**RIIO-3 Sector Specific Methodology Consultation – E3G Response**

**Summary of our view on the Future of Gas (Individual Q responses below)**

* We agree with Ofgem that the future role of gas networks remains deeply uncertain. However, the need for change is already clear: gas demand is already declining, and gas networks will need to proactively manage this transition. The future is likely to involve a combination of managed decommissioning of some assets, alongside conversion of some of the network to transport hydrogen or carbon dioxide (for CCUS). While the majority of these activities will not take place until after the time period addressed within RIIO3 it is essential that the government and Ofgem move ahead with strategic longer-term planning to avoid stranded assets in the future – which could otherwise end up increasing costs for consumers. The Strategic Spatial Energy Plan and Centralized Strategic Network Plan will be essential to help guide action and investment where needed, and Ofgem should ensure that allocations can be revised following publication of these more up-to-date plans.
* The extent to which the network will be repurposed, rather than decommissioned, is especially uncertain at distribution. Whilst Government has yet to formally make a strategic decision on the role of hydrogen for domestic heating, there is a wide body of evidence to suggest this role will be limited or non-existent. This includes independent research as well as statements by Government ministers[[1]](#footnote-2). The majority of gas distribution networks will likely need to be decommissioned in the long-term, rather than being repurposed.
* In this context, Ofgem are right to pursue an approach which avoids expenditure on potentially stranded assets and placing unnecessary additional pressure on consumer bills.
* In the event that further expenditure on speculative future needs (e.g. hydrogen) does become necessary within the timelines covered by RIIO3, uncertainty mechanisms within RIIO could provide Ofgem with sufficient options to “re-open” the price control but these need to be carefully designed.
* We agree that the Hydrogen Transport Business Model (HTBM) is a more appropriate vehicle for development of hydrogen transport infrastructure, and this spending should remain outside the scope of the RIIO-3 price control.
* This should extend to any repurposing of the existing natural gas infrastructure for hydrogen, i.e. this should remain out of scope of RIIO3. Given the high risk of investments leading to stranded assets, natural gas consumers should not be expected to foot the bill for such highly speculative investments. If such investments go ahead at all, they should be funded through the HTBM instead.

**Future of Gas**

OVQ1 – Partially Agree. Ofgem are right to pursue an approach which avoids expenditure on potentially stranded assets or placing unnecessary additional pressure on consumer bills.

However, repurposing natural gas assets should be kept explicitly out of scope of RIIO-3, due to the high risk associated with such investments leading to stranded assets. Such investments should be funded outside of the RIIO price control and should not place a cost burden on energy consumers.

Preparatory costs relating to development of hydrogen infrastructure should also be out of scope of RIIO-3. Given systematic changes to the gas networks will not take place until the mid-late 2030s, well after RIIO-3 concludes, such costs would be premature, unnecessary, and highly speculative.

Where early development of hydrogen infrastructure does take place, this should be guided by a clear long-term strategic plan, developed in collaboration between Government, Ofgem and the National Energy System Operator. Development should be aligned with strategic priority areas for hydrogen deployment (e.g. key industries without alternative options for decarbonisation), rather than lower priority use cases which are unlikely to materialise at scale (e.g. domestic heating).

The Hydrogen Transport Business Model (HTBM) is a more appropriate vehicle for development of hydrogen infrastructure at this point in time and is likely to lead to greater alignment of investments with strategic priorities. This approach would also facilitate competition and ensure incumbent gas networks do not receive unfair advantages. Ofgem should proactively encourage competition to ensure best possible value for consumers.

OVQ2 – No. As set out above, the HTBM is a more appropriate vehicle for development of hydrogen infrastructure. Any additional spending via RIIO3 faces a high stranded asset risk and offers poor value for energy consumers.

OVQ3 – Yes. Government's Strategic Policy Decision, published in December 2023, set out that hydrogen blending into gas distribution networks would only happen as an “offtaker of last resort”. The Government dEecision also noted that blending at distribution would require amendments to legislation.

