Ofgem Significant Code Review: *Gas Security of Supply Draft Policy Decision*

Tata Steel Response

We make brief comments on those aspects of the draft policy document which are of direct relevance to industrial consumers such as Tata Steel

For gas intensive users the 'further interventions' work is the key dimension of the SCR process. We understand this train of work will commence after an updated appraisal of risks facing the GB and global gas market.

Ideally, the two streams of work would have been developed in parallel and measured as one package. For that reason we can give qualified support to Ofgem's draft policy decision (Option 4) on the basis that the cash-out reform and domestic VoLL provides a framework for compensating firm load shedding of industry.

We doubt nonetheless that amended cash-out as a standalone measure could materially improve long term energy security. It has not been demonstrated, beyond the theoretical, that current cash out arrangements are discouraging suppliers from taking steps to insure against supply disruption. Therefore of greater relevance to gas intensive industry are direct measures to prevent an emergency occurring in the first place. We therefore welcome consideration of the arrangements common place in our mainland European markets such as storage obligations and System Operator (SO) contracts for 'last resort' demand side response.

Do you agree with how we have estimated Value of Load and the level of VoLL that we have used.

The true level of VoLL for industry is inconsistent and will vary with time, trade sector and product. However, in terms of representing the level of cross subsidy of industry being the insurer of last resort to smaller users and domestics, then domestic VoLL is an appropriate administrative level.

Will enhanced incentives to avoid an interruption occurring increase the number of interruptible contracts entered into by industrial consumers? Please explain why

We doubt that the price-signals alone will secure the market further as this is predicated on the supply industry developing and implementing demand side contracts. These contracts are unlikely to be given priority by Industrial & Commercial supply specialists; their physical long position and high load factor DM customers mean a lower incentive for product development than suppliers carrying the risk of supplying the NDM sector including domestics.

Unfortunately without these contracts the VoLL mechanism risks creating additional but ineffective cost smeared across industry without tangible or reliable improvement in long term security of supply.

Do you agree with our broad proposal for collection of monies from shippers and passing this through to customers? Should extended payment terms be applied to emergency cash-out?

Timing of compensation to customers is crucial where involuntary (or voluntary) demand side response has left that business unproductive. Therefore extended payment terms are not supported if this delays compensation to industry.

Do you agree with our assessment that a gap in the emergency arrangements would remain following the introduction of capped cash-out. If so, to what extent do you believe that this gap can be overcome through further interventions?

Option 2 assumes a significant degree of contractual progress on demand side response. Without significant development in this area the probability of firm load shedding for all DM users remains unchanged. For this reason further interventions work needs to be given equal weight to cash out reform.

Do you agree with the assessment of cost and benefits of the various options?

The sensitivity of Redpoint's analysis to the level of demand side contracts assumes three main tranches of VoLL across named industrial sectors. These are simplistic; even within one sector there will be different levels of VoLL dependant on capital plant, supply chain and sale terms.

Do you have a preference over specific interventions that you think might be most effective ensuring security of supply whilst minimising the risk and unintended consequences.

We have supported the potential for a SO operated last resort mechanism (interruption auctions with costs incorporated into cashout) alongside storage obligations which include essential load for a final tier of industrial plant. The last resort mechanism incorporated into a stage one scenario would allow the SO to call for reduced or limited off-take in tranches in order to limit the likelihood of the supply/demand position deteriorating further.

A number of stakeholders have suggested an auction for interruption. We outline several challenges with such an approach and are keen to hear proposals on how to overcome these.

An SO auction for the largest users (VLDMC/DMC consumers) addresses the inequity of current arrangements in that the largest users have the greater risk of 100% firm load shedding. A SO mechanism enables the largest gas users to contingency plan for a staggered gas reduction as a genuinely *last resort mechanism* whilst also receiving payment. This facility is not possible under current contingency procedures and is an important non-price related incentive.

With the inertia for demand site contracts from industrial suppliers, the SO auction provides a means of responsive contingency planning and layered compensation. The layered approach would be more acceptable to gas intensive users and their customers, could reduce both the likelihood of any emergency event developing and the impact on our capital plant.

We view this option as an easier and more attractive option for the largest most exposed industrial users of gas. The obstacles to their implementation seem to us largely bureaucratic in nature and have already been set-aside for National Grid Operating Margins.

If some kind of storage obligation was to be implemented do you favour an obligation on suppliers or shippers. Alternatively do you think the SO or government should invest in strategic storage or build storage facilities for the industry to use

Along with other gas intensive users and in common with our mainland European markets, we have concluded the UK government should establish an enhanced public storage obligation which requires utilities to hold in store a set proportion of their gas sales.

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