



Anna Barker
Ofgem
9 Millbank
London
SW1P 3GE

31 January 2012

Dear Anna,

Gas Security of Supply Significant Code Review - Draft Policy Decision

Introduction

WINGAS welcomes the opportunity to comment on the draft policy decision document. We are concerned that Ofgem appears eager to press ahead with these radical proposals, but trusts that it will properly consider any counter-arguments which are forthcoming during the industry consultation phase.

WINGAS is not convinced that a robust case has been presented to justify amending the current arrangements and certainly, based on the cost-benefit analysis presented by Redpoint, it is highly dubious if the solution proposed by Ofgem will offer any benefits to UK consumers. WINGAS understands that there is a high degree of subjectivity around this area, given the lack of historical context and the low probabilistic/high impact nature of major supply events, but it is critical that fundamental changes are properly considered in terms of their impacts on market functioning.

Although WINGAS is unconvinced of the case for change, in the interests of providing constructive feedback on the proposed changes, we trust that Ofgem will consider our more detailed points in the spirit in which they are intended.

Assessment of the SCR Proposal

This section provides a summary of the key points we wish to submit in response to the main elements of the SCR proposal.

- The basic premise of the SCR proposal is that suppliers/shippers are best positioned to quantify and insure against the possibility of a GDE occurring. Ofgem has determined that the imposition of an artificial “penalty” will incentivise shippers/suppliers to enter into appropriate risk mitigation arrangements. In our opinion, we do not necessarily believe that this approach is the most appropriate nor the most cost effective for a number of reasons:
 - It assumes that suppliers/shippers are able to quantify the risk of a low probability event occurring; quantification is essential for insurance contracts
 - Even if shippers/suppliers are able to quantify the risks, some of them may elect not to seek to insure against them, because they are unable to do so at an appropriate cost.
 - The level of risk afforded to shippers/suppliers is excessive, as it does not recognise their ability to insure against them e.g. speed by which the GDE develops, FM events etc...
- We are not convinced that the proposed domestic VoLL is a rational level to be applied as compensation for the interruption of Industrial and Commercial (I&C) consumers. We do not agree with Ofgem’s assertion that the establishment of a “cap” based on the most extreme valuation of loss of supply will not compromise the ability of suppliers to contract for DSR at appropriate prices.
- WINGAS does not believe that sufficient numbers of customers will be willing to enter into DSR arrangements, at sustainable prices, with suppliers for a number of reasons. Firstly, following the reform of interruptible arrangements a number of customers which previously maintained infrastructure to support fuel switching have decommissioned the equipment as a cost saving measure. Secondly, we believe that customers may look to exploit the potential for upside and offer DSR at prices close to, or at the cap – noting that the likelihood of this occurring is directly related to the depth of the DSR market.

- On the basis that the ability of suppliers to mitigate against the exposures inherent in the proposal is likely to be limited, we do not agree that the impacts will be same for all suppliers. Larger shippers, with greater credit facilities, will not only be able to enter into more diverse demand/supply contractual arrangements, but also will be able to sustain periods of high market prices. We believe that the combined effect of an excessive VoLL and artificially high cash-out prices will undermine the market and lead to market distortion and insolvency of shippers/suppliers.
- WINGAS is perplexed by the overall approach set out by Ofgem. It would appear that Ofgem is of the view that review should be carried out in two stages; the introduction of the SCR proposals, followed by an assessment of additional intervention measures. We do not understand the logic behind this approach as it implies that the SCR proposals are necessarily independent of any additional changes. In our view, it is valid to suggest that, irrespective of the debate around the need for change, that an intervention measure alone may provide the required level of insurance. We recommend that in the event that Ofgem justifies the case for change, it suspends the SCR process and fully examines the benefits which may be accrued from introducing an intervention measure. This assessment should be done independently of the SCR proposal.

DSR arrangements

WINGAS is not adverse to the use of DSR as a means of mitigating against the occurrence of a GDE. In fact, WINGAS wishes to confirm that under the current arrangements, shippers do contract with customers to provide some degree of DSR.

In the event that Ofgem presses ahead with the SCR then we would like to set out a proposal which we believe will encourage customer participation in offering DSR services. As stated previously, we believe that a number of customers will be reluctant to voluntarily enter into DSR arrangements. Full interruption of gas consumption is not an option for many customers as the economic impact of doing so could be catastrophic – for example, this is likely to be the case for particular processing plants where complete cessation of operation can damage equipment.



WINGAS recommends that alternative firm load shedding arrangements are considered whereby customers are able to enter into partial interruption contracts with shippers/suppliers. This could be in the form of tranche style load shedding down to guaranteed levels of minimum offtake levels to protect equipment, jobs and other environmental considerations.

Rob Johnson

WINGAS UK Limited

more energy - together

Direct Line: +44 (0) 208 439 9686

Mobile: +44 (0) 7540 414 012

Fax: +44 (0) 208 439 9696

Email: robin.johnson@wingas-uk.com