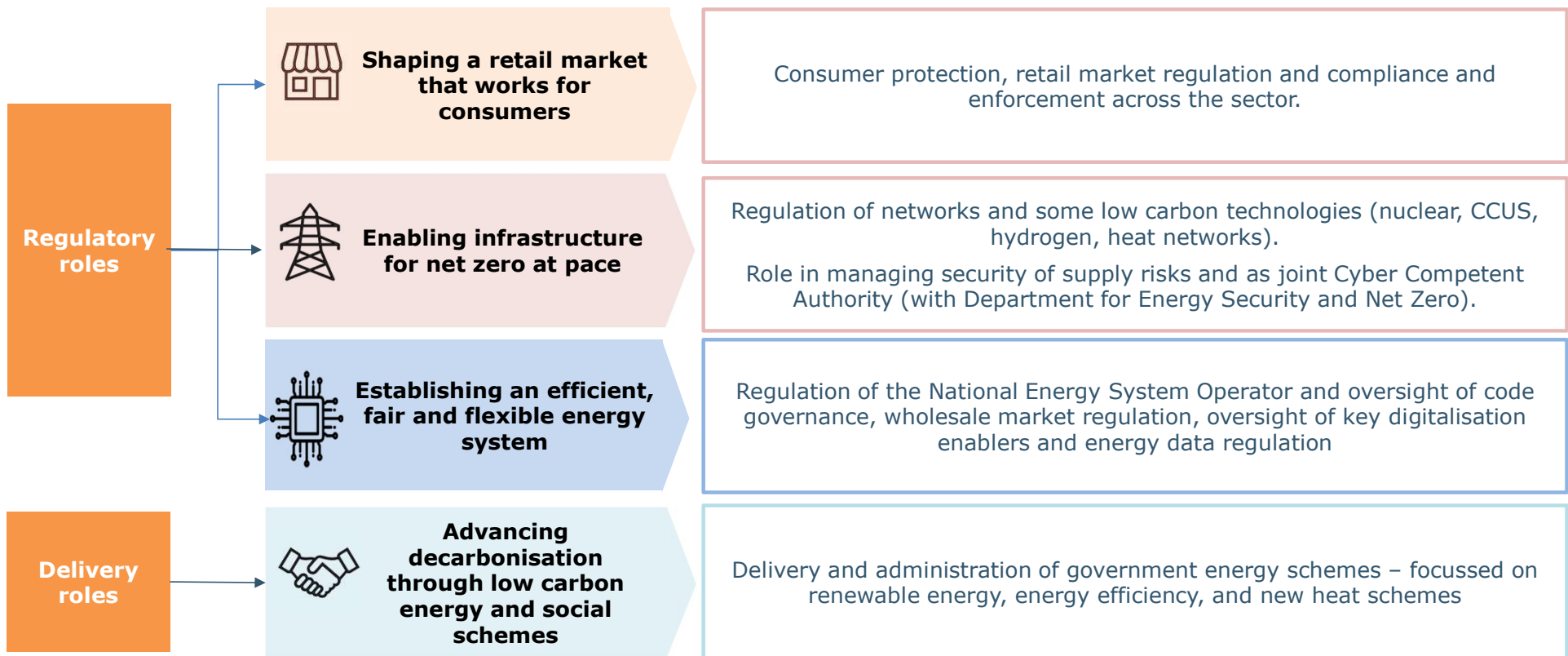




**ACCC/AER Regulatory
Conference:** Electrification
and the disruption to domestic
gas markets

2 August 2024

Ofgem is Great Britain's independent energy regulator

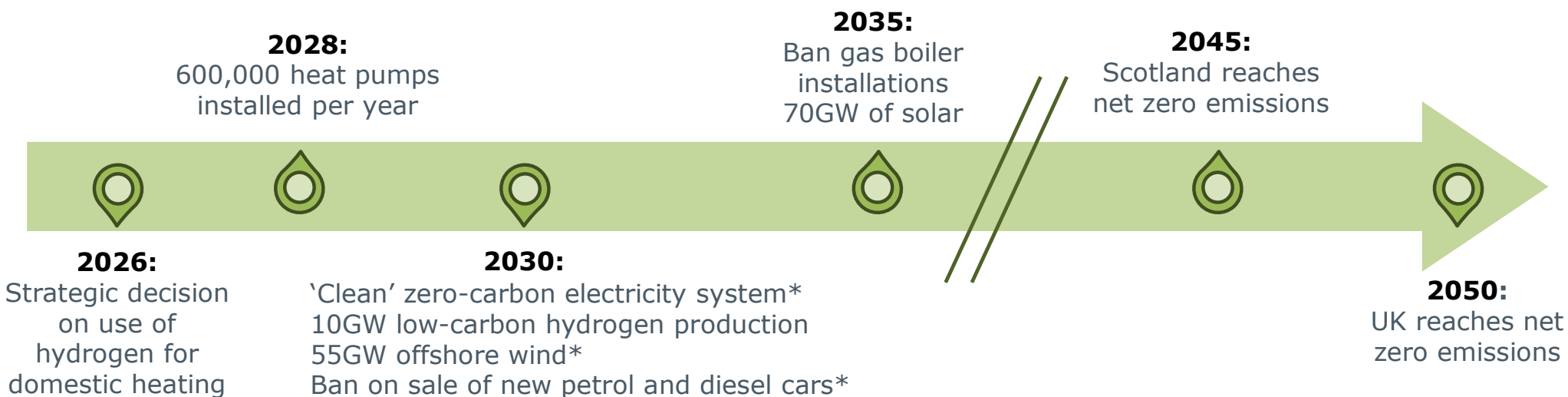


- The GB gas network is made up of ~285,000km of pipes
- The **gas transmission network** is owned and operated by National Gas Transmission (NGT)
 - NGT is also the System Operator - balancing supply and demand, maintaining system pressures, ensuring gas quality standards
- There are 8 **Gas Distribution Networks (GDNs)**, owned by 4 companies
 - GDNs operate and maintain their networks and provide a 24-hour gas emergency service
