

INDUSTRIAL GAS PRICES

ACTION POINTS FROM THE GAS PRICES WORKING GROUP

INTRODUCTION

Over the past two years, gas supplies into the GB market have tightened, contributing to substantial rises in the prices of both gas and, consequently, electricity. The price differential with the Continent for wholesale gas is also significant. In response to concerns from industrial users, the DTI established a Gas Prices Working Group (GPWG), with EIUG in January 2005. In addition, officials from Ofgem and Treasury were asked to attend to give advice and support. The DTI and EIUG have identified a number of key issues and conclusions:

- Recognition of the potentially very serious implications of current prices for UK competitiveness and continued viability of some industrial operations;
- Analysis commissioned from Global Insight which concluded that forward gas markets are functionally liquid but more should be done to build confidence and increase liquidity;
- A potential for distortive interactions between the UK's liberalised market with the less liberalised markets on the Continent, and the urgent need for rapid progress towards full liberalisation and effective market arrangements in Continental markets in order to remove such distortion;
- New import projects that help ease market tightness are expected to reduce upward pressure on prices.

This Note reports the conclusions arising from the Group's work, including the report on the forward gas market by independent consultant Global Insight, and a stakeholder seminar for 40 senior players across the gas chain. As a result of the work done since January, DTI and the EIUG have agreed the following actions:

ACTION LIST

Maximise gas supplies from UKCS

North Sea gas continues to make a significant contribution, and the DTI is working with industry to maximise production. This year's licensing round attracted unprecedented levels of interest. Ministers have been in contact with the key producers operating in the North Sea to stress the importance of securing maximum flows and reliable deliveries over the winter months.

Maximise gas supplies from storage

DTI will continue to do its utmost to ensure that new UK storage projects commission on time, and is supporting the work of the Commission and the European regulators to provide non-discriminatory access rights for storage facilities across Europe.

Maximise gas supplies from imports

DTI will continue to work closely with new import projects (pipelines and LNG terminals) to ensure that any avoidable roadblocks in the Government's control are swept away.

Ensure interconnector import capacity is fully utilised

DTI is introducing this autumn a new licensing regime for all interconnectors (both new and existing); regulation for LNG import facilities was introduced in August 2004. Obligations will apply to interconnectors and LNG facilities to make unused capacity available to the market under the "use it or lose it" obligation. All import facilities and interconnectors will be brought under Ofgem's regulatory oversight. DTI and Ofgem have hosted a meeting to discuss the new provisions and details of these proposals with EIUG and its members.

Encourage Demand Side Response

Ofgem is urgently progressing work with the Demand Side Working Group to identify and assess any practical and/or commercial obstacles to demand side participation in the wholesale gas and electricity trading arrangements. As part of the progress made by this group, Ofgem has, on customer's request, facilitated the daily release to the market of increased storage information; sought to develop a new information webpage with National Grid ahead of this winter, sought to ensure that there is increased quality and transparency of information available to the market; and has developed together with the group and National Grid a 'Gas Balancing Alert' that will work as an effective system warning to the market by the system operator prior to any emergency. Ofgem will continue to work with the group to ensure that these measures will all be available ahead of this winter

Further improving information flows

DTI and Ofgem will monitor the provision of upstream information through the voluntary agreement with gas producers, and Ofgem will consider whether more downstream information could be provided to enable wider market transparency. In particular, as outlined above, Ofgem is progressing improved downstream transparency in its work with the Demand Side Working Group.

Confidence building arrangements for forward markets

DTI is planning, with the Futures and Options Association, a series of one-to-one meetings or a roundtable with banks, commodity traders, hedge funds etc. to identify if/why they are not directly trading on the forward market.

Reform of Gas Imbalance Charges

Ofgem has accepted a modification to the cash out arrangements in gas in the event of an emergency, the modification sharpens incentives upon shippers to avoid an emergency. These changes have been implemented and are now in place ahead of this winter

Ofgem is working together with industry as part of its Cash Out Review Group to identify areas of the gas and electricity cash out arrangements where improvements could be made ahead of winter 2006/7 to the functioning of the wholesale markets in delivering security.

Pursue energy market liberalisation in Europe

DTI will continue to use the UK Presidency to make progress on the liberalisation agenda. DTI, Ofgem and EIUG will support the Commission inquiry into gas and electricity markets in Europe by highlighting any concerns about the operation of the market, such as reported differences in contract terms and conditions for industrial consumers between the Continent and the UK.

NEXT STEPS

DTI, EIUG and Ofgem will continue to work together to deliver these actions and to discuss other possible measures for as long as it is agreed that it would be useful to do so. They will meet again in the autumn to review progress on this programme of work.

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