

National Grid Transco

Potential Sale of Gas Distribution Businesses
Regulatory Impact Assessment
Interruption Arrangements

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We are grateful for the opportunity to respond to this consultation. The document covers an area of importance to Corus as we are a major user of natural gas with individual sites of firm and interruptible supply status.

Overview:

In our reply to Ofgem's initial DN Sale Impact Assessment (July 2003) we stressed that subsequent proposals should be in accordance with principles of good regulation, specifically those of proportionate change.

We cannot understand Ofgem's desire to introduce large scale and complex changes to the current exit regime at the same time as major structural changes resulting from the sale of DNs. We therefore question if consumers best interests are served by introducing another major reform at a time when the industry faces a profound change in structure. It would much better to make only minor unavoidable changes to effect the DN sale.

Requirement for change:

We note Ofgem's exit reform is still predicated on a number of opposing points to our own. There continues to be a major divergence between the views of I&C gas users and Ofgem on the fundamental points of cross-subsidy and discrimination.

In our view the current regime:

- a) provides a subsidy to *firm* users because of the non cost-reflective capacity:commodity split which has greater weighting to capacity, both for NTS and LDZs. Firm users also benefit from continued supply at times of high demand.
- b) fails to provide customers a choice in interruptible terms and does not make allowance for difference in risk and actual levels of interruption. We are surprised by Ofgem's view that the current discounts discriminate because they do not reflect customers costs; we believe Transco had an obligation to use a network cost-reflective basis for their transportation charges.

Current Proposals:

We are pleased to see the proposals include variations of matrix and option / fee arrangements. It has long been our view that customers would be better served by a move away from “one size fits all” services.

Unfortunately the current proposals remove choice of supply status from customers and potentially introduce a level of complexity and inflexibility which may drive a significant proportion of current interruptible users to switch their supplies to firm status. Very few end-users, we suggest, are resourced to develop or participate in complex schemes and view the purchase of gas as a non-core activity.

We understand option 2A* was not originally proposed as an unconstrained option. This model would appear to be closest to the model requested for a number of years by end users. This proposal warrants further development if:

- a) Transco publishes matrices with cost reflective charges, to be available on a non-discriminatory basis.
- b) customers can elect to participate and not have levels of interruption imposed on them. Additional complexity of interruption should not be imposed on users that do not feel they would benefit from these arrangements.

Investment Signals -v- Central Planning:

We question the wisdom of introducing further ‘market instruments’. Following implementation of entry capacity auctions, the industry has experienced years of unstable transportation costs, ever-changing recovery methodologies and volatility in the basic commodity price. Transco’s latest 10 Year Statement advises that supply forecasts are generated using well developed central planning process. This does not include signals that should have been generated from long term entry auctions.

The guiding principle for network planning is the 1 in 20 obligation. It is not clear how Ofgem’s current exit proposals interact with their proposals on offtake ? Ofgem’s preferred option on offtake included removal of the 1 in 20 obligation from DN’s. Presumably the HSE objection to removal the 1 in 20 obligation may cast doubt on the viability of Option III of the exit regime proposals ? We understand Option III assumes exit capacity should be determined by shippers assessment of customers future needs

From a consumers perspective we do have some concerns that the principles being developed here and in Ofgem’s proposals for offtake, will lead to end users having little control and input over capacity used and required from Transco’s systems.

Security of Supply / Default Arrangements:

We are concerned that any current proposals would accelerate the trend for end users to move from interruptible to firm gas supply status and may therefore have wider security of supply implications. Incentives on users to remain as interruptible are already low owing the non-cost reflective capacity: commodity split. Ofgem’s proposals do not include any default arrangements for widespread customer inertia and the resulting impact this may have on security of supply.

Cost/Benefit Analysis:

We are not convinced that the scale of benefits for any of the options, including the cost of change, warrants such fundamental reform. We have indicated some merit to elements of 'option 2A*', but we would like to have clarification on the original intent and form of this proposal and the negative NPV figure.

On a more general note, we observe that NPV values have a high subjective content and in places detail is not provided to substantiate the conclusions made.

We believe that any proper benefit analysis should describe the probability of these benefits and costs happening. Given the high degree of subjectivity of some benefits, these are likely to have the lowest probability. This is particularly true of the alleged benefit of "market signals" informing Transco investment decisions which has the biggest influence on the NPV benefits. The costs associated with implementing change are likely to have a higher degree of certainty. After taking account of these factors, we suspect that the overall nett benefits are likely to be much lower than represented and insufficient to warrant the risk and disturbance of change.