- **Natural gas is still an essential service** and demand is split equally between:
 - power (308 power generation sites),
 - industry (67,000 connections), and
 - residential (85%: >22m homes)



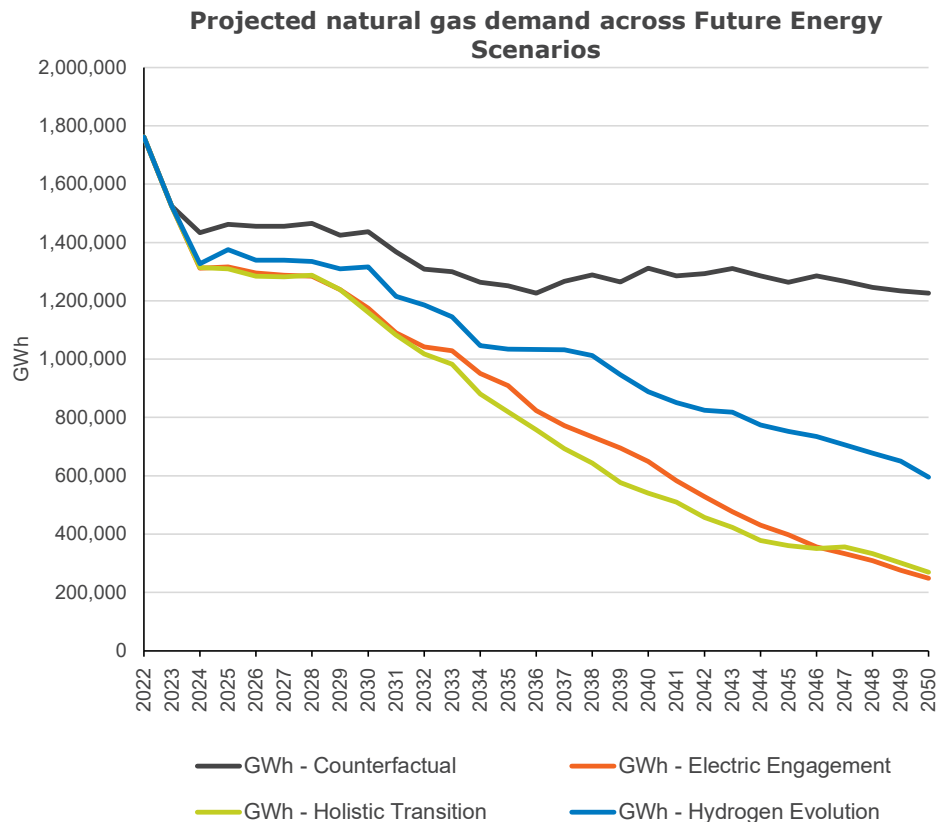
The UK has committed to bring greenhouse gas emissions to net zero by 2050

- The 2008 Climate Change Act committed the UK to reducing greenhouse gas emissions by 80% by 2050 compared to 1990 levels
- In 2019 this was strengthened to reducing emissions to net zero by 2050
- Scottish government has set a target for Scotland to reach net zero by 2045



*Commitment from new Labour government which was elected on 5th July 2024

We expect natural gas demand to decrease to meet net zero...



