



**Proposed Incentive Arrangements for the Provision of entry capacity at
Milford Haven
Comments by Association of Electricity Producers**

12 May 2006

The Association¹ welcomes the opportunity to provide comments on this consultation.

We provide comments against each of the questions

Question 1: should new incentive arrangements for NG NTS be developed in relation to the delivery of gas transmission capacity at Milford Haven?

We agree that it would be appropriate to introduce new incentive arrangements otherwise under the existing arrangements if the cap were to be breached then incentives on NG would be diminished and customers would bear the cost of late delivery. It is also the case that late delivery of this capacity could have wider reaching impacts on security of supply and gas prices in winter 07/08. NG would not be exposed to increased gas costs, except to a small extent through the incentives relating to shrinkage costs whilst shippers and customers would bear these costs.

Question 2: are the principles identified in paragraph 4.3 an appropriate basis for new incentive arrangements?

We broadly agree with these principles and consider that it is important that capacity is delivered in a timescale consistent with contractual commitments. It is appropriate that NG should face some of the costs arising from its own actions where this leads to late delivery and that consumers should be protected from these costs. We also agree that compensation above the level of a simple refund of transportation charges could be the right course of action in some circumstances, but that if this were to be the case then similar compensation should be considered at other locations and at exit to avoid undue discrimination, where NG fails to provide the contracted capacity.

Question 3: should NG NTS's exposure to buyback costs be deferred if there are undue delays due to consents for the construction of the reinforcement pipelines, adverse weather conditions or other exceptional factors?

¹ The Association of Electricity Producers is the UK trade association representing electricity generators. It has some 90 members ranging from small firms to large, well-known PLCs. Between them they represent at least 90 per cent of the transmission connected generating capacity and they embrace nearly every generating technology used in the UK.

Whilst we accept it is not reasonable to incentivise parties to perform when they do not have full control over all the factors affecting their performance. It is also appropriate to question whether the actions of the party could influence these other factors. So for example in this case it appears that obtaining consents is a critical step, so why did the gathering of 12 months data for the environmental impact assessment not begin earlier than summer 05? Even if there was uncertainty over the route prior to this might it not have been more efficient to begin the data gathering exercise covering a range of possibilities?

Similarly the interaction of the TBE and auction process needs to be considered, there seems to have been awareness of LNG development at Milford Haven in 2002/3 but uncertainty over the volume and timing. Clearer signals of the volume of capacity only came following the auctions in September and December 2004. At the time the shippers would have expected delivery in October 2007, but this now seems at risk. We note that a pre-works agreement was entered into by NG and the terminal developers, but before NG's exposure to buyback costs is relaxed consideration must be given to whether all reasonable steps were taken at the early stages of the project rather than just the latter stages when the risk of delay increased.

Question 4: what are the advantages and disadvantages of the new incentive arrangements described in this chapter?

The main advantage of these incentive arrangements is to protect consumers from some of the costs that they could face if such incentives were not introduced, and to provide strong incentives on NG to deliver capacity on time.

The Association does not have a strong view as to which option is most appropriate but considers that monthly caps may provide stronger incentives than quarterly ones which could be 'used up' early in the period. We also consider that there might be scope for rolling forward any unused cap in a month to subsequent months.

It will also be necessary for Ofgem to closely monitor NG's buyback actions so that it is only buying back capacity for gas which would otherwise have flowed rather than 'empty' capacity.

Question 5: Should this deferral 'skip' the period November – February during which construction is not practical?

The document simply states that construction during the winter period causes difficulties but little information is provided to substantiate this. While we can understand that deep frozen ground or water-logging might be problematic, it appears overly generous to assume that no work is possible during this time. Surely work plans can be designed which mean the areas which might cause most difficulty are completed in the summer months? We therefore do not agree that any deferral should simply skip the winter months.

Question 6: what are the advantages and disadvantages of the new incentive arrangements described in this chapter?

This is the same as question 4?

Question 7: are there further steps that should be taken to encourage NG NTS and the relevant shippers to enter into arrangements that would minimise the economic costs of any delay in the provision of transmission capacity at Milford Haven?

It is difficult to envisage any further regulatory steps which could be taken without adding complexity and regulatory intervention. It would be more appropriate to allow parties to make commercial decisions and monitor these actions consistent with Ofgem's regulatory powers and role under the Competition Act.