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24 October 2012

Dear Anjali,

**Ofgem further consultation: Gas Security of Supply Significant Code Review – Proposed Final Decision**

We welcome the opportunity to respond to this consultation and to provide views on behalf of ScottishPower, part of the Iberdrola Group, as a Gas Shipper, Storage Operator, CCGT generator and major gas customer. When taken in conjunction with our sister Shipper, Iberdrola Generacion S.A.U., which brings significant volumes of LNG into the GB market at Isle of Grain, we are significant market players and contributors to gas security of supply.

We continue to share your view that gas security of supply is a critical issue that demands the closest ongoing scrutiny, particularly in these times of the changing UK gas supply portfolio and the likely future demands to be made on gas generation, both in its own right and as the flexible support from intermittent renewables. However, we believe that the market has delivered and will continue to deliver the necessary security of supply through both a diverse portfolio mix and similarly diverse and flexible infrastructure, although we still recognise that complacency should be guarded against.

That having been said we therefore welcomed the SCR but have been disappointed at its continued narrow focus. Indeed the proposed final decision detailed in your consultation has changed little in substantive terms from that outlined in your draft policy decision that was published in November 2011. We responded to that on 31 January 2012 and for the sake of brevity please regard the points made in that response as also being reiterated in this submission.

However we would wish to stress the following points as being aspects that we believe remain of particular significance: -

- In your initial consultation the primary objective for reviewing the current arrangements was “to enhance gas security of supply” and specifically to “minimise the likelihood of an emergency occurring, by encouraging gas shippers/suppliers to take out sufficient insurance (e.g. in the form of long term contracts and storage capacity)”. It is not clear to us from the evidence provided how initiatives based around short term pricing mechanisms such as cash-out are likely to foster that kind of strategic long-term investment. To that extent we are concerned that the review will fail in that objective and that perversely it may actually aggravate such security of supply problems with the potential for wider price contagion, greatly diminished market liquidity and shipper failures.
- The primary purpose of a SCR should be to identify and develop holistic solutions. However, in this instance we remain concerned that the approach has been piecemeal and that no account has been taken of significant interactions such as the soon to be announced gas

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generation strategy, electricity market reform (particularly the operation of any capacity mechanism), whatever conclusions may be drawn from the Further Interventions work done by Ofgem on security of supply and the movement towards a single European market with the ongoing work to develop the relevant Framework Guidelines and Network Codes in furtherance of the Gas Target Model.

- There has been a widespread industry consensus for alternative solutions designed around more market based mechanisms, as evidenced by those advanced via the Gas Forum and more particularly Uniform Network Code Modification MOD0435 “Arrangements to better secure firm gas supplies for GB customers” as proposed by Centrica. These alternatives appear to command support from a breadth of interests, from large upstream producers, large and small downstream shippers and consumers associations such as the Major Energy Users Council. It is anticipated that that support shall be reflected in the responses to your consultation and we would certainly endorse the views developed in the major industry associations, particularly Energy UK and the Gas Forum.

However we are concