



Guernsey Electricity Licence Modification E1585G

Draft Decision

Date: 24 September 2021

GUERNSEY COMPETITION & REGULATORY AUTHORITY

Suite 4, 1st Floor,

La Plaiderie Chambers, La Plaiderie, St Peter Port,

Guernsey, GY1 1WG

T : +44 (0) 1481 711120

E : info@gcra.gg

CONTENTS

1. Summary	3
2. Introduction	4
3. Structure of this Document	5
4. Licensing and Background	5
5. Reason for the Proposed Modification	7
6. Proposed modification.....	10
7. Next Steps	12

1. Summary

- 1.1 Guernsey Electricity Limited (**GEL**) is licensed by the Guernsey Competition and Regulatory Authority (the **Authority**) to generate, convey and supply electricity in Guernsey. There are two other electricity licensees in Guernsey, namely the International Energy Group and The Little Green Energy Company, both licensed to generate electricity for the purposes of giving or enabling supply to any premises. The Authority has also recently received a licence application for the same from Rubis Channel Islands.
- 1.2 The Electricity Law provides for essentially two forms of charges, those which tariff customers (ie the vast majority of customers) are subject to and those that are negotiated through agreements under section 16 of that law. The distinction, therefore, is between tariff customers on the one hand who are not in a contractual relationship with a licensee, and any persons who require a supply of electricity and enter into a special agreement under section 16 where the rights and liabilities between the parties are governed by the terms of the agreement rather than by the statutory regime found in sections 10 to 15 of the Electricity Law.
- 1.3 A competitor alerted the Authority to developments in the Guernsey electricity market where it was discovered that GEL was using special agreements to contract with existing customers on a bespoke basis using the provisions in section 16 of the Electricity Law. Concerns arose because of several aspects of that behaviour, namely:
 - a lack of public transparency of pricing by a regulated dominant firm,
 - the extent of that risk and implications for nascent competition given that s.16 agreements appear to have been offered to existing tariff customers,
 - there was no ability for competitors to receive information that might better assist them in informing and alerting the Authority beforehand if the pricing in these agreements placed fair competition at risk, and
 - the risk of discriminatory treatment of consumers who may not have been offered comparable prices in comparable circumstances.
- 1.4 Since those concerns appeared to have some initial merit, rather than launch a full investigation using its regulatory or competition law powers, the Authority first attempted a more proportionate approach by seeking to obtain all such agreements and assess these through a public process, relying on an existing licence condition in GEL's licence (Licence Condition 20). That licence condition placed an obligation on GEL to notify the Authority when it intends to introduce different charges, provide details of those to the Authority, publish information on those charges, and demonstrate that certain pricing principles had been applied.
- 1.5 That approach was resisted by GEL to the extent that at the present time the Authority has sight of only a single agreement but understands there are at least four agreements entered into. GEL also appealed against the Authority's Direction to comply with the above requirements. The Royal Court confirmed in July 2021 that the Authority had legal jurisdiction to regulate these

agreements, but it did not endorse the use of the licence condition relied upon by the Authority. The judgment means at the present time there are no ex-ante provisions around transparency of those prices or pricing principles that GEL must comply with when entering into arrangements using the facility of the Section 16 special agreements.

- 1.6 The Authority is therefore minded to introduce a new licence condition in GEL's licence to meet its regulatory obligations in exercise of its jurisdiction confirmed by The Royal Court. The purpose of the licence condition is to achieve the benefits of transparency and an obligation on GEL to satisfy certain due diligence safeguards regarding its pricing in special agreements prior to their coming into effect.

