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Via e-mail: TCR@Ofgem.gov.uk

Andrew Self
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11th February 2019

Dear Andrew,

UKPIA Response to Ofgem consultation - Targeted charging review: minded to decision and draft impact assessment

The UK Petroleum Industry Association (UKPIA) represents the eight main oil refining and marketing companies operating in the UK. These play a vital role in the manufacture and supply of petroleum products used as road transport, marine and heating fuels and for power generation. The UKPIA member companies – BP, Essar, Esso Petroleum, PetroIneos, Phillips 66, Shell, Total and Valero - are together responsible for the sourcing and supply of product meeting over 85% of UK inland demand, accounting for a third of total primary UK energy consumption[1].

The refining, distribution and marketing activities involved are spread across a large number of sites, including airports, import terminals, power generation plants, pipelines, distribution terminals and filling stations, all of which are likely to be affected by the changes proposed under the Targeted Charging Review.

Broadly speaking, UKPIA are supportive of the Ofgem proposal that residual charges be levied on final demand. Although Ofgem have made a comprehensive assessment of the options

1. BEIS Digest of UK Energy Statistics (DUKES) 2017 Tables 3.2-3.4 (see https://www.gov.uk/government/statistics/petroleum-chapter-3-digest-of-united-kingdom-energy-statistics-dukes).

identified against the main principles of the Targeted Charging Review (TCR), UKPIA believe it is also important to quantify the impacts on competitiveness of energy intensive industrial (EII) sectors, given the potential that these will be subject to the greatest impacts.

The UK refining sector faces strong competition from refineries in North West Europe and further afield - energy costs represent the second largest operating cost for the refining sector after feedstock costs[2]. It is also electro-intensive, with the UK refining sector using 4.4 GWh in 2017[3] and is exposed to competitiveness challenges and risk of carbon leakage due to direct and indirect costs incurred from GHG emission and renewable costs passed through in electricity pricing and network connection charges. This has motivated calls for refining sector eligibility for compensation against indirect EU ETS costs - this is currently not permitted under EU ETS State Aid guidelines.

UKPIA also note the commitments made in the Government's white paper "Industrial Strategy - Building a Britain fit for the future", published in November 2017[4]. This states: *"The government is committed to minimising energy costs for businesses, to ensure our economy remains strong and competitive. We recognise that our industrial electricity costs are currently higher than those of our competitors. We will act to address this by taking steps to reduce costs both now and in the future."* Any changes made by Ofgem to electricity network costs via the Targeted Charging Review should support the policy measures under consideration by BEIS to act on the commitments made under the Industrial Strategy.

Yours sincerely,

Andrew Roberts

cc:	Michael Duggan	BEIS
	Simon Stoddart	BEIS
	Paul Mannion	BEIS

2. Joint Research Centre Science for Policy Report "EU Petroleum Refining Fitness Check: Impact of EU Legislation on Sectoral Economic Performance". This is available at https://ec.europa.eu/energy/sites/ener/files/documents/0%20a_refining%20fitness%20check%20sfpr%20-%20last%20final.pdf.
3. BEIS Digest of UK Energy Statistics (DUKES) 2017 Table 5.1 (see https://www.gov.uk/government/statistics/electricity-chapter-5-digest-of-united-kingdom-energy-statistics-dukes).
4. See https://assets.publishing.service.gov.uk/government/uploads/system/uploads/attachment_data/file/730048/industrial-strategy-white-paper-web-ready-a4-version.pdf.

Attachment 1

UKPIA Response to Ofgem consultation - Targeted charging review: minded to decision and draft impact assessment

Q1. Do you agree that residual charges should be levied on final demand only?

1. Of the options assessed in the consultation, UKPIA and its member companies agree that residual charges should be levied on final demand only.

Q2. Do you agree with how we have assessed the impacts of the changes we have considered against the principles? If you disagree with our assessment, please provide evidence for your reasoning.

2. Although Ofgem have made a comprehensive assessment of the options identified against the main principles of the Targeted Charging Review (TCR), UKPIA believe it is also important to quantify the impacts on competitiveness of EII sectors, given the potential that these will be subject to the greatest impacts.

3. Energy costs represent the second largest operating cost for the refining sector after feedstock costs[2], using 4.4 GWh in 2017[Error! Bookmark not defined.]. The sector is also exposed to competitiveness challenges and risk of carbon leakage due to direct and indirect costs incurred from GHG emission, renewable costs passed through in electricity pricing and network connection charges etc.

4. In view of this exposure, it would also be useful to have an understanding of the charging regimes found in key EU Member States and extra-EU countries where EIIs compete directly with UK industrial sectors. However, from the assessment presented in Annex 4 of the consultation document, the level and basis for the banding of the fixed charges proposed appears proportionate and unlikely to pose any significant challenge to competitiveness, although UKPIA has not been able to assess the net cost impacts on the broader refining and downstream oil sector.

