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Gas Security of Supply Significant Code Review – Proposed Final Decision National Grid Gas Transmission Consultation Response

Dear Tom,

Thank you for the opportunity to respond to Ofgem's Proposed Final Decision on the Gas Security of Supply Significant Code Review (SCR). This response is made on behalf of the National Grid Gas's Transmission business (NGG).

Our role as the owner and operator of the gas transmission network is to ensure the safe, economic and efficient development, operation and maintenance of the system.

NGG is supportive of the main aim of the SCR process to implement measures that reduce the potential for a National Gas Supply deficit Emergency (NGSE) to occur. An important step in minimising the risk of such an emergency occurring, and minimising the duration once such an emergency does occur, is to have clear objectives, roles and responsibilities for all Users of the System in an emergency. In addition, providing a better understanding the level of security of supply will enable Users, including demand side, to better manage these risks and, where appropriate, put alternative arrangements in place.

However, in respect of the proposed changes to cash out; while we agree with the high level principles of the Proposed Final Decision that seek to include a 'price' of firm demand interruption in the emergency cash-out calculation, we consider that even though the proposed cash-out reform may increase Shippers' exposure to the consequences of failing to have sufficient gas available to meet their contractual obligations during an emergency, these proposed measures alone will be insufficient in providing strong enough incentives for Shippers to invest in solutions and therefore are unlikely to result in additional physical gas being made available to alleviate a supply / demand deficit.

We believe further enhancements to the present Shipper obligations that require the availability of sufficient gas for extended periods of high demand would help strengthen roles and responsibilities in, and leading up to, an emergency. Such an obligation could be met through a range of tools, such as increasing supplies, storage or demand side reduction. The effectiveness of such an obligation is in some part dependent on effective monitoring; therefore, we believe that an external party should be tasked with ensuring compliance with any such obligation.

Although considered out of scope of this SCR; with the expected further increase in gas fired power station connections over the next 5 – 10 years and the associated further increasing interdependency of the gas and electricity markets, the issue of Security of Supply enhancement should be considered on a more wider basis cognisant of this interaction.

If Ofgem choose to implement their final proposals as outlined in the consultation, we believe that further minor developments of the business rules and legal text are required to fully represent the issues raised at the industry workshops.

We have outlined some additional concerns with the proposal in question 6 of the feedback questionnaire attached. If you would like to discuss any of the points raised in this response, please contact Malcolm Arthur at malcolm.arthur@nationalgrid.com (01926 654909).

Yours sincerely,



Mike Calviou
Director, Transmission Network Service

**Gas Security of Supply Significant Code Review – Proposed Final Decision
Response on behalf of National Grid Gas Transmission
Response to Feedback Questionnaire**

1. Do you have any comments about the overall process, which was adopted for this consultation?

The Gas SCR process has included all parties from the industry, and as such has had a good level of industry engagement. Industry engagement has improved throughout the process, with initial workshops having restricted attendance, with later workshops having an open invite.

The process adopted has generally followed the initial outline; however, there have been a number in delays associated with the publication of draft and final proposals. This has resulted in the process extending over a reasonably long period.

One potential improvement for future SCR initiatives is to outline up front the process for consideration and development of alternative options and how these will be addressed by Ofgem.

2. Do you have any comments about the overall tone and content of the report?

The report, as with the previous reports published as part of the process, provides a good overview of the process, Ofgem's aims, industry discussions and also the reason for Ofgem's decision.

However, the impact assessment is not clear on how the quantified evaluation has been calculated and the assumptions used. Therefore, it has been difficult to validate the outcome of the assessment.

3. Was the report easy to read and understand, could it have been better written?

Generally the main report was well written and easy to read and understand. The Impact assessment could have provided additional clarity on the methodology, and assumptions used in the quantitative and qualitative assessments.

4. To what extent did the report's conclusions provide a balanced view?

The report outlines the discussions and consultation responses from the industry. However, the report does not consider in detail some of the main issues outlined by the industry, such as the interaction with the electricity arrangements or the impact on credit arrangements.

