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Dear Chris,

Ofgem's Proposed Corporate Strategy 2004-7

Thank you for the opportunity to present our views on Ofgem's Proposed Corporate Strategy for 2004-7. This letter is not confidential and may be placed in Ofgem's library and on the website.

BP remains of the view that Security of Supply in the UK is the major challenge facing the industry over the coming years. Liberalisation in Europe, with open access to networks and markets, is key to solving this challenge and Ofgem must continue its role in influencing the European position.

There are also a number of other challenges competing for resources both from Ofgem and from industry participants, and these will need to be carefully prioritised and managed. Regulatory Impact Assessments (RIAs), that are accurate, well-informed and subject to wide consultation, will play an important role in determining these priorities.

Where regulation is necessary it should be energy-sector specific, recognising the differences between markets and customer-types, and only impact those sectors where it is relevant and appropriate. BP supports the withdrawal of regulation where competition is effectively established.

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BP has structured its specific comments in line with Ofgem's themes;

Creating and sustaining competition

BP supports the development of competitive markets and in general agrees with Ofgem's strategy to create and sustain competition.

Wholesale markets: BP supports the view that market liberalisation and connectivity issues with Europe will be crucial determinants in ensuring that the UK and Europe continue to enjoy abundant energy supplies at affordable prices. We therefore support Ofgem's strategy to encourage the reforms necessary to increase competition in European gas markets.

We support Ofgem working with bodies such as the FSA to monitor the traded wholesale market. This will help to provide increased confidence for all participants in the continued efficiency of the UK gas market.

We welcome Ofgem's intention to respond quickly and efficiently to proposals for changes to industry agreements, but these changes must be subject to RIAs as appropriate. As a principle we support evolution rather than revolution.

With regard to improved access to information relating to wholesale markets, we are supportive of the principle of greater transparency so long as issues of commercial confidentiality and liability are addressed. RIAs must be carried out to ensure that benefits outweigh the costs. BP is actively participating in the current discussions with Ofgem, Dti and NGT.

Retail markets: whilst BP supports Ofgem's commitment to improving the customer transfer process, any efforts to apply solutions should take account of the market sectors in which the problems occur, i.e. it should recognise the differences between gas and electricity markets and between domestic and industrial & commercial customers, before seeking to apply a one-size-fits-all solution that may adversely and inappropriately impact processes that are working well.

Local gas distribution: BP is participating in the Gas Forum NGT DN Disposal workgroup, and awaits with interest the enhanced RIA and further details of the proposal. We hope that these will provide assurance to the industry of both the cost-effectiveness of the proposals and of the absence of any detrimental impact to the industry. The specific concerns we expect to be addressed will be those of administrative complexity, IT cost of separation and the potential complications of the balancing regime.

BP believes that it is essential to separate out areas of potential reform which are not essential elements of a proposed sale of a DN (e.g. Exit reform), but which have been bundled together with the DN sale issue. Only then will the true value of DN sale be discovered. The non-essential elements could of course continue to be considered in their own right and be subject to their own separate RIA.

We recognise that the proposed sale of one or more Distribution Networks will require significant industry resources, and Ofgem must ensure that sufficient resources remain in place to address Security of Supply concerns and other high priority industry issues as the UK transitions from being a net exporter to a net importer of natural gas.

Metering: the industrial and commercial gas metering market is not yet competitive, and BP is actively participating in developing the framework to support competitive metering with effect from 12 July 2004. The key to effective competition in gas metering would be for Transco to offer for sale its meter assets (as it is pro-actively pursuing the disposal of its network assets) and BP would welcome Ofgem's support in facilitating this.

Regulating network monopolies

BP supports Ofgem's proposed strategy for the regulation of network monopolies, and welcomes Ofgem's recognition of the importance of taking into account future Security of Supply considerations as well as price, as the UK moves over the next few years to become a net importer of natural gas.

We also recognise the positive way in which Ofgem have progressed the LNG import debate, managing the uncertainty in the period before UK legislation is in place with the objective of responding positively to the industry's requests for guidance.

Helping protect security of Britain's energy supplies

BP believes that this is the major challenge facing the gas industry over the coming years. As the UK moves to greater import dependence, there is a need to create an appropriate environment to encourage more diverse supplies of gas. Along with this will come the challenge of accepting a wider range of gas quality in a timely fashion and with minimum disruption to consumers.

In our response to Ofgem's original request for views on its strategy, BP suggested that we consider how the regulatory regime needs to evolve in order to assure security of supply, e.g.

- Are the incentives appropriate to encourage incremental investment and new sources of supply landing in the UK?
- Is gas quality variation manageable, and how is it best managed?
- As the 2nd Directive is transposed into law in member states, does a level playing field exist across Europe (and at a consistent pace in all member states)?

BP agrees with Ofgem's view that we should avoid the risk that customers are forced to pay excessive costs to "gold-plate" infrastructure. We would, however, add that it is also important to ensure that in the drive to reduce customers' costs, the system is not reduced to a level that offers insufficient "insurance" capability, thereby increasing Security of Supply risks for customers beyond acceptable levels.

A leading voice in Europe

BP supports Ofgem's role in influencing and shaping the debate in Europe; this is closely linked with concerns over future Security of Supply. There is a need for a robust framework that incentivises long-term investment and includes the promotion of active traded markets in gas and power.

The three main challenges in the short to medium term are;

- The UK's transition to a net importer of natural gas
- Transposition of the 2nd Gas Directive into UK legislation
- The pace of liberalisation across Europe

It is important that UK consumers are not disadvantaged by variances in the degree of de-regulation between member states.

Ofgem have clearly recognised that UK regulation can no longer be undertaken in isolation from mainland Europe, and BP acknowledges Ofgem's response to the call for them to become more closely involved in shaping and influencing the EU's liberalisation debate and agenda.

Helping protect the environment

BP strongly supports emissions trading as the leading element within a suite of market-based initiatives to achieve environmental objectives. An effective, clear and transparent EU emissions trading scheme is a priority and BP welcomes Ofgem's support in this area.

Improving Ofgem's efficiency and effectiveness

BP welcomes Ofgem's recognition of the financial impact of regulation on industry costs, as well as the indirect costs of participating in industry workgroups and responding to consultations. We would be interested in hearing the scope of Ofgem's review of how they work and organise themselves with a view to lowering running costs. We would be pleased to contribute to this debate at the appropriate time.

It would help if Ofgem could better recognise issues of commerciality and appreciate the impact of regime changes on industry participants and consumers. We expect that increased application of RIAs will assist with this. We welcome the positive step of the introduction of RIAs and urge Ofgem to continue the ongoing refinement of the RIA process.

A key challenge for Ofgem this year will be for it to prioritise work activities in order to effectively allocate limited resources across those issues that are demonstrated to provide the greatest benefits.

Conclusion

Security of Supply is currently the major challenge faced by the UK; this is closely linked with liberalisation in Europe. We welcome Ofgem's focus on these areas in particular, and the utilisation of effective RIAs in determining the priorities of further activities requiring industry and Ofgem resources.

Please do not hesitate to contact me if you would like to discuss any of the points raised.

Yours sincerely,

Beverly Ord
Regulatory Affairs