



Mark Feather
Associate Director, Industry Codes
& Licensing
Office of Gas & Electricity Markets
9 Millbank
London
SW1P 3GE

Centrica Energy

Millstream East
Maidenhead Road
Windsor
Berkshire
SL4 5GD

Tel. (01753) 431242
Fax (01753) 431150

Our Ref.
Your Ref.

6 March 2007

Dear Mark,

**Transmission Price Control Review – Offtake Arrangements:
Impact Assessment on Modification Proposals, February 2007**

Thank you for the opportunity to comment on the Impact Assessment on the Modification proposal and Alternates relating to the Enduring Offtake Arrangements.

Given below are the views expressed on behalf of the various group companies of Centrica plc involved in the use of the Gas and Electricity Transmission networks, but excluding Centrica Storage Ltd.

Quantitative Analysis

There are a number of areas within the Quantitative Analysis where figures submitted by Users and those within the Gas Forum submission, prepared by NERA, are challenged and then amended, if not discounted without adequate explanation. Although we concede that there will inevitably be differences in interpretation, we believe that a number of these challenges may be unfounded. There is a more detailed paper, again prepared by NERA, that covers the individual issues in more detail and which has been submitted on behalf of Gas Forum members. We do not wish to replicate the points made in that document in this response but we are broadly supportive of the content.

It is our observation that although the same pattern of relative net benefit emerges from the NERA work, the differential net benefit between the various alternate proposals is even more marked than that identified within the IA.

Page 1

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www.gas.co.uk

Non-discriminatory allocation of Capacity products

We challenge the assumption that any benefits from the non-discriminatory allocation of exit capacity products would be equally distributed between Flat capacity and Flexibility. Our view is that very little benefit would be accrued by non-discriminatory allocation of flexibility until such time as there is genuine scarcity and thus an objective justification for a market-based rationing mechanism. We have clearly stated, and demonstrated by proposing Modification 0116CVV, that this situation does not apply currently. The proposal includes the requirement to monitor the situation to establish whether that were to be the case.

In these circumstances we believe that a much smaller proportion (<10%) of any benefit should be allocated to the flexibility product. This would reduce the differential between the benefits of the various Modifications to circa £1m (Table 3.6).

Qualitative Analysis

Our observation is that much of the Qualitative Analysis is concentrated upon areas where there is little or no quantitative measure available. We recognise the value of the more subjective judgement on issues of this nature but would argue that this should not outweigh the Quantitative benefits unless there is an overwhelming *prima facie* case for doing so.

There are a number of sections within the Qualitative analysis:-

- efficient network development and system operation;

We are of the view that any benefit to network development and system operation would be extremely limited. In respect of new connections, the existing Advance Reservation of Capacity Arrangement (ARCA) process enables financial commitment to capacity, in support of the planning process conducted by National Grid in addition to the requirements upon the developer for planning and consents. The alternative proposal 0116CVV would provide the enhanced level of commitment if this were deemed a necessity. With respect to Flexibility, we are assured by the Transporter that no investment would be carried out specifically to provide additional Flexibility. Therefore there appears to be no benefit, in terms of network development, of a Flexibility product. Similarly, there is no system operation requirement for a long-term Flexibility product. Available Flexibility is very much driven by actual gas flows and system configuration which, by definition, is a short term process. Alternative Proposal 0116CVV would provide for the monitoring of Flexibility use and signal any requirement for more rigorous rationing.

- promotion of competition;

We also challenge the assertion that competition would be promoted by this Proposal. As Flat Capacity is allocated at a nodal level there is no scope for competition between Users or end consumers. The comments above, on network development, address the need to signal incremental requirements. Although it is proposed that Flexibility is allocated on a zonal basis where there would be multiple parties at the zone, there is no mechanism to identify co-incident use of flexibility. It is current experience, as is asserted within proposal 0116CVV, that there is sufficient flexibility within the existing system to cater for all

foreseeable requirements. This is confirmed by the Transporter on the basis of current experience. We strongly hold the view that any requirement to anticipate the level of flexibility that MAY be required in the distant future would simply create an artificial scarcity, inevitably leading to higher costs which will ultimately be borne by consumers. We concur with the view that the increase in complexity necessary for a full Capacity and Flexibility regime may serve as a barrier to new entrants to the market.

- appropriate allocation of risk;

We would agree that the introduction of User Commitment does serve to underpin the existing planning process in terms of capacity. This may have some effect in reducing the number of ARCA disputes but our understanding is that these are infrequent occurrences; therefore this benefit is small. In contrast the introduction of a rationing mechanism for flexibility in the long term, when requirements are by definition uncertain, does serve to increase the risk borne by Users and their customers with little or no benefit.

- simplicity and transparency;

Although it may be the case that there is a Qualitative view of the benefits of these proposals in terms of simplicity and transparency, any change in complexity will be reflected quantitatively. It is accepted that the benefit arising from Flexibility will be is very difficult to quantify at this stage. It is our view that greater transparency would be provided with proposal 0116CVV, in that there would be routine reporting of flexibility use, even where a long term rationing mechanism were not in place.

- preservation of security of supply;

The area of security of supply is one where we believe that the implementation of the full Capacity and Flexibility regime may have a detrimental impact. In the event that Users and Distribution Networks are forced to compete for Flexibility that they MAY require in the long-term, this will lead to a shortage of flexibility available to match ACTUAL requirements in the short-term. This could lead to some consumers, particularly power generators, operating their facility sub-optimally in the absence of available flexibility.

- preventing undue discrimination.

You will be well aware that there has been a long debate within the industry on the matter of differential conditions for classes of connectee and whether this constitutes discrimination. It continues to be our view that the service offered to classes of connectee does not need to be identical as long as there are sound reasons for doing so. Therefore, whilst we are of course entirely supportive of measures to prevent undue discrimination, we believe that in some areas differential products may be appropriate. We note in passing that significant differences in gas supply conditions exist between different classes of customer, without it being suggested that there is undue discrimination.

In summary, we are of the view that the Quantitative analysis of your Impact Assessment clearly demonstrates that Alternative Proposal 0116CVV is that which provides the maximum benefit to the industry as a whole and, in our view, best meets the relevant objectives. The scale of this advantage is the subject of some dispute. As we have stated

above and as contained in the NERA paper this advantage could be more significant that is evidenced by your analysis.

Much of the case contained in the qualitative analysis is related to the benefit of a Flexibility regime. In addition to our specific challenge to view of this benefit within the Impact Assessment, we also revert to the basis of our Alternative Proposal in that there is no requirement at present for this level of complexity to ration a product that is not in short supply. We are firmly of the view that a period of monitoring of flexibility use would clearly resolve the matter of whether more complex solutions are required in the longer-term.

Please contact me if you require any further information.

Yours sincerely,

Mike Young
Commercial Manager