

SOUTHERN GAS NETWORKS PLC

SCOTLAND GAS NETWORKS PLC

- 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 2026, Southern Gas Networks plc and Scotland Gas Networks plc (jointly SGN) sought permission to bring an appeal under sections 23B(1) and (3) of the Gas Act 1986 against the decision by the Gas and Electricity Markets Authority (GEMA), dated 3 February 2026, under section 23(1)(a) of the Gas Act 1986 to modify the gas distribution licences of SGN (the Decision) to give effect to the RIIO-GD3 price control determinations.

Requirement for permission to appeal

2. Under section 23(B)(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 SGN's Notice of Appeal, to the submissions in response made by GEMA on 17 March 2026 and to SGN's representations to the CMA on 24 March 2026 in relation to: (i) whether the CMA should consider together each of the appellants'¹ (the Appellants) grounds of appeal relating to Ongoing Efficiency (OE); and (ii) SGN's preliminary observations on GEMA's submissions of 17 March 2026.

¹ The CMA received a total of four applications for permission to appeal the Decision from Cadent Gas Limited, Northern Gas Networks Limited, SGN and Wales & West Utilities Limited.

Decision on permission

5. On 3 March 2026, SGN'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 of the Gas Act 1986). The Decision relates to the modification of the gas distribution licences of SGN. **I am therefore satisfied that SGN is a relevant licence holder.**
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. SGN seeks permission to appeal the Decision on two grounds. The first ground is that GEMA made errors in its calculation of SGN's Totex Model Allowances (Ground 1). The second ground is that GEMA made errors in setting OE at 1% (Ground 2). SGN submitted that, as a result of the errors in each of Grounds 1 and 2, GEMA's decision was wrong on the basis of all of the statutory grounds set out in section 23D(4)(a) to (e) of the Gas Act 1986.

Ground 1 – Totex Model Allowances

9. SGN submitted that GEMA made errors in its calculation of SGN's Totex Model Allowances and that GEMA's approved baseline total expenditure under RIIO-3 (its totex allowance) for SGN underfunds SGN because GEMA made errors:
 - (a) (Ground 1A) arising from GEMA overriding each GDN's own replacement expenditure ('repex') forecasts in particular by:
 - i. Error 1: Applying its "normalisation adjustment" to GDN repex forecasts which, in the case of SGN, was flawed, unnecessary and disproportionate; and
 - ii. Error 2: Misapplying the adjustment and failing to fully "normalise" SGN repex forecasts, by applying a 'mix and match' approach to assumptions (i.e. combining WWU decommission-to-lay assumptions with SGN-specific technique assumptions).
 - (b) (Ground 1B) in relation to calculating Composite Scale Variable ('CSV') weights, in particular by:

- i. Error 1: GEMA's approach fails to reflect genuine differences between GDNs' cost structures, (Error 1A) and, by applying average weights to cost drivers, its approach is logically inconsistent with the workloads it has approved (Error 1B).
 - ii. Error 2: GEMA has placed undue weight on historical data and has failed to account for exogenous structural changes to spending.
 - iii. Error 3: GEMA's reasons for adopting its top-down method and rejecting SGN's proposed bottom-up method are flawed.
10. GEMA submitted that there is no reasonable prospect of SGN demonstrating that GEMA's approach in calculating SGN's Totex Model Allowances was wrong, i.e. that SGN's Notice of Appeal in respect of this ground has no reasonable prospect of success.
11. GEMA submitted that:
 - (a) In respect of Ground 1A, the decision which GEMA took was plainly open to it, particularly given historical modelling uncertainties and discrepancies which it had identified. The consequence of that normalisation was to award SGN greater totex than if GEMA had not so intervened. Against that background, GEMA submitted that SGN appears to recognise that some normalisation was appropriate, but submits that it alone should have been exempted from this process, even though the exercise was specifically intended to standardise modelling across all of the GDNs.
 - (b) In respect of Ground 1B, GEMA submitted that it was entitled to weigh the advantages and disadvantages of the distinct approaches to calculating CSV weights and it reached a reasoned decision as to why its approach was preferable notwithstanding the existence of alternatives. GEMA further submitted that the very premise of at least some of the grounds of appeal advanced by SGN in Ground 1B is legally unsustainable on the basis that there is no reasonable prospect of the CMA finding that SGN's suggested approach is materially better than GEMA's.
12. In preliminary observations to GEMA's submission sent to the CMA on 24 March 2026, SGN submitted that it is clear from GEMA's submission that there are factual areas of disagreement between SGN and GEMA, and that the issues raised are complex and require detailed consideration.