2. Introduction

- 2.1. The Guernsey electricity market is subject to independent ex-ante economic regulation provided for under the Electricity (Guernsey) Law, 2001 (the Electricity Law) because of unusual features. Electricity in Guernsey is an essential commodity provided by a commercial business with virtually all of the electricity market share. GEL inherited considerable commercial advantages when it was commercialised, including 100% share of the consumer market as well as the infrastructure and operations of an established business. These are advantages other licensees and potential competitors did not have, relying instead on private investment and acquiring market share based on the merits of their offering starting from a zero customer base in electricity.
- 2.2. Nevertheless, the benefits of competition to consumers can be substantial. As set out in the report by the States of Guernsey consultants reviewing the Guernsey utility regime¹.
- 2.3. An objective of the commercialisation process was to enable the trading entities to be managed commercially and adopt a commercial culture within a regulatory structure, working to firm performance targets for efficiency and productivity (see Para 4.1, page 421, Billet D'Etat 2000, 15 March²). The statutory, independent regulatory structure was introduced to represent and protect the interests of consumers and competitors (Para 4.5).
- 2.4. GEL has previously indicated that its current tariff structure requires rebalancing and was provided with clarity on the scope for doing so under its existing price control. The statement in the Authority's 2020 work programme reiterated this³.

¹ "On competition, we conclude (contrary to the view put to us by some parties) that the scope for competition on the Island – and in the regulated sectors, including electricity – is greater than is generally assumed. While Guernsey's size means the intensity of competition may not be as vigorous as in larger economies, the possibility of challenge through competitive entry can still be a powerful inducement to better performance in many sectors and industries (including the regulated sectors)." (Page 1, iv - [RPI review Guernsey utility regulatory regime.pdf \(rpieurope.org\)](#))

² <https://www.gov.gg/CHttpHandler.ashx?id=3556&p=0>

³ "GEL has indicated that its current tariff structure requires rebalancing. Given the form of the existing price control on GEL it could, of its own initiative, rebalance its tariffs based on its commercial priorities with due regard to consumer interests and other duties placed on it through licence conditions and legislation, but we understand GEL has made a decision to await the outcome of the Guernsey energy policy before doing so. CICRA therefore undertakes this work stream on the basis that GEL

- 2.5. GEL remains a monopoly at each level of the Guernsey electricity supply chain and economic regulatory protection is therefore in place to reflect the extent of risk faced by competitors given the above context in which GEL was commercialised and where nascent competition is fragile. These are in part achieved by ex-ante obligations where the Authority considers them appropriate. In practice, this translates into obligations such as transparency where the risks to the health of the overall market of lack of transparency about the behaviour of such a commercial business tends to outweigh the risks of disclosure. While ex-post investigatory and examination powers are available to the Authority, ex-ante measures are an important means to mitigate a range of risks relevant to the matters in this paper.
- 2.6. On the 10th of September the States of Guernsey resolved to agree to certain interim arrangements for tariff regulation in the electricity market. This included a resolution that the Authority’s current responsibilities for determining the tariffs and prices charged by GEL for the supply of electricity should be transferred to the States of Guernsey, acting by and through the States Trading Supervisory Board. The States directed the preparation of the necessary legislation to give effect to this as well as other decisions agreed. The Authority will in the interim carry out its functions and duties in accordance with the law as it applies.

3. Structure of this Document

3.1. The remainder of this document is structured as follows:

Section 4	Sets out the licensing and other background to the Proposed Decision
Section 5	Sets out the reasoning that underpins the proposed Licence Modification and its terms.
Section 6	Sets out the proposed modification.
Section 7	Sets out the further steps for respondents to follow in response to the proposed Licence Modification.

4. Licensing and Background

4.1. GEL is regulated by the Guernsey Competition and Regulatory Authority (**GCRA; the Authority**). The Authority has general powers conferred upon it by section 5 of the Regulation of Utilities (Bailiwick of Guernsey) Law, 2001 (the Regulation Law). These powers include:

will, of its own initiative, undertake and implement a tariff rebalancing exercise after the first quarter of 2020. It will expect that GEL will be mindful of the functions and duties placed on CICRA by the States of Guernsey through the relevant legislation. Subject to the availability of a Guernsey energy policy it would be the intention of CICRA to consider whether GEL’s tariff structure is consistent with relevant legislation, licence conditions, general economic regulatory principles and in particular reflects the ambitions of Guernsey’s energy policy.” (Page 3, [electricity-2020-work-programme.pdf \(gcra.gg\)](#))

