# Ofgem Consultation on Gas Transmission Charging Review:

# Response by Oil & Gas UK

Oil & Gas UK is pleased to respond to the consultation on Ofgem's proposed policy position on the GTCR. We offer the following generic comments on the policy position and on the accompanying impact assessment, which we hope will be considered before Ofgem takes a final decision. We do not seek at this early stage to capture or to present all the diverse positions of our individual member companies.

**Analysis of current arrangements.** Ofgem has identified a number of alleged deficiencies in the current entry capacity charging arrangements. Some of these are well-defined and widely understood, for example the potential barrier to UK gas imports from an ever-increasing TO entry commodity charge. However, the alleged costs and benefits of the proposed changes are not presented within the context of the competing objective of GB tariff design (cost-reflectivity, equity, efficiency, stability/predictability, security and EU NC compliance). There may indeed be a good case for revision of some aspects of the current arrangements but the case for the particular radical reform proposed (a fully-floating capacity charge and the reduction of short-term discounts) is not convincingly made. Is the objective to comply with what is expected to emerge shortly in the EU Tariffs Network Code or is it a principled move to radically re-design the GB regime according to new economic principles regardless of the TAR NC?

The policy position represents a very radical change in the principles of GB tariff design. Has sufficient consideration been given to a less radical reform such as the reduction in the existing discounts for short-term capacity products alone?

**Modelling as basis for policy**. We have reservations about the reliance of Ofgem's policy position on the outputs of a model which Ofgem itself acknowledges is necessarily an abstraction from reality and is itself reliant on a series of behavioural assumptions. It is clear that CEPA made considerable efforts to construct a plausible and consistent model. However, Ofgem appears to be placing excessive weight on its single-point outputs as a means of assessing the impact of the proposed reforms. We are not convinced that the model successfully captures all the important distributional effects of the proposed reform and it is not evident how sensitive the combined outputs are to changes in the model's assumptions.

**Distributional effects**. Even though the application of the fully floating capacity charge is not yet determined, the proposed reform will clearly create some significant winners and losers and will entail changes to existing long-term capacity contracts. It should be a matter of concern to Ofgem and DECC that the introduction of fully floating capacity charges may also introduce additional capacity price risk for prospective new projects which need to secure long-term entry capacity.

**Allocation of historical network costs**. Ofgem lays much emphasis on what it sees as the inappropriate allocation of 'historical network costs', which are reflected in the regulatory asset base and contribute to the calculation of allowed revenue. In Ofgem's view, the current flow-based charging means that some shippers are not making an appropriate contribution to network costs and are not paying the 'true cost of network access'. This argument is at least in part based on a judgement about equity and a proper allocation of costs and benefits but it alone does not itself provide support for the particular reform which Ofgem is proposing. There are number of competing objectives to be served in the design of a charging regime and we believe that these objectives need to be more clearly identified and the trade-offs between them explicitly addressed before a final decision is made.

**Over-booking of short-term capacity**. The policy position cites what it sees as the 'overbooking' of capacity arising from the current discounts for short-term products. However, it is not made clear how this 'overbooking' leads to inefficient use of the network or how it might impair NGGT's operation of the network. If there is evidence that NGGT's operational role is impaired in the current regime, it would be helpful to present it. In our view, in a market with highly variable sources of supply, observed flows and shipper nominations are likely to remain key indicators for network management. An assessment of the alleged incremental benefits to NGGT may be helpful to win support for Ofgem's policy position.

**Network investment and consumer impact.** 'Overbooking' of capacity is also alleged to create 'a risk of inefficient investment in the network by NGGT'. This claim too deserves to be examined in more detail, not least because of the network is largely unconstrained. We acknowledge that NGGT has some important investment/decommissioning decisions to make about how it complies with the Industrial Emissions Directive (IED) while preserving network flexibility. Is there any link between the proposed GTCR reform and the adaptation of the network to the IED and the demand for flexibility? Unless there are large, discernible benefits for the future NGGT investment budget, the expected benefits of the proposed GTCR reform for UK consumers would appear to be minimal.

**Gas day change and enforced short-term capacity booking**. Unwelcome though it may be, the GB market will have to operate with two different gas days from 1 October 2015 at most of the terminals bringing UKCS-produced gas to the NTS. We estimate that in 2015 these terminals will be responsible for 25-30 bcm of gas flowing into the NTS. The industry is seeking to develop new commercial and legal arrangements and a scaling option (Option A) to mitigate the impact of two different gas days. If Option A is implemented, shippers' NTS allocations will be routinely adjusted retrospectively both up and down. This will require entry shippers to hold a higher level of bookings in order to accommodate these scaling adjustments. In effect, this will require them to over-book entry capacity at 6am-6am terminals, which will represent a new, unrecoverable, deadweight cost. We think that the proposed GTCR reform highlights the need for Ofgem to engage in the gas day issue as a matter of urgency.

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