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Initial thoughts on the reform of interruption arrangements on gas distribution networks

Dear Joanna

EDF Energy welcomes the opportunity to respond to Ofgem's initial thoughts on the reform of interruption arrangements on the gas Distribution Networks (DNs). EDF Energy has only one interruptible customer on a DN, namely Greenwich Power Station, which is classed as a Network Sensitive Load (NSL) due to its location within the London area.

We understand the need for reform now that the sale by National Grid of four of its eight DNs has changed the competitive and operational nature of the DNs. However, we also believe that much work and analysis is needed to understand the level of impact that this model, designed by the DNs, will have.

The current system was designed by Transco to ensure that it had sufficient interruptible capacity to ensure the safe running of the system 320 days of the year - hence the 45 days interruption duration. The fact that this interruption capability has hardly been used is not so much a reflection of the improper functioning of this system but the fact that fortunately it has never been needed due to mild winters and customers and NG having managed the system and demand so well. It could be argued that the current interruption regime has saved the industry millions in reinforcement costs as the costs to customers from not being able to interrupt in a severe winter are likely to far outweigh any inefficiencies found in the current regime .

We believe that the current system does provide customers with choice and is relatively inexpensive but agree that it is not efficiently priced as interruptible customers have rarely suffered any downside from being interrupted. We therefore welcome Ofgem's consultation on this topic and hope that in the next consultation phase there is more detail to be able to fully evaluate the pros and cons of the DN's proposals.

We have answered your questions in the order that they are presented in your consultation and hope that you find our views useful. Please contact me on the number below should you wish to discuss any point in this response further.

Yours sincerely

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Appendix 1

Chapter 1

Question 1: Has Ofgem identified the key weaknesses of the current interruption arrangements for GDNs?

We believe that Ofgem has identified some of the weaknesses of the current regime but we also recognize that some of these weaknesses are also strengths which must not be ignored. For example, the choice of being firm or interruptible was a key objective when the regime was originally developed as the risks/rewards for a customer of being interrupted were clear. Customers will no longer have these choices with universal firm arrangements even though they are willing to be interrupted as they have backup fuels on site. Changes to this regime will affect customers when deciding to build extra backup facilities on site during the design phase of a project.

The level of choice under the current regime seems appropriate but it is perhaps the opportunity cost calculation which needs to be analysed as we agree the 100% discount on firm charges may not be the right level of discount. We agree though that the current level of interruptible products may be too limited and may prevent customers offering different levels of interruption. We also recognize that DNs may not have the same level of choice in offering or declining interruptible capacity requests.

The current regime also acts as a clear and transparent safety net for the industry in a 1 in 20 or 1 in 50 winter during a stage 1 emergency. It is not clear from Ofgem's analysis how this safety net will be replaced in the new regime and how the same level of security can be replaced at the same cost. This type of analysis is necessary so that DNs are aware of their 1 in 50 obligations to ensure capacity is made available to all, and could lead to significant over investment by the DNs, whose costs are ultimately passed onto customers. The UK is currently facing its tightest winters to date and it will be a shame if we are changing the current interruptible regime at a time when it is most needed to protect UK customers. EDF Energy would like to know how the same level of security will be made available to the industry under this new regime, and at what cost, as it is not evident from reading Ofgem's document.

Question 2: To what extent do interested parties consider the current arrangements have significant strengths, and if so, what are these strengths?

As stated above, we believe the current system is transparent, economic and easy to understand and operate whilst providing an acceptable and efficient level of customer choice and safety. However, we recognize they may not be the optimum level and thus we would welcome Ofgem's analysis to show which parts of the current regime could be improved upon and to what extent.

In terms of the level of interruption that could be accessed in a stage 1 emergency it would be useful if Ofgem could state in their IA how this level of system support could be replaced and at what cost.

Question 3: Do you agree with Ofgem's key principles for reform?