- The power to determine conditions to be included in a licence
 - The power to require the production of information in relation to utility activities from licensees, licence applicants and other interested persons
- 4.2. The law with respect to “special agreements” for the supply of electricity is found in Part II of the Electricity Law, specifically in section 16 of that law (**Special Agreements; Section 16 Agreements**). Special Agreements are agreements for the supply of electricity by GEL otherwise than on GEL’s general regulated tariffs. GEL has the ability to provide services under Section 16 Agreements. Such services are not subject to GEL’s general tariffs but are nevertheless susceptible to price regulation.
- 4.3. In a recent judgment, which concerned an appeal by GEL against a direction by the Authority to GEL to publish certain information relating to Special Agreements into which it had entered (the **Judgment; the Direction**), the Royal Court stated:
- That the Authority could, as a matter of law, require GEL to provide the Authority with copies of the Special Agreements between GEL and its customers; but
 - The Authority could not rely on condition 20 of GEL’s licence (**LC20; the Licence**) to require GEL to publish details of its Special Agreements.
- 4.4. GEL is designated as having a dominant position in the provision of electricity in Guernsey. The Authority has the power to price regulate services provided by a dominant electricity supplier, whether through tariff services or through Special Agreements.
- 4.5. The only Special Agreement and related information that the Authority does have sight of indicates that the customer with whom the Special Agreement was concluded was previously a tariff customer whose tariff prices would have been published. The Authority has reason to believe that all Special Agreements GEL made were with customers previously on tariffs. As such the prices those customers were charged were all previously published by GEL and subject to a specific form of price regulation, namely price control. The price control was based on such customers being included in the price control which would have informed certain assumptions made when setting the control. There were also no Special Agreements the Authority was aware of prior to concerns being raised and the Authority therefore did not have any form of price regulation for Section 16 Agreements in place other than what it considered was covered by LC20 on which it relied and which the Royal Court ruled was not applicable to Special Agreements.
- 4.6. There are several issues that arise from GEL’s behaviour:
- The customers approached by GEL were existing commercial customers on tariffs rather than customers that the special agreements provisions in the law seem to have been intended for.
 - The timing of GEL’s approaches to former tariff customers is not specified in the evidence available to the Authority but it would appear from correspondence and information that GEL initiated these approaches soon after the first new entrant

electricity licence application was granted in August 2017. There is reason to consider these former tariff customers were the sort of customers that newly licensed competitors were likely to have based their market entry investment plans on for acquiring market share. In some circumstances the above conduct can constitute abusive conduct by a dominant firm; despite this the Authority was not given sight of such developments in a regulated market by a licensee with a dominant position.

- There was no prior indication of the extent of GEL's activity in this area. Dominance designations in a regulated market are intended to trigger certain rules of conduct of such licensees that ensure high levels of transparency when carrying out their commercial business since the consequences of their behaviour in such market contexts can be particularly significant for consumers and competition.

5. Reason for the Proposed Modification

- 5.1. The Authority has duties set out in Section 2 of the Regulation Law.
- 5.2. It has powers under Section 5 of the Regulation Law to do anything that appears to it to be necessary or expedient for the purpose of exercising its functions and powers and has the power to determine the conditions to be included in a licence having regard to the provisions of sections 2, 3 and 4 of that law.
- 5.3. Given these market developments and having regard to its general duties, States Directions and its functions the Authority proposes that a new licence condition should be included in GEL's licence specific to Section 16 Agreements. The licence condition would be added with the purpose of obliging a significantly greater degree of transparency of GEL's pricing than it would otherwise be prepared to provide regarding these Special Agreements.
- 5.4. The Authority proposes to place obligations on GEL requiring it, as the licensed dominant supplier of electricity, to publish details of prices when customers enter into Special Agreements with it. The licence condition will also provide for assurances that certain pricing safeguards have been adhered to by GEL prior to such agreements coming into effect, and that all details of these agreements are provided to the Authority. Transparency in the context of the Guernsey electricity market serves several purposes relevant to this proposed decision:
- 5.5. *Drawing on industry knowledge* - The know-how and insights of other licensees and industry participants is relied on to alert the Authority to potential concerns it might not otherwise be alive to. Given the existence of an effective monopoly with all the advantages over competitors discussed above, together with large information asymmetries between the regulator and the regulated entity, transparency of price changes by that dominant firm is a key means of addressing that. Competitors, including potential competitors, have commercial experience in the electricity sector or sectors like it and can therefore be an important source of insight into the commercial effect of actions taken by the dominant firm. Competitors also have specialist skills that a regulator does not have and must necessarily draw on if it is to intervene appropriately and proportionately in a sector using its powers and insights complemented by