Until such legislative changes have taken place, it would not be appropriate for Ofgem to pre-empt that blending will go ahead. As such, uncertainty mechanisms are the most appropriate way to address any costs.

Our analysis suggests it is highly unlikely that substantial hydrogen blending will be required at distribution, as demand from other potential offtakers significantly exceeds expected hydrogen production. Without a strategic vision, blending risks locking in hydrogen for inefficient uses like domestic heating, at the expense of other sectors where hydrogen is the only option for decarbonisation. Blending does not encourage strategic deployment of hydrogen in sectors where it is the primary option for decarbonisation, and is a costly distraction from higher priority uses of this critical fuel. According to analysis by E3G, blending could increase household gas bills by 7-20%[[2]](#footnote-3).

OVQ4 – Regardless of the outcome of Government’s strategic decision in 2026, Government has indicated that hydrogen will not be used for heating until the mid-2030s at the earliest. Therefore, it seems unlikely that the strategic decision will directly require substantial costs for networks within the RIIO-3 price control period. Networks should not be allowed to charge customers for speculative investments based on their assumptions around government decision-making on hydrogen for heating, particularly given the strong evidence case that this is not a nationally appropriate solution for heat decarbonization. If networks indicate that costs will be incurred, this claim would merit substantial scrutiny from Ofgem to ensure any costs offer value for consumers. A re-opener would be the most appropriate mechanism for this.

Whilst Government has yet to formally make a strategic decision on the role of hydrogen for domestic heating, there is a wide body of evidence to suggest this role will be limited or non-existent. This includes substantial independent research[[3]](#footnote-4) as well as statements by Government ministers[[4]](#footnote-5).

Research by the Committee on Climate Change confirmed sunk costs associated with the gas grid do not automatically mean it will be low cost to switch over to hydrogen[[5]](#footnote-6). Furthermore, extensive research suggests that hydrogen costs will inherently be higher than those of natural gas, and are unlikely to offer a cost competitive solution for domestic heating[[6]](#footnote-7). As a result, the use of hydrogen for heating would likely have a negative impact on fuel poverty.

The majority of gas distribution networks will therefore likely need to be decommissioned in the long-term, rather than being repurposed. Gas networks will need to plan ahead strategically and proactively for this transition to avoid stranded assets in the future. If networks bury their heads in the sand, this will lead to higher costs for consumers both now and the future.

OVQ5 – Strongly support. Gas networks face a significant conflict of interest and historically the evidence they have produced has been highly partial and of poor quality. Further funding would not offer good value for consumers. Independent sources of evidence likely offer better value for money.

OVQ6 – We agree that Ofgem should enable some anticipatory investment in future decommissioning liabilities, to spread the burden of expected future decommissioning expenses over current and future generations, in line with the approach taken to regulatory depreciation. Networks should be required to report on potential decommissioning costs associated with network developments, and to consider decommissioning when calculating depreciation.

Ofgem should work with Government and the National Energy System Operator to produce a comprehensive long-term plan for gas network transition and decommissioning. This document should set out a jointly agreed approach to decommissioning gas network assets and how future decommissioning liabilities will be funded.

If decommissioning costs are to be borne by gas consumers, Ofgem should consider the distributional impacts of this and consider how the impact on vulnerable and fuel poor consumers could be mitigated, for example via social tariffs.

**Scenarios and Planning Pathways**

OVQ7 – Yes, the Future Energy Scenario (FES) framework is the best currently available set of scenarios. However, Ofgem should also review business plans following the publication of the Strategic Spatial Energy Plan in 2025, and again following the publication of the Centralised Strategic Network Plan in 2026. Ofgem should ensure that appropriate mechanisms are in place to respond if gas demand decreases more rapidly than forecast within the current FES.