5. To what extent did the report make reasoned recommendations for improvement?

The report provides a good outline of why Ofgem has arrived at its final proposals. However, there are a number of areas that have not been addressed e.g. current level of system security versus level of system security desired.

6. Please add any further comments?

The comments below are focused on the proposed changes outlined in the Final Proposals.

Further Interventions

Ofgem's Draft Proposals outlined a number of additional measures that may merit further development if perceived gaps within the Security of Supply arrangements continue to be evident post implementation of the proposed cash out reforms. The proposed scope of these potential 'Further Interventions' may have a considerable impact on market participants and the market in general. We believe that prior to formalising a decision on the Cashout aspect outlined within this proposal; the industry and Ofgem should be given the opportunity to better understand the interactions, and implications, Further Intervention initiatives may have when considered alongside the Cashout revisions proposed by Ofgem.

Introduction of Administered VoLL and Commercial DSR

We have concerns with the introduction of administered VoLL for non-domestic customers when firm demand is involuntarily curtailed during an emergency. We are not convinced that the introduction of an administered VoLL in isolation (of other measures) will lead to a material increase in the volume of commercial demand side response contracts. We consider that a true reflection of VoLL should be represented in individual shipper / user supply contracts and these VoLL prices submitted to the market as a potential balancing action. We believe that an administered VoLL reduces the incentive on end users and shippers to determine a meaningful VoLL price. Additionally we consider that shippers and end users should be incentivised or potentially obliged to develop supply contracts that inherently include an agreement on the applicable VoLL for that consumer. Therefore, we conclude that the implementation of an administered VoLL, during a Stage 2 Gas Deficit Emergency, is likely to require the development of additional measures to ensure a rise in volume of interruptible contracts.

One such additional measure would be to oblige all shippers with DM consumers to enter into contracts that explicitly provide for an agreed VoLL and trigger point for interruption pre-emergency.

In addition, we believe that the use of a pre-determined VoLL holds the risk that it distorts the operation of the market by setting a "target price" for both supply and demand side that could lead to a quickly escalating price as we head towards an emergency. This could lead to unintended consequences which impact not only the UK gas markets but also European and global gas markets.

Impact on Credit

Although not included within the quantitative assessment, the introduction of VoLL into imbalance prices will have an impact on the level of indebtedness of shippers and the credit arrangements. Due to the probable increase in credit requirements leading up to, and during an emergency, further consideration of the impact on the credit arrangements is needed. NGG would support a review of the current energy balancing credit arrangements to ensure that they remain fit for purpose post implementation.

Impact Assessment

In assessing the costs and benefits of a high impact low probability event that has not occurred there are a number of assumptions that have to be made. The outcome of the assessment is dependent on these assumptions. The quantified cost-benefit analysis attempts to consider the overall impact of the proposal. The results are dependent on the assumption of the volume of commercial DSR contracts. As mentioned above, we do not believe the proposals in themselves will increase the level of DSR contracts.

In addition, the interaction with the electricity market assumes that there is a quantity of CCGT's that have distillate backup. It is not clear what volume of CCGT is assumed within the assessment. We believe that the quantity of such facilities will reduce from the current levels due to the full implementation of Exit reform and therefore the impact on the electricity system may be understated.

There are a number of commercial incentives on long shippers to increase throughput in an emergency. These are the Post Event Claims Process, potential level of imbalance payments and the potential smear of costs from neutrality. A number of these incentives will not be known at the time of the event. With the proposed arrangements, there is a risk that 'supply-side' shippers who increase their throughput in an emergency will be exposed to significant increase in costs associated with the smear of the residual under recovered DSR payments. This will provide a commercial disincentive to increase throughput in an emergency as supply-side shippers will be exposed to an unknown risk. Although supply-side shippers may be able to sell their gas at prices close to £20/therm, the unknown risk of neutrality smear could disincentivise an increase in throughput.

Development of alternative options

The Gas Forum has presented an alternative option that looks to achieve the same aims to Ofgem's SCR. We believe there is merit in considering and developing this alternative further to better understand how such an option could work in practice.