Impact Assessment of UNC Mods 501V, 501AV, 501BV and 501CV 'Treatment of Existing Entry Capacity Rights at the Bacton ASEP to comply with EU Capacity Regulations

Submission of Oil & Gas UK

Oil & Gas UK, the upstream industry association, is pleased to respond to Ofgem's Impact Assessment dated 20 May 2015

We believe that the Impact Assessment is not an adequate basis for decision-making since it does not address the key economic issues which underlie the split of entry capacity at Bacton. Neither does it adequately distinguish the four Mod proposals in a way which could serve a basis for a final decision on the four options.

Capacity return option. A capacity return option should be an essential feature of any Mod approved to address the treatment of existing entry capacity rights at Bacton. Only a return option can provide a fair and equitable solution for holders of capacity booked before the EU CAM Network Code was adopted, or even discussed. Without a capacity return option, a single Bacton product with flexibility would be replaced by two separate products without any flexibility or fungibility, as Ofgem itself has already acknowledged. We continue to believe that 501AV and 501CV offer the most attractive options due to be re-considered by the Mod Panel and by Ofgem.

MER UK. As we pointed out in earlier submissions, Bacton entry capacity reform presents a number of problems for gas producers in the Southern North Sea (SNS) and future offshore development projects. There is no reference in the IA to the wishes or behaviour of existing and future SNS GAS producers in booking entry capcity. Following the passage of the Infrastructure Act 2015, the Oil and Gas Authority (OGA) has an obligation to ensure the maximum economic recovery of UK oil and gas resources (MER UK). In our view, the preference in the allocation of Bacton capacity to interconnector flows rather than UKCS production runs counter to the principles of MER UK. The split of Bacton capacity may be required by EU law but Ofgem's approval of one of the four options should take account of the principles of MER UK and seek to mitigate the potential adverse impact on future SNS gas production.

The SNS is the most mature sector in the UK Continental Shelf and, in some respects, the most vulnerable to the risks of premature decommissioning and a loss of investor confidence identified by the OGA. According to DECC, the SNS still contains >200 bcm of 2P gas reserves and >100 bcm of potential and yet-to-find gas. We believe that Ofgem's decisions which affect UKCS producers' access to NTS entry capacity should not in future years become a barrier to future resource development.

Quantitative cost assessment. The basis of the comparison of the four Mods is expressed entirely in terms of the expected effect on the TO commodity charge for all GB shippers under different assumptions about the return of existing capacity bookings. This does not satisfactorily capture all the expected quantitative impacts expected from the four options. It is also rather odd to express the results in terms of a charge which Ofgem itself expects will disappear from the GB charging regime.

The costs of the three Mods which incorporate a capacity return option are quite properly a matter of concern for Ofgem. However, in Ofgem's own analysis, the simplistic assessment shows an overall impact (0.8% to 2.8%), based on 100% capacity return, which is negligible for network users and consumers and barely significant in adjudicating between the three options. Furthermore, the assessed impact on the TO commodity charge is small in comparison with some of the variations that have been occurred in recent years. In short, the methodology does not provide a basis for decision-making, partly because it does not incorporate the qualitative impacts of the options.

Market competition. Ofgem translates the assessed impact on the TO commodity charge into an expected impact on competition without any reference to the factors which influence wholesale market participation and competition. There is no evidence provided to support the claim that a very small increase in the TO commodity charge (or its replacement charge in future years) will have an adverse effect on wholesale market competition. In our view, there are far more important factors affecting market competition than the level of the TO commodity charge.

Value of flexibility. There is insufficient attention given in the IA to the value of flexibility at Bacton, which is addressed explicitly by 501CV. The IA acknowledges the benefits of the aggregate overrun plus rebate mechanism included in 501CV but regrettably it does not present a sufficiently detailed or robust assessment of both the costs and benefits of this option.

It is with regret that we conclude that the IA does not provide a suitable basis for decision-making and that further quantitative and qualitative analysis will needed to be conducted and considered by Ofgem before it makes its final decision.

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Oil & Gas UK, 17 June 2015