in the best interests of consumers. These are the right routes through which to develop policy and protect the interests of consumers.

Arbitrarily imposed price cuts could undermine the future supply of gas and/or simply lead to higher prices in the future. **It is much better to have the JCRA working with Jersey Gas on an open-book basis, so that they can fully understand trends in the costs and prices of gas in Jersey and what, if any, remedies might be justified.**

The Council of Ministers urges members to reject this proposition, irrespective of whether the amendment of Deputy S.Y. Mézec of St. Helier is adopted.

APPENDIX

Jersey Gas comments on trends in gas prices

With respect to current (2015) tariffs –

- Jersey Gas were fully hedged (that is 80% of our outputs) for all of 2015.
- The hedges were taken out in July 2014 at competitive prices at the time.
- Hedging at this time was considered appropriate, as there were a number of conflicts in oil- and gas-producing regions (Ukraine/Syria) which, in the view of the market, could have resulted in higher prices.
- Hedging our gas purchases has served our customers well in avoiding tariff shocks, and it allowed us to budget to not increase prices in 2015. This seemed a significant challenge at the time as prices had risen continuously since 2009.
- The risk with hedging is that if the market moves down within the hedged period, it is usually very costly to "unwind" the hedge.
- Jersey Gas is a very small player in the market and as a result is a price-taker, and so the spot wholesale price quoted in the media is not the price paid for gas.

As a gas supplier, Jersey Gas faces competition for customers from competing fuel sources. We are heavily dependent on 2 key factors which are beyond our control, and mean gas tariffs are subject to fluctuation and cannot be guaranteed at a particular level. These are feedstock prices (LPG) and weather –

- Feedstock price forecast is based on hedges that we have in place, which never exceeds 80% of our requirement, plus an assumption of what we might pay for the balance, based on specialist market forecasts.
- Weather significantly affects sales, and we base our forecast on a simple average of the last 5 years' sales, plus or minus new or lost loads.
- When we develop our budgets, we have to make critical assumptions about how the future will turn out, given these uncertainties, and then try to set a tariff on that basis.
- We can advise that we will be reducing tariffs by 3.5% with effect from 23rd March 2015. This represents a saving of £57 per annum for an average central heating customer.
- From 1st October 2015, we will be introducing a new banded standing charge depending on the volume of gas that is used. The new banded standing charge does not increase the revenue that we receive, but the changes will make it easier for customers to budget for gas throughout the year, and will help us separate the cost of supplying gas to homes and businesses from the cost of gas itself, providing a fairer pricing structure.