

## **CADENT GAS LIMITED**

**-and-**

## **GAS AND ELECTRICITY MARKETS AUTHORITY**

### **Decision on Permission to Appeal**

1. Under cover of a Notice of Appeal received by the Competition and Markets Authority (CMA) on 3 March 2021, Cadent Gas Limited (Cadent) sought permission to bring an appeal under section 23B of the Gas Act 1986 against the decision by the Gas and Electricity Markets Authority (GEMA), dated 3 February 2021, under section 23 of the Gas Act 1986 to modify the conditions of the Cadent licence to give effect to the RIIO-GD2 price control determination (the Decision).

#### **Requirement for permission to appeal**

2. Under section 23B(3) of the Gas Act 1986, the CMA's permission is required before such an appeal may be brought.
3. I make this decision on permission to appeal in my capacity as an authorised member of the CMA (see paragraph 1(8) of Schedule 4A to the Gas Act 1986).
4. In making this decision I have had regard to Cadent's Notice of Appeal, to the submissions in response made by GEMA on 17 March 2021, to a further letter of 26 March 2021 from Cadent's solicitors containing a number of representations and observations on GEMA's response, and to further submissions made by GEMA's solicitors in an email dated 29 March 2021.

#### **Decision on permission**

5. On 3 March 2021 Cadent's Notice of Appeal was received by the CMA within the period prescribed by paragraph 1(3) of Schedule 4A to the Gas Act 1986.

6. Section 23B(2)(a) of the Gas Act 1986 provides that an appeal may be brought by a relevant licence holder (within the meaning of section 23(10) of the Gas Act 1986). The Decision relates to the modification of the conditions of the Cadent licence. I am therefore satisfied that Cadent is a relevant licence holder affected by the Decision.
7. Under section 23B(4) of the Gas Act 1986, the CMA may refuse permission to bring an appeal only on one of a number of specified grounds. The potentially relevant grounds in the present case are (i) that the appeal is brought for reasons that are trivial or vexatious, or (ii) that the appeal has no reasonable prospect of success.
8. Cadent seeks permission to appeal the Decision on the following three grounds:
  - (a) Ground 1: Baseline total expenditure errors. Cadent submitted that there are three distinct errors that (individually and collectively) act to reduce Cadent's baseline total expenditure allowance below its efficient costs, which it splits into three sub-grounds: 1A (Local transmission system rechargeable diversions), 1B (London regional factors) and 1C (Ongoing efficiency target).
  - (b) Ground 2: Cost of equity. Cadent submitted that the cost of equity for RIIO-GD2, prior to the application of the outperformance wedge, significantly underestimates the rate of return on equity capital required for an efficient gas distribution network. Cadent splits this into two sub-grounds: 2A (Errors in estimating capital asset pricing model parameters) and 2B (Failure to 'aim up').
  - (c) Ground 3: Outperformance wedge. Cadent submitted that application of an outperformance wedge is unjustified and unprecedented, undermines investment and distorts efficiency incentives, and is not in the interests of consumers.
9. GEMA submitted that Ground 1B should be refused on the basis of materiality. GEMA submitted that each of the specific errors alleged by Cadent under Ground 1B should be considered separately and individually for the purposes of assessing materiality, and that when considered as such, the value of each alleged error amounts to a negligible percentage of Cadent's final determination total expenditure allowance, such that it does not meet the threshold for further consideration by the CMA.

10. I have reviewed the submissions made by GEMA, the letter from Cadent's solicitors dated 26 March 2021 and the further response from GEMA on 29 March 2021. GEMA's submissions do not demonstrate sufficiently that it is appropriate to separate out each of the specific errors in the way proposed. I do not find that these calculations of the value of individual elements of Ground 1B are sufficient to demonstrate that the ground has no reasonable prospect of success.
11. I am satisfied that each of Cadent's other grounds of appeal are substantive arguments that are clearly not trivial or vexatious. At permission stage, I am not able to conclude that any of the grounds have no reasonable prospect of success. These issues will be determined as part of the appeal.

### **Grant of permission and conditions**

12. Under paragraph 1(11) of Schedule 4A to the Gas Act 1986, the CMA's grant of permission may be made subject to conditions, which may include:
  - (a) conditions which limit the matters that are to be considered on the appeal in question;
  - (b) conditions for the purpose of expediting the determination of the appeal; and
  - (c) conditions requiring that appeal to be considered together with other appeals (including appeals relating to different matters or decisions and appeals brought by different persons).
13. I have therefore considered whether, in granting permission to appeal, any grant of permission should be subject to particular conditions. The CMA received seven other applications for permission to appeal the Decision, and sought representations from the appellants and the respondent in this regard.
14. I have decided to grant permission to Cadent to bring the appeal on all grounds set out in its Notice of Appeal, pursuant to section 23B and paragraph 1 of Schedule 4A to the Gas Act 1986.
15. Pursuant to paragraph 1(11)(c) of Schedule 4A to the Gas Act 1986, this grant of permission is conditional upon the following:
  - (a) Ground 2 (Cost of equity) of this appeal shall be considered with the cost of equity grounds pleaded by National Grid Electricity Transmission plc (Ground 1), National Grid Gas plc (Ground 1), Northern Gas Networks

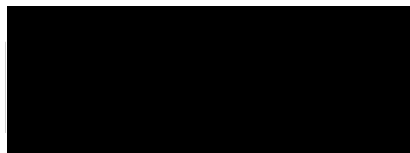
Limited (Ground 1), Southern Gas Networks plc and Scotland Gas Networks plc (joint application) (Ground 1), Scottish Hydro Electric Transmission plc (Ground 1), SP Transmission plc (Ground 1) and Wales & West Utilities Limited (Head B).

(b) Ground 3 (Outperformance wedge) of this appeal shall be considered with the outperformance wedge grounds pleaded by National Grid Electricity Transmission plc (Ground 2), National Grid Gas plc (Ground 2), Northern Gas Networks Limited (Ground 2), Southern Gas Networks plc and Scotland Gas Networks plc (joint application) (Ground 2), Scottish Hydro Electric Transmission plc (Ground 2) and SP Transmission plc (Ground 2).

(c) Ground 1C (Ongoing efficiency) of this appeal shall be considered with the ongoing efficiency grounds pleaded by Northern Gas Networks Limited (Ground 3), Southern Gas Networks plc and Scotland Gas Networks plc (joint application) (Ground 3), SP Transmission plc (Ground 3) and Wales & West Utilities Limited (Head E).

16. Grounds 1A and 1B will be considered as a separate appeal to those grounds that are joined with others.

17. I consider that the above conditions will enable the CMA to dispose of the appeals fairly and efficiently and at proportionate cost.



Kirstin Baker

*Authorised Member of the CMA*

31 March 2021