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Dear Anjli

### **Gas Security of Supply Significant Code Review – Proposed Final Decision**

ESBI welcomes the opportunity to respond to Ofgem's decision on improving security of supply through the GB gas trading arrangements. However, whilst appreciating the importance of maintaining secure supplies in a future generation mix that is likely to rely on the flexible characteristics of gas-fired generation to mitigate future increased intermittency, it is still our opinion that the market will continue to appropriately deliver in times of gas shortage. Given this, we are not convinced that the Significant Code Review is necessary, and are concerned that Ofgem's proposals carry the risk of detrimental, unintended consequences. In particular we have concerns around credit requirements, the interactions with other aspects of the GB market and the impact on the Irish market.

### **ESB International**

ESB International (ESBI) brings together our worldwide generation, engineering and related services businesses.

ESBI has been a developer and operator of independent Combined Cycle Gas Turbine (CCGT) generation projects in the GB market for almost 20 years. We own, operate and trade Corby power station and developed the 850MW plant at Marchwood, which was commissioned late in 2009. We also recently reached financial close on our latest 860MW development at Carrington, which is intended to become operational in mid-2015. Additionally, we own and operate the 406MW Coolkeeragh plant in Northern Ireland, and are developing further large-scale CCGT projects at other locations across GB. To service these developments, we are an active shipper of gas across the UK with capacity bookings at various places on the GB system including at the Moffat Interconnector. This provides gas for ESB's significant generation and supply interests on the island of Ireland.

ESBI Investments is a trading name of ESB International Investments Limited.

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**Registered in Ireland No.** 137736



In addition to increasing our conventional generation fleet, we continue to grow our position in the UK wind market. Our operational and development portfolio will be around 165MW, comprising: the 24MW West Durham Wind Farm in Northern England; the 20MW Hunters Hill; and 15MW Crockagarron projects in Northern Ireland. We own and operate England's largest on-shore wind farm, at 66MW, at Fullabrook in Devon and have started construction of our 38MW Mynydd y Betws Wind Farm in South Wales. We are also active in the ocean energy sector.

### **Summary of views**

ESBI is an active shipper of gas within GB and to the island of Ireland where our parent company ESB has a large generation and supply business. Ofgem's Proposed Final Decision does not discuss the question of interconnectors and we are concerned that the impacts upon GB's neighbouring markets have not been sufficiently considered.

With firm offtake positions at Moffat serving both our domestic customers and our generation fleet, within the island of Ireland, we would be keen to have assurances that interconnectors will not be curtailed prior to larger loads. This is not explicitly mentioned in the Decision, and there is no assurance that compensation at VoLL would be provided to those prevented from taking contracted gas off the system at interconnected exit points. We believe that it is necessary to make this clear in order to prevent the accusation that Ofgem is encouraging behaviour that would benefit the GB market to the great detriment of its interconnected neighbours.

As stated in our response to the original consultation, ESBI is concerned about the credit implications of Ofgem's proposals, and we do not believe that these have been adequately addressed over the course of the SCR process. As currently proposed, the SCR will set a value of VoLL approximately twenty times as large as the highest prices seen in the wholesale market over the past six years. The significant increase in the collateral requirements of shippers that such a level of VoLL entails could, in a time of constrained financial markets, force smaller players from the market and prevent the entry of new shippers, thus decreasing competition and liquidity. In addition, these costs would have to be recovered by shippers, leading to an



increase in both the wholesale price of gas and in the cost of gas-fired generation of electricity, with a corresponding rise in the cost of energy for customers.

One of our major concerns is what appears to be the lack of interaction between concurrently running consultations and market change proposals in Ofgem and DECC. As has been highlighted by stakeholders on a number of occasions, the combination of the Gas Security of Supply SCR and DECC's current proposals for the capacity mechanism penalty in the Electricity Market Reform (EMR) could create a perverse incentive for gas-fired generation to remain on the system in a Gas Deficit Emergency (GDE).

The prevailing view is that the capacity mechanism will incorporate a penalty regime based around a discussed electricity VoLL of £10,000 per MWh minus electricity cash out; this electricity VoLL equates to £293 per therm, compared to the £20 per therm gas VoLL in Ofgem's SCR proposals. On a rough calculation, assuming 50% efficiency of gas to electricity conversion and having taken into account the payment of £20 per therm gas VoLL, gas-fired generators could be penalised up to £126.50 per therm under the capacity mechanism in the event that they do not deliver when required. This equates to £4316 per MWh. This is an extremely clear incentive to continue generating even in a time of gas shortage, and could very easily precipitate a GDE situation which need not have arisen under the current market arrangements.

The pricing of electricity VoLL above that of gas VoLL has severe implications for the safety of the gas system, yet pricing gas VoLL at a 'safety' level would have even more severe credit implications than the current proposals. The potential for negative unintended consequences due to the interplay of different proposals is therefore significant and of grave concern.

Although we understand that the paper on alternative measures is due to be released in November to tie in with the Government's EMR process, it seems somewhat perverse not to address security of supply as a whole, rather than focusing on cash-out ahead of other measures. It seems clear that Ofgem does not intend to change its plans on the SCR; however we would strongly urge that the above points are taken into account and considered holistically before any implementation takes place.



**International**  
ESBI Energy Innovation

Should you wish to discuss any of the above in more detail please do contact me using the details below.

Best wishes,

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