industry expertise. Engaging such external parties on potentially significant market developments at the earliest possible stage is more likely to ensure that possible harmful behaviour by the dominant firm is highlighted sooner and potential damage to the health of the electricity market can be mitigated whether that behaviour is deliberate or inadvertent.

5.6. *Implications for other electricity customers* - While consumers may not have the same degree of commercial know-how and expertise as other stakeholders, since they ultimately pay the bills, where they might be affected by changes in the market it is appropriate for them to be informed and given the opportunity to contribute to a regulator's considerations. The transfer of a customer from a tariff to a bespoke agreement is not without potential implications for other customers. Decisions around bespoke pricing involve judgment about attribution of cost in circumstances where a material proportion of cost might be common to many users including those not party to the bespoke agreement. Without additional checks, this would be done without any regulatory oversight prior to a special agreement coming into effect. While GEL and customer entering into such bespoke agreements will undoubtedly look to their own interests, in the context of the Guernsey electricity market such decisions should, in the view of the Authority, be subject to safeguards, such as an obligation on the dominant firm to meet certain criteria in the form of pricing principles. Greater accountability through transparency can also address issues that would not otherwise be apparent. There is for example a risk that bespoke agreements include explicit or implicit assumptions that customers on tariffs fully bear the costs of pass-through rises that customers on special agreements do not⁴. This is an example of an issue of detail that is not best reviewed after the fact.

5.7. *Timeliness of intervention* - Pricing safeguards are of greater importance in a context where changes made to prices by an effective monopoly have potentially significant commercial consequences for competitors. Competitors will have based their investment plans on the regulatory protections of ex-ante regulation. In circumstances where a monopoly whose tariff customers are subject to price control constraints chooses to employ a legal provision that, in effect, removes customers previously on those tariffs from the scope of that price control, certain assurances are in the view of the Authority appropriate. Alternative regulatory interventions around pricing can take a long time in the context of commercial developments and the ability of ex-post regulatory intervention to address risks to the market after the fact can therefore be considerably less effective in mitigating harm. It can be particularly difficult to remedy or establish an objective basis for regulatory redress when parties are harmed by behaviour, particularly where damage is irreversible or subjective (for example reputational). Placing GEL under an ex-ante obligation to undertake a degree of due diligence in advance of its prices coming into effect is considered appropriate in the circumstances, since observance of pricing principles that safeguard fairness and cost reflectiveness, can be better at reducing market risk in what is a fragile competitive environment.

5.8. *Use of special agreements for purposes other than they appear intended for* – the Authority understands that GEL's explanation for entering into these special agreements was to contract

⁴ There is a facility that GEL has available to it to request the Authority to agree increases (or reductions) in its unit prices in response to changes in certain uncontrollable costs. These are termed 'pass-through costs'.

with certain customers as to allow it to rebalance and reconfigure its tariffs to some of the larger electricity users. As already set out in paragraph 2.4 of this document, GEL has for some time already been given scope to do so across its customer base and would have been expected to undertake this equitably across its tariff customer base. However, GEL chose not to do so but rather to enter into bespoke agreements under the special agreements provision in the law. The facility in the Law for special agreements and related policy documents suggest that this was available in circumstances where there was demand for very substantial, unique, and new electricity installation/supply requirements requiring particularly high levels of research and investigation as to the feasibility and cost of provision. The following extracts from the States Policy letter regarding section 16 agreements support that interpretation⁵:

