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Peter Sherry
OFGEM
9 Millbank
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Tuesday, 01 March 2011

Dear Peter,

RE: Gas Significant Code Review Process - Security of Supply

Further to our conversation with you, we would like to take this opportunity to provide some written feedback on the proposals being discussed.

We are very much in favour of a discussion around Security of Supply. We have long felt that in the case of a Gas Deficit Emergency (GDE), Industrial and Commercial (I&C) users bear the risk and cost of firm load shedding to protect the supply of others. Whilst we appreciate that such an event is 'low probability', it must be acknowledged that it would be 'high impact', so we welcome OFGEM's review of the matter. Following the changes to the DN Interruption Regime under modification 90 of the Uniform Network Code (UNC), we have felt that a step backwards was taken for UK security of supply. Our fear is that many I&C consumers may well have decided, as their supply was changed to 'firm' from October 2011 onwards, that there was no longer such a requirement to maintain backup equipment. In addition, the reduced charges that helped to cover the cost of such equipment will no longer be there to support it.

Much of the discussion so far has centred on some of the technical aspects of the emergency processes, e.g. Value of Lost Load (VoLL) and the merits of dynamic or frozen cash-out and these are certainly important parts of the whole solution. We would, however, like to provide some feedback on more practical elements of the discussion, in which we have greater experience.

As an I&C consumer, we maintain backup equipment in order to minimise the likelihood of disruption to our process by commodity or network emergencies. There is a significant cost to maintaining this ability. Not only do we continue to make substantial investment in renewing our backup equipment to ensure it is reliable and serviceable, but there are also the ongoing costs of repair, testing and inspection, not to mention the cash cost of holding reserve fuels. Given that we have a "firm" supply from October 2011 onwards due to the changes in the DN Interruption regime, we could take the view that we should avoid this cost by mothballing or removing this backup capability.



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If the aim of the SCR is to: a) Avoid a GDE and b) should a GDE occur, get out of it as quickly as possible, it would seem wise to incentivise I&C consumers to retain this capability. In order to do that, it must be recognised that the method of providing any compensation should take into account that the costs are ongoing, they do not accrue only during an emergency.

Providing compensation for lost load takes into account the high value placed on security of supply, but that high value takes into account, not just the alternative fuel cost, but principally the ongoing investment required to maintain the capability to respond.

As a result, it would be beneficial for any compensation arrangements to allow each I&C to reflect the different balance between “option” and “exercise” costs that their own operation requires. We see this as a key part of allowing each I&C consumer to express their VoLL.

For those who are able to cease production, their costs will no doubt be weighted to “exercise”. For those who maintain backup equipment, their costs will reflect a heavier weighting on “option”, as the costs exist whether an emergency is declared or not.

Two of the options that seem to have been popular are: 1) operating an auction of demand as emergencies unfold, via a new Demand Side pre-warning and 2) securing commodity interruption as is done for DN Interruption, in advance.

With respect to 1), our concern would be the speed at which this process would have to be conducted. It would seem likely that many I&C consumers, for whom selling back gas is not a core activity, would need some time to work on a proposal and to gain approval internally. Perhaps, due to the risks and time pressure, some would opt not to be included in an ‘emergency’ auction.

Proposal 2) seems to us to have more merit, although we would make several recommendations based on our experience of the DN interruption regime.

- 1) The process of bidding for and securing interruption should be made as simple as possible.
- 2) The terms, obligations and penalties should be clear and well understood by all parties. Rather than using the UNC as the basis under which the interruption contracts are governed, the use of a simpler “contract” that clearly outlines the rights and obligations of each party would be preferred. For companies not daily dealing with the complexities of the UNC, entering into a contract for interruption that is underpinned by such a complex and unwieldy document is a high risk.
- 3) A single central party could be engaged to provide support to potential bidders, to accept and manage the bids and to notify the bidders of the outcome of the auction. This would provide uniformity of information, and should result in a higher level of knowledgeable support to the process. In the past, Suppliers have been used for this role and the level of support, knowledge, expertise and interest displayed has been, at best, variable.

We hope that our perspective proves useful to the discussion, and we await OFGEM’s draft decision document with interest

Yours sincerely



Phil Hindmoor
Purchasing Team Leader