OVQ8 – Yes. The Leading the Way scenario is the most appropriate pathway to be used for planning purposes. In particular, it is important that the planning pathway selected should be compatible with achieving Net Zero by 2050, given Ofgem’s responsibility to ensure networks develop in a way which is compatible with the UK’s legally binding Net Zero targets. Ofgem should also work with Government and the Future System Operator to produce a comprehensive long-term plan for gas network transition and decommissioning.

OVQ9 – No. Falling Short should not be considered, as Ofgem is responsible for ensuring that network development is compatible with Net Zero by 2050.

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Using different scenarios to plan for electricity and gas could lead to contradictory investments, incurring unnecessary costs for consumers.

Gas networks face substantial conflicts of interest when developing scenarios, and should not play a role in the development of scenarios. The National Energy System Operator and Ofgem should lead the development of all common scenarios.

OVQ10 – No. Neither option is appropriate, as Falling Short is not compatible with Net Zero by 2050, and gas networks face substantial conflicts of interest in developing an alternative scenario.

The “Leading the Way” scenario should be the lead scenario for planning purposes, to ensure consistency between electricity and gas investments. When considering more conservative planning options, Ofgem should take a more nuanced approach to identifying “no regrets” and “low regrets” options rather than adopting a scenario which is inconsistent with falling gas demand and fails to comply with Net Zero.

It would be disappointing if no FES scenario is deemed appropriate. If this is the case, it is the NESO which should asked to propose an appropriate scenario, rather than the gas networks. If Ofgem were to ask gas networks to develop their own alternative scenario, this could be taken as a sign that Ofgem does not see the FES scenarios as fit for purpose.

**Uncertainty and re-openers**

OVQ35 – Yes. The re-opener approach allows Ofgem to maintain appropriate flexibility to respond to Government policy changes, and mitigates the need for allowances to include scope for unlikely or uncertain expenditure. Therefore the re-opener approach helps to ensure good value for energy consumers. Re-openers also help to avoid excessive allocations where an unlikely or uncertain expenditure does not materialize.

OVQ36 – We do not support the proposal for Use It Or Lose It (UIOLI) allowances to continue for gas distribution or gas transmission networks. The UIOLI allowance reflects a trade-off between the need to allow networks to undertake development work promptly, and the need to ensure allocations offer value for money to consumers.

As noted in the consultation, the RIIO-2 UIOLI allowances for gas networks have largely funded hydrogen related projects. It is not clear that these have offered value for money for consumers. Given the uncertain nature of the future of the gas networks, further development of these networks merits a higher degree of regulatory scrutiny. Gas networks should instead take such proposals forwards through the Net Zero Pre-construction Works and Small Net Zero Projects (NZASP) process outlined in the consultation.

OVQ37 & OVQ38 – Yes. We would support the removal of UIOLI allowances for gas networks, and for this form of project to be taken forwards as part of the NZASP re-opener process.

OVQ41 - Yes. However, networks should be expected to proactively horizon scan for potential future risks. Re-openers should not be relied on excessively as a substitute for good planning by network companies.

1. <https://www.energylivenews.com/2023/11/27/uk-energy-minister-hydrogen-will-have-limited-role-in-home-heating/> [↑](#footnote-ref-2)
2. <https://www.e3g.org/publications/the-case-against-hydrogen-blending-a-costly-distraction/> [↑](#footnote-ref-3)
3. <https://www.hydrogeninsight.com/policy/unambiguous-a-total-of-54-independent-studies-now-say-there-will-be-no-significant-role-for-hydrogen-in-heating/2-1-1571646> [↑](#footnote-ref-4)
4. <https://www.energylivenews.com/2023/11/27/uk-energy-minister-hydrogen-will-have-limited-role-in-home-heating/> [↑](#footnote-ref-5)
5. <https://www.theccc.org.uk/wp-content/uploads/2018/11/Hydrogen-in-a-low-carbon-economy.pdf> [↑](#footnote-ref-6)
6. <https://b80d7a04-1c28-45e2-b904-e0715cface93.filesusr.com/ugd/252d09_54035c0c27684afca52c7634709b86ec.pdf> [↑](#footnote-ref-7)