We understand Ofgem's key principles for reform but it is difficult to assess with the current level of detail if they will outweigh any benefits to be gained from moving radically away from current arrangements. In theory, Ofgem's reform makes economic sense but it remains to be seen whether these reforms will just generate more cost and complexity for customers, as it appears the sale of the DNs has had on systems operations and management. For example, it has been noted by several industry participants that errors in the area of demand forecasting, where some Independent DNs have actually deviated from the agreed and proven model of forecasting their own demand, has caused NGG's forecasts to deteriorate significantly at a cost to shippers, suppliers and ultimately consumers. EDF Energy would not want to a deterioration of services provided by the DN's through this regime change but we recognize that Ofgem will be policing the new regime closely if it is implemented to ensure parties are not manipulating it.

Chapter 2 Implementing reform

Question 1: To what extent do respondents consider that the model so far developed by the GDNs meets Ofgem's principles for reform?

We believe the model goes a long way to meeting Ofgem's principles for reform as they are similar in nature to the reforms proposed during the sale of NG's DNs. The model will provide 3 years of investment signals which should be enough to undertaken necessary investment and consider the risk of buying back capacity. However, it is difficult to say whether this model will work in practice without the detail as Ofgem itself recognizes in paragraph 3.10.

Question 2: Has Ofgem identified all the key interactions with the enduring offtake reforms for the NTS?

We believe Ofgem has covered the main issues relating to the interaction with the NTS enduring exit reform and agree that the sequencing of purchases by DN connects is of paramount importance to understand how much NTS capacity needs to be acquired. However, we disagree with the sequencing proposed in paragraph 3.7. A start date of mid-2007 for DN capacity purchases will conflict with a start date of summer 2007 as per Ofgem's latest

Transmission Price Control document.[1] The DN commitment would have to start earlier than the NTS offerings so that the DNs will know how much to bid for in any NTS auctions. We would recommend no less than 6 months space in between both offerings so that all parties had a chance to evaluate how the purchases went and formulate a strategy for the next round of NTS capacity offerings.

Finally, we find it interesting that Ofgem recognizes that different capacity arrangements between NTS and DNs are acceptable due to their distinct difference in scale and operation. We would hope that Ofgem uses this same rationale when designing NTS offtake arrangements for the DNs and Direct Connects (DCs) which are even more dissimilar in scale and operation.

[1] Ofgem's Transmission Price Control Review – Initial Proposals, 26th June 2006, paragraph 1.13

Chapter 4 Incentives for the GDNs in the next price control

Question 1: What is the appropriate form of an incentive on GDNs for the purchasing of interruption?

It is not clear from the level of detail provided what level of incentives should underpin these new arrangements but we agree with Ofgem that it would be appropriate to set a caps collars and risk sharing factors outside the overall RPI-X price control.

We agree that the Network Sensitive Loads (NSLs) will have some market power as they are selected by DNs to be interruptible to relieve constraints locally but believe it appropriate that these loads are offered a higher level of discount compared to non NSLs. Where they do not accept the level of discount provided NSL's should have the right to go firm and then sell back capacity when needed by the DN.

Question 2: Do respondents support the continuation of a similar incentive to the transitional incentive for GDNs purchasing of NTS offtake capacity?

We agree with Ofgem's concern regarding the scope of the transitional incentive not applying to short term purchases of NTS offtake capacity and believe both long-term and short-term purchases should be included to ensure DNs make efficient trade-offs between short and long-term purchases.

Appendix 2 – Impact Assessment information request

EDF Energy is a supplier of gas and electricity to over 5 million customers in the UK. However, at present we have very few I&C customers on the DNs which will be able to participate in individual capacity requests or become interruptible other than Greenwich Power Station. This offtake is designated as a NSL due to its location within the London area and thus we would hope that it continued to enjoy a discounted rate for being interruptible. It is important that where the site, or other NSLs, do not agree to the discount provided then it should have the right to go firm just like any other DN offtake. The DNs would then have to contract for the necessary amount of buyback or interruptible capacity.

It is difficult to ascertain the level of financial and operational impact from the level of detail provided in the consultation. However, we do not anticipate a large cost impact from the introduction of these reforms, compared to the more radical changes to the NTS Enduring Exit regime, other than changes to systems and procedures to incorporate the purchasing of capacity every year.