Q3. For each user, residual charges are currently based on the costs of the voltage level of the network to which a user is connected and the higher voltage levels of the network, but not from lower voltage levels below the user's connection. At this stage, we are not proposing changes to this aspect of the current arrangements. Are there other approaches that would better meet our TCR principles reducing harmful distortions, fairness and proportionality and practical considerations?

5. In principle, UKPIA supports the proposal to base residual charges on the costs of the voltage level of the network to which the user is connected and the higher voltage levels of the network, but not to the costs applicable for voltage levels below the voltage level of the user's connection. Inclusion of the latter would go against the principles of fairness and cannot be justified.

Q4. As explained in paragraphs 4.41, 4.43, 4.46, 4.49, 4.80, we think we should prioritise equality within charging segments and equity across all segments. Do you agree that it is fair for all users in the same segment to pay the same charge, and the manner in which we have set the segments? If not, do you know of another approach with available data which would address this issue? Please provide evidence to support your answer.

6. UKPIA support the concept of equality within charging segments and equity across all segments. It is fair for all users in the same segment to pay the same charge, based on Line Loss Factor Classes (LLFCs), reducing the potential for harmful distortions. For refinery operators, this also protects the significant investments made in on-site CHP plants over recent years to improve energy efficiency and reduce overall CO_2 emissions.

Q5. Do you agree that similar customers with and without on-site generation should pay the same residual charges? Should both types of users face the same residual charge for their Line Loss Factor Class (LLFC)?

7. Customers within a given sector with and without on-site generation should pay the same residual charges for their LLFC, as both types of user generally benefit from the security of supply afforded by their network connection.

Q6. Do you know of any reasons why the expected consumer benefits from our leading options might not materialise?

8. From the assessment presented in the consultation document, UKPIA agree that the expected consumer benefits available through implementation of the preferred options should be realised.

Q7. Do you agree that our leading options will be more practical to implement than other options?

9. UKPIA agree that application of a fixed charge for transmission and distribution residual charges should be straightforward, with no requirement for additional metering or data.

Q8. Do you agree with the approaches set out for banding (either LLFC or demanding for agreed capacity)? If not please provide evidence as why different approaches to banding would better facilitate the TCR principles.

10. The approach set out for banding based on LLFC appears to be the most practical, as this approach is already accepted by industry.

Q9. Do you agree that LLFCs are a sensible way to segment residual charges? If not, are there other existing classifications that should be considered in more detail?

11. UKPIA support the use of LLFCs as a practical basis on which to segment residual charges, and is not currently aware of any viable alternative basis.

Q10. Do you agree with the conclusions we have drawn from our assessment of the following?

a) distributional modelling
b) the distributional impacts of the options
c) our wider system modelling
d) how we have interpreted the wider system modelling?

Please be specific which assessment you agree/disagree with.

12. UKPIA has no response on this Question, as we do not have the resources to review the distributional and wider system modelling.

Q11. Do you agree with our proposed approach to the reform of the remaining non-locational Embedded Benefits?

13. UKPIA agree with the proposed approach, on the basis that wider system analysis indicates that both of the options considered (Transmission Generation Residual and full or partial Balancing System Use of Services reform) are broadly neutral with regards to system costs.

Q12. Do you agree with our proposal not to address any other remaining Embedded Benefits at this stage? Which of the embedded benefits do you think should be removed as outlined in xx? Please state your reasoning and provide evidence to support your answer.

14. UKPIA have no response on this Question concerning other remaining Embedded Benefits as identified in Sections 6.6 to 6.8 of the consultation document.

Q13. Are there any reasons we have not included that mean that the remaining Embedded Benefits should be maintained?

15. UKPIA has no response on this Question.

Q14. Do you agree with our proposed approach to transitional arrangements for reforms to: a) transmission and distribution residual charges b) non-locational Embedded Benefits? Please provide evidence to indicate why different arrangements would be more appropriate.

16. Based on our current understanding of the potential impacts on the refining sector alone, these do not support phased implementation of the reforms.

Q15. Do you agree with our minded to decision set out? If not please state your reasoning and provide evidence to support your answer.

17. UKPIA agree with the proposed changes set out in the minded-to decision, although we continue to have broader concerns regarding electricity market reform and eligibility of the refining sector for compensation against indirect emission costs.

Q16. For our preferred option do you think there are practical consideration or difficulties that we have not taken account of? Please provide evidence to support your answer.

18. UKPIA is not aware of any further considerations or difficulties that have not been taken account of concerning practical implementation of the preferred options.