

The Gas Forum



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Sir John,

Gas Forum Response to Ofgem open letter – Ofgem’s five year strategy 2007 – 2012

I am pleased to be able to respond on behalf of the Gas Forum to your request for input into Ofgem’s five year strategy.

The areas or challenges that the Forum’s members would like to see included in the forthcoming strategy are set out in order of the priority in which we view them;

1. Reducing the Regulatory Burden.

Gas Forum members believe that Britain already enjoys the benefits of a vibrant, self sustaining and fiercely competitive market in the shipping and supply of gas. Achieving this position has been at least partly due to the leadership shown by Ofgem in the past; however it is now more appropriate than ever that the regulator should withdraw from leading change to a position of monitoring the market.

This is perhaps the key challenge faced by the industry in the short to medium term - how to enable Ofgem to successfully minimise its activities in the market, withdraw to the sidelines and adopt a very light touch regulatory position.

In the past there has been a number of wide ranging initiatives sponsored and sometimes driven by Ofgem, discussion and development of which has placed a significant burden upon our member’s resources, often with little or no tangible benefits. We believe that the time is now right for Ofgem to become responsive to issues that arise from within the competitive market rather than proactively seeking change and that it should slim down its operations accordingly. The agenda for further evolution can and should be driven from within the industry.

This issue is not one of efficiency or of costs alone and will not be resolved by Ofgem controlling and spreading its costs over a greater number of initiatives. It requires an absolute reduction in activity and a corresponding reduction in resources. It is perhaps a moot point as to which should lead, for example a reduction in staff numbers would automatically lead to a reduction in activity. Members note the achievement of “nearly 10% cost savings” yet believe that the downward pressure on the regulators costs does not match that on market participants

Therefore the Forum would like to see firm plans for the reduction in regulation with some clear milestones and the publication of criteria by which Ofgem can satisfy itself that its withdrawal would not prejudice its duty to protect customers' interests or lessen the degree of competition. The Gas Forum would be happy to work with Ofgem in defining such a plan.

Forum members also believe that Ofgem's future plans should include a "post investment appraisal" with publication of details of the actual benefits derived from projects compared to those forecast in its Regulatory Impact Assessments. In this regard the Forum would specifically like to see proposals from Ofgem as to how it intends to monitor and report upon the actual costs and benefits from the entry reforms compared with the estimates used to justify the project. We would also like to understand what feedback loops mechanisms are in place to improve Ofgem's estimation process and what action it might contemplate where the estimated benefits upon which significant decisions are based fail to materialise.

2. Security of Supply

In the last few years this essential subject has received a great deal of deserved attention but some of the resulting actions, notably modifying the Uniform Network Code (UNC), have seemed rushed, ill timed and short sighted. Some Forum members have undertaken initiatives involving infrastructural development which require significant long term investment and others may be considering further investment but the key to viability of all these projects is a predictable degree of commercial stability and low regulatory risk.

The frequent changes to the UNC which are no doubt designed to improve security of supply can have unexpected and undesirable consequences. For example further development to incentivise gas balancing through a penal cash out regime does not deliver security of supply. Britain already has one of the most heavily penalised regimes in Europe yet security of supply remains an issue. In practice the present regime is more likely to result in a reduction in the number of market participants and consequent diminution of customer choice rather than increasing supply security.

The Gas Forum would therefore urge Ofgem to allow greater time for consideration of all aspects of proposed modifications which have a potential impact upon security of supply. As a matter of principle the Forum would not favour centralised planning but in this area a degree of centralised oversight and co-ordination is required. It is therefore proposed that, in keeping with the principles of better regulation Ofgem should undertake the co-ordination role which is an appropriate use of its resources, and, using long range planning information available to it, set up (or ask the Joint Office of Transporters to set up) a workgroup to consider what changes or developments in the UNC are either necessary or desirable to promote long term security.

Members are also concerned at the potential threat to gas prices and security of supply presented by the prospect of differing gas quality specifications between GB and mainland Europe. We are concerned that this disparity could restrict future supplies from Europe, or elsewhere in the form of LNG. The technical solutions are at hand and failure to make the necessary investment in good time must not be allowed to act as a barrier to imports. We therefore urge Ofgem to put pressure upon both DTI and National Grid to ensure that the infrastructure investment necessary to facilitate supplies is required to be provided in a timely fashion as part of the regulated activities.

3. Promoting fair competition in Europe

Whilst our members have mixed views on Europe, the Forum nevertheless continues to support Ofgem's role in influencing European partner states to deliver compliance with

their existing EU obligations. At the same time the Forum would like to see more rigour and transparency in the budgetary aspects of Ofgem's European activities and a demonstration that those activities are delivering value for money.

In keeping with our views on reducing the regulatory burden Forum members would wish to see Ofgem fully embracing the principles of better regulation, in spirit and practice, as well as in name, and promoting those ideals in Europe. In addition Ofgem should advocate harmonisation of the European position on environmental issues such as carbon emissions and energy efficiency which should help simplify business conditions for our members.

Finally in this area we would ask Ofgem to make more effort in disseminating information about developments in the EU, perhaps through newsletters and seminars as appropriate.

4. Regulating monopoly service providers.

Gas Forum members are very keen to see Ofgem maintain its attention on ensuring that the regulated monopolies deliver and continue to deliver, the best possible value for money services. In short we believe that the overall extent of regulation in Britain can and should be reduced and that the regulator should concentrate to a much larger extent on the monopoly sectors of the industry rather than on the competitive supply sector.

Naturally the Distribution Price Review is the major vehicle for setting out what is required from the network operators and members will be contributing to this review both individually and through participation in the Forum's Workgroup. However there may well be scope for examining the range and standards of service being provided to ensure that the service providers are applying appropriate resources to the activities within their organisations. Echoing an earlier point, the Forum would also wish Ofgem to ensure that the service providers are investing properly and that benefits derived are accurately measured and compared with those claimed either within the Price Review or as special projects (e.g. entry reforms).

Within this context the Forum would like to see Ofgem undertake specific work to identify and eliminate potentially perverse incentives. An example of an area where members feel this may prove useful is that of leakage. We would also like to see the incentives simplified, more transparent and where appropriate linked to delivery of services and/or improved infrastructure.

I trust that you will find our input useful and that you are able to incorporate the points made into your Draft Corporate Plan. As in the past I would be happy to discuss any of the issues raised in this letter with you and am keen to establish dialogue at an appropriate level to assist in carrying forward the programme of change implied.

Yours sincerely,

Steve Briggs

Chairman, Gas Forum