

26<sup>th</sup> November 2007



John McNamara  
Ofgem  
9 Millbank  
London SW1P 3GE

Dear John,

**Re: DNPC03 - LDZ System Charges Capacity Commodity Split and Interruptible Discounts - Draft Impact Assessment**

Corona Energy ("Corona") wishes to submit the following in response to the above consultation.

Corona responded to DNPC03 stating that it was unconvinced by the evidence by the DNs to inform the proposed split of charges. In that response we identified cost categories which do not necessarily lend themselves for recovery via capacity charges. We note that Ofgem concurs with this view stating that the data provided in the consultation proposal *"does not appear to support the assertion, on which the proposal is based, that 95% of Use of System costs are directly related to system capacity."* That said, Ofgem does conclude that 95% of costs appear to be unaffected by system throughput, albeit on an average cost basis. Although Corona has reservations over this observation based on the data presented by the DN's, we are willing to accept this shift for the purposes of achieving the wider benefits associated with price stability and predictability.

We wish to make it clear, however, that although we accept the shift in the balance of charges, for reasons stated above, it can be stated without any ambiguity that there will be a resultant, and significant, shift in risk from the DNs to shippers/suppliers. This rebalancing in risk must be recognised and processes put in place to protect competition and minimise disruption to consumers.

Corona commented on the challenge of considering this risk in our response to the consultation paper as follows:

*"The issue of customer/supplier contracts should not be underestimated. The majority of customers in the I&C market tend to enter into annual supply contracts commencing at the start of each Gas Year. Negotiations of these contracts will start much earlier in the Calendar Year. Traditionally, smaller I&C customers have*

*resisted fixed charges and have a strong preference for volume based charges which when operated in parallel with capacity bias transportation charges will impose significant risks on those shippers operating in these markets. As a result, it is imperative that the market is provided with an appropriate period of time to consider future methodology changes so that suppliers can negotiate effectively with customers and investigate various risk mitigation tools.”*

The analysis produced by Ofgem indicated that the small I&C sector will be the most adversely impacted by the shift change. Corona does not underestimate the impacts on consumers in this regard and we are not confident that consumers will be as passive as possibly inferred in this consultation. Unlike wholesale gas prices, which are market determined, transportation charges are regulated, and any changes in such charges are less understandable. Clearly, consumers need to be engaged in this process and it will be incumbent upon the industry to educate and inform consumers of the potential longer term benefits of the proposed increases.

In order to achieve the benefits associated with the shift in the balance of charges, Corona is satisfied that an October 2008 implementation date is achievable as long as three conditions are met:

- 1) Ofgem makes a decision not to veto the proposal by no later than the end of January 2008
- 2) DNs are required to provide indicative charges for October 2008 no later than the end of February 2008
- 3) The Licence condition D11, or UNC, is strengthened to prohibit DNs making any changes to charging levels more than once a year

The first two conditions are necessary to ensure that the market is provided with sufficient time to absorb the changes and implement appropriate mechanisms to allow for; customer education, risk evaluations, contractual changes and ultimately effective competition in the supply of customers.

It is important that the market is allowed to operate rationally and this can be most effectively achieved by providing participants with sufficient time to manage change. In addition the provision of indicative charges will enhance transparency which in turn will contribute to market awareness and better functioning competition.

The third bullet recognises that through the implementation of this Proposal, DNs will experience significantly reduced levels of revenue variation. This is particularly apparent when considered in conjunction with the removal of the volume driver from the Price Control Formula. The DNs have made it very clear that the introduction of this Proposal will secure stable revenue and prices whilst recognising that the financial risk will shift to the shipper/supplier community. It seems entirely reasonable to us that if the principal justification for this change, as promoted by the DNs, is to guarantee price stability then this should be reinforced through modification of the DN Licence or potentially the UNC. Corona can see no reason for



permitting DNs the ability to make additional price changes within the Gas Year. These changes are damaging to competition and therefore damaging for customers.

We trust you find our comments useful and if you have any questions then do not hesitate to get in touch.

Yours sincerely

Ian Simpson

Head of Operations

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