Ground 2 – Ongoing Efficiency

13. SGN submitted that GEMA made the following errors when it set OE at 1%:

- (a) Error 1: GEMA erred in setting a 1.0% OE parameter that is incompatible with the rate of UK productivity improvement since 2008 and/or is incompatible with and misinterprets recent, independent forecasts.
 - (b) Error 2: GEMA's expectation that gas networks are insulated from and therefore can outperform materially the economy wide slowdown is not supported by the evidence and is based on flawed reasoning.
 - (c) Error 3: GEMA erred in finding 0.7% to be the minimum OE companies can achieve and/or that 0.7% - 1.3% constitutes a plausible or narrow plausible range.
 - (d) Error 4: GEMA's assertion that qualitative factors support a 1.0% OE assumption is unevidenced and is based on flawed reasoning.
 - (e) Error 5: GEMA has erred by disproportionately decreasing allowances by setting a higher OE on the basis that the OE should be applied to stretch and incentivise companies to deliver productivity improvements
14. GEMA submitted that the OE figure is ascertained by GEMA weighing a variety of quantitative and qualitative factors, involving not a mathematical assessment but an exercise of regulatory judgement. GEMA adopted a figure of 1%, which was consistent with independent expert advice it received and regulatory precedent. The gas distribution network companies (GDNs) had each suggested that a figure of 0.5% be adopted, although electricity transmission network companies proposed higher and lower figures than this (spanning from 0.7% to 0.1%). GEMA submitted that, ultimately, GEMA's decision is plainly justifiable, and the Appellants cannot show that any alternative approach would have been materially better.
15. I have reviewed GEMA's submissions. **I have concluded that SGN should be granted permission on all of its grounds of appeal for the reasons set out below.**
16. I consider that the appeal, in relation to Ground 1, raises arguable points of substance in relation to GEMA's approach to setting repex forecasts and to calculating CSV weights, including the extent to which there were materially better alternatives to the approaches adopted by GEMA.
17. I consider that the appeal, in relation to Ground 2, also raises arguable points of substance in relation to GEMA's assessment of OE. I do not consider that the CMA can come to a decision on this issue without a substantive review of the evidence.

18. I am therefore satisfied that SGN's grounds of appeal are not brought for reasons that are trivial or vexatious. Each of Grounds 1 and 2 raises arguable points of substance which will require detailed consideration and therefore it is not the case that the appeal, in relation to Grounds 1 and 2, has no reasonable prospect of success.

Grant of permission and conditions

19. 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).
20. The CMA received a total of four applications for permission to appeal the Decision. I have therefore considered whether, in granting permission to appeal, any grant of permission should be subject to a condition that GEMA's assessment of OE, which each of the Appellants has raised in their respective Notices of Appeal, should be considered together.
21. The CMA sought representations from the Appellants and GEMA in this regard, all of whom were in favour of each of the Appellants' grounds of appeal relating to GEMA's assessment of OE being considered together.
22. Pursuant to section 23B and paragraph 1 of Schedule 4A to the Gas Act 1986 I have decided to grant permission to SGN to bring the appeal on all grounds set out in its Notice of Appeal. Pursuant to paragraph 1(11)(c) of Schedule 4A to the Gas Act 1986 this grant of permission is conditional upon the following:
- (a) that Ground 2 of this appeal (Ongoing Efficiency) shall be considered together with the OE grounds pleaded by Cadent Gas Limited, Northern Gas Networks Limited and Wales & West Utilities Limited (WWU) (Grounds 1, 2 and 3 in WWU's Notice of Appeal).
23. Ground 1 of this appeal (Totex Model Allowances) will be considered separately.
24. I consider that the above condition will enable the CMA to dispose of the appeals fairly and efficiently and at proportionate cost.

Cyrus Mehta

Authorised Member of the CMA

31 March 2026