Non - Confidential Response

e-mail: gb.markets@ofgem.gov.uk

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Anna Barker
Senior Economist
Ofgem,
9 Millbank,
London, SW1P 3GE

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Dear Anna,

Total Gas & Power (TGP) and Total E&P UK (TEPUK) response to Ofgem's Security of Supply Significant Code Review

Thank you for providing TGP and TEPUK with the opportunity to respond to Ofgem's draft policy decision on the gas security of supply significant code review dated 08th November 2011.

Ofgem proposes to change the commercial arrangements to apply during a gas deficit emergency (GDE). In an attempt to incentivise shippers and suppliers to invest against shortage, Ofgem intends to legislate for a £20 per therm cash out price (Value of Lost Load – VoLL) that would apply to short shippers and customers that are subjected to involuntary demand side response (DSR). "Short" shippers would be cashed out at £20 per therm and interrupted customers would be compensated by this same amount. The regulator has also stated that it is likely to supplement this change with imposition of additional measures (e.g. new storage obligations, licence conditions) in due course. In our view, the proposed reforms would generate significant and disproportionate costs for market participants and may lead to unintended consequences following a GDE.

The following provides a summary of the points that we would like to make in response to this consultation.

- The market has performed well with no gas deficit emergency occurring to date. We therefore question the need for significant regulatory changes such as those proposed. Existing levels of cash-out charges for suppliers' imbalance already sufficiently encourage suppliers to procure storage, enter into long term contracts and negotiate arrangements with end consumers to enact DSR to reduce their demand at a time when the supplier or system is short of gas.

- The introduction of additional obligations would increase investment costs and therefore increase gas prices for end consumers as well as inhibit liquidity in the market. This could also lead to creation of additional barriers to entry in the market.

- New statutory or licence obligations on industry participants could distort the market or result in unintended consequences such as reduced competition. Some suppliers may be unable to meet onerous credit requirements in a market where prices could potentially rise much higher than they could do under current arrangements. This could have implications for the credit-worthiness of shippers, particularly those with smaller balance sheets. In addition, we believe that such high cash-out charges could lack credibility which could undermine their effectiveness.

- Further to the credit issue outlined above, a "short" shipper may become insolvent as a result of the Gas Deficit Emergency (GDE). Balanced or "Long" suppliers would have to make payments to their customers that were subject to involuntary DSR without sufficient funds to be paid back from "short" suppliers who may have been unable to meet the £20 VoLL cash-out penalty and become insolvent.

- Should GB be approaching a GDE then VoLL set at £20 a therm could actually make a GDE more likely if customers hold out for this payment rather than commercially interrupting through arrangements with their suppliers. In effect it serves as a reverse incentive for customers and incentivises against action that would be helpful in reducing demand under current arrangements.

- The proposals with respect to VoLL payments would not ensure that market participants will respond appropriately to price signals in order to avoid or mitigate a high impact, low probability event.

- With respect to the Post Emergency Claims (PEC) procedure, we believe that this should continue but a mechanism should be developed to provide more certainty or a guarantee to suppliers which would remove any incentive to sell gas to other markets that may offer a higher price than they would get by selling to GB, thus helping to ensure gas flowed to the GB market.

- Certain events that are outside of Shipper's control such as unplanned outage of storage facility, pipeline or interconnector should be classified as force majeure and there should be no payment to customers for involuntary DSR

- It is our view that no decision regarding cash out reform in a GDE should be taken without further analysis on the impacts, costs and benefits of the various further potential interventions. Without having an understanding of these further measures it is not possible to estimate the extent to which they would help to avert a GDE. Other alternatives could be developed and incentivised in the market such as investment in new storage, interconnection with Europe, long-term supply contracts, import diversification or DSR mechanisms— each of which could enhance security of supply and mitigate any potential need for cash out reform and the introduction of VoLL at £20 per therm. In summary the final decision for the Gas SCR should focus on further interventions so that a complete picture can be understood and commented upon by the industry.

Should you wish to discuss any of the above points please do not hesitate to contact me by email andrew.green@totalgp.com or by telephone on 01737 275 554,

Yours Sincerely

Andrew Green
Head of Regulation
Total Gas & Power
UK Energy Retail