“...likely that in the foreseeable future an application or applications will be received for a supply by a large consumer or consumers and Guernsey Electricity (GEL) considers that special agreements negotiated under Section 16 of the Law are likely to be appropriate for consumers requesting a very substantial supply.” (Para 1.2)

“...might arise in the event of an application being received by a potentially large consumer for the development of, for example, a data centre, or indeed of any other development of significant size and scope.” (Para 1.3)

“...it is inevitable that requests from one or several users for a very significant electricity supply will be received in the near future. In particular, these are likely to arise through the plans that are already under way for the establishment in the Island for one or several data centres.” (Para 2.2)

“The purpose of this Report is to provide the legislative framework in respect of the electricity supply to ensure that the development of data centres and other comparatively large scale developments that require a significant supply of electricity can successfully proceed.” (Para 3.4)

“However, Guernsey Electricity (GEL) considers that special agreements negotiated under Section 16 of the Law are likely to be appropriate for consumers requesting a very substantial supply and therefore the principal purpose of this Report is to amend the Electricity Law to ensure that the appropriate provisions are in place to enable GEL to conclude effective and successful special agreements under Section 16 to meet requests to supply from large consumers. Such requests could originate to support the activities of a wide range of different businesses, although in the foreseeable future it is likely that demand will arise principally from data centres.” (Para 4.2)

“While it would be easy to make the assumption that the energy costs for such a consumer might increase, in reality the increased demand, provided that it is provided efficiently, should result in significant advantages, for example in the following ways: • Through economies of scale, reducing the actual cost per unit that has to be paid for electricity by the individual consumer compared to what otherwise would have been the case. • Encouraging the transition to alternative sources of supply, for example by providing additional commercial justification for further cable links for the

⁵ <https://www.gov.gg/CHttpHandler.ashx?id=84016&p=0>

importation of electricity or for the development of renewable energy resources. Additional cable links may also have an important function in enabling the export of renewable energy from the Island should such a surplus be available at some time in the future.” (Para 4.5)

5.9. Where special agreements are used in circumstances and in a manner not anticipated, while not expressly prohibited, in the view of the Authority special scrutiny is appropriate.

5.10. *Transparency as a principle in the context of economic regulation of markets with a dominant firm* – The Authority’s interventions need to take account of the interests of consumers in particular and the market more generally. A regulatory examination confined to a bilateral exchange between a regulator and a licensee is only appropriate in very limited circumstances such as where commercial confidentiality overrides the interests of consumers and the wider market. Given GEL is an effective monopoly, the circumstances in which commercial confidentiality of consumer prices presents a substantive risk to its business would be expected to be extremely limited. The Authority does not consider that those limited circumstances apply in the context of Special Agreements that are entered into with customers in the present Guernsey electricity market on a bespoke basis, particularly when these were previously tariff customers. The default premise is therefore that transparency is appropriate as a principle.

6. Proposed modification

6.1. The proposed modification to GEL’s licence is the addition of the following licence condition:

Licence Condition 20B - Special agreements under section 16 of the Electricity Law

20B.1 Where the licensee intends

a) to enter into agreements that set charges in relation to the generation of electricity, where those charges are determined by a Special Agreement, it shall publish notice of those charges at least 7 days prior to their coming into effect,

b) to enter into agreements that set charges in relation to the conveyance of electricity, where those charges are determined by a Special Agreement, it shall publish notice of those charges at least 3 months prior to their coming into effect,

c) to enter into agreements that set charges in relation to the supply of electricity, where those charges are determined by a Special Agreement, it shall publish a notice of those charges at least one month prior to their coming into effect,

or it shall publish notice at such longer periods as may otherwise be required by law. and the licensee shall provide full details of same to the Authority at the same time as the publication notice is required.