...but we don't expect changes to the size of the gas networks until the mid-2030s

- The impact of falling gas demand on gas networks is uncertain and will be affected by:
 - how much network is retained, repurposed or decommissioned
 - the scale and pace of change
- This is dependent on future government decisions on hydrogen use
- Some gas network will be retained up to 2050 (and potentially beyond)

...and it's vital that the gas network remains safe and resilient while it is still in use

The uncertain future of gas generates strategic questions for setting the gas networks' next price control (RIIO-3), running from 2026-2031

Issue:

Uncertainty around the future use of the gas network impacts our ability to plan what investment is required

Uncertainty around potential future decommissioning – could lead to significant costs from mid-2030s but not clear who should pay

How to recover investment from a declining number of customers through depreciation charges on gas bills

Our approach:

- No upfront funding where need is unclear, e.g. hydrogen for heat
- No funding to repurpose assets for industrial hydrogen – this will be part of a separate hydrogen business model
- Uncertainty mechanisms allow the funding to flex once need is clear
- Continue funding to maintain the network and meet safety requirements

- No upfront funding for potential future decommissioning activities
- Fund projects looking to reduce future decommissioning costs
- Work with government to develop a strategy for how to plan and pay for potential future decommissioning

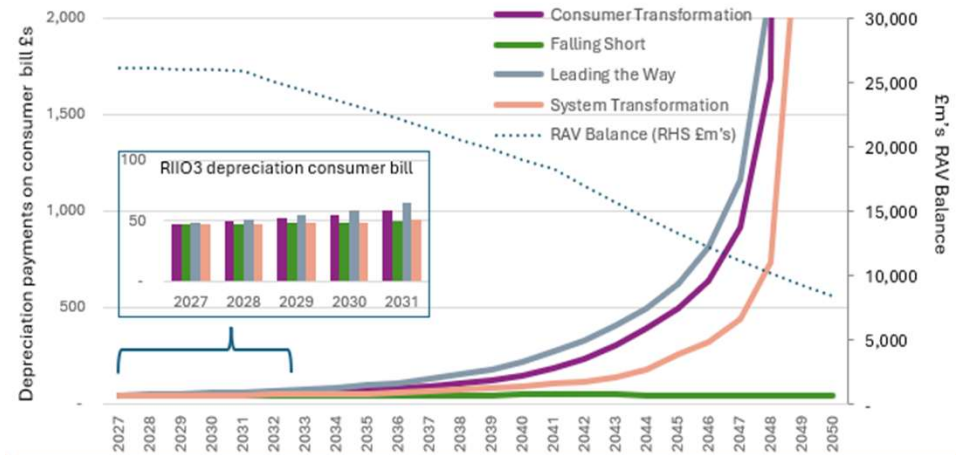
- Accelerate how quickly this investment is paid back and target repaying the investment by 2050 for gas distribution
- Ensure our approach is adaptable to changes in government policy
- Work with government to consider whether further intervention is required

Future gas consumers are likely to face rising network costs as a declining user base is left repaying the largely fixed cost of historical network investment

This creates risks which we need to address to protect consumers:

- 1. Consumer impact and intergenerational fairness risk** - depreciation payments could increase rapidly in 2030s
- 2. Perceived asset stranding risk** - without intervention there will be ~£8bn of outstanding gas distribution investment in 2050 (dotted line)
- 3. Financeability risk** - uncertainty of RAV repayment could damage investor confidence

Indicative analysis of the existing GD depreciation policy using Future Energy Scenarios (2023)



We will develop options to implement our decision to accelerate depreciation this year, considering:

1. Impact on consumer bills during RII0-3

2. Consumer bills over time

3. Perceived asset stranding risk

4. The impact on company financing

Ofgem is the Office of Gas and Electricity Markets. We are a non-ministerial government department and an independent National Regulatory Authority, recognised by EU Directives. Our role is to protect consumers now and in the future by working to deliver a greener, fairer energy system.

We do this by:

- **working with Government, industry and consumer groups to deliver a net zero economy at the lowest cost to consumers.**
- **stamping out sharp and bad practice, ensuring fair treatment for all consumers, especially the vulnerable.**
- **enabling competition and innovation, which drives down prices and results in new products and services for consumers.**