20.B.2 The Authority may determine the maximum level of charges the Licensee may apply under any Special Agreement concluded in a relevant market in which the Licensee has been found dominant. A determination may:

- a) provide for the overall limit to apply to such charges;*
- b) restrict increases in any such charges or to require reductions in them whether by reference to any formula or otherwise; or*
- c) provide for different limits to apply in relation to different periods of time falling within the periods to which any determination applies.*

20.B.3 Where any charges in relation to generation, conveyance or supply are determined by a Special Agreement they shall be cost-justified and applied without undue preference.

20.B.4 If the Authority, after consulting the Licensee and such other persons as it may determine, is satisfied that any charges determined by a Special Agreement are in breach of the Regulation Law, Electricity Law or this Licence, the Authority may, by issuing a direction, require the Licensee to bring the charges into conformity with the Laws and/or the requirement of this Licence.

20.B.5 The Authority may exempt the Licensee from the application of Licence Conditions 20.B.1 to 20.B.3. where, in the opinion of the Authority, application of those conditions is not required to achieve pricing transparency in the interests of consumers and/or to enable the Authority to exercise its powers and duties under the Electricity Law and/or the Regulation Law. The Authority shall consider any application by a Licence for an exemption under this Licence Condition and shall place on its website and provide to the Licensee its written reasons for granting or refusing any such application.

In this Licence Condition:

“Special Agreement” means an agreement concluded between the Licensee and a customer or customers of the Licensee pursuant to section 16 of the Electricity Law

“Publish” means publication by the Licensee on a relevant and publicly accessible part of its website, which for the avoidance of doubt, must not be password protected

6.2. The proposed Licence Condition 20.B.1 is intended to oblige the publication of the details of prices in any Special Agreements entered into by GEL. Licence Condition 20.B.2 provides for a specific intervention under this licence condition that will be relied on if considered appropriate, to set those charges or place some form of constraint of those charges. Licence Condition 20.B.3 is intended to provide the Authority with adequate assurances that certain pricing safeguards have been observed by the Licensee prior to their coming into effect. Licence Condition 20.B.4 provides for timely intervention to address concerns identified by prices in those Special Agreements. Licence Condition 20.B.5 is provided given a recognition by the Authority that there may be circumstances in which Special Agreements are entered into where the safeguards underpinning the basis for the licence conditions may not be as necessary. In such an event, the Licensee is afforded the ability to make such a case to the Authority to which it will give due consideration, consulting with wider stakeholders as appropriate to the circumstances of the case, before exercising its right to exempt or not to exempt the Licensee from applicable conditions. Justification for such exemption applications should reference the basis for the safeguards and principles that are the rationale for the licence modification and explain why the case to access wider industry knowledge may not be relevant to the special

agreement for which an exemption from this licence condition is sought, why the implications for other electricity customers is not sufficiently relevant in the circumstances of that special agreement, why timeliness of intervention is not a sufficiently strong consideration for the Authority to take into account, how the use of the special agreements is consistent with States policy and why transparency as a principle in the context of regulated markets with a dominant firm is not a sufficiently strong basis in the context of that special agreement.

7. Next Steps

7.1. Objections and representations to this proposed modification and its terms should be in writing and delivered by hand or by e-mail to the following address:

Suite 4, 1st Floor
La Plaiderie Chambers
La Plaiderie
St Peter Port
Guernsey
GY1 1WG

E-mail: info@gcra.gg

7.2. All comments should be clearly marked "*Comments on GEL Licence Modification: Special agreements*" and should arrive before 5pm on Monday, 15 October 2021.

7.3. In line with the Authority's policy, it intends to make responses to the consultation available on its website. Any material that is confidential should be put in a separate annex and clearly marked as such, in order that it may be kept confidential.

7.4. Pursuant to section 5(4) of the Electricity Law, the Authority has published notice in *La Gazette Officielle* of the availability of this document on the Authority's website (www.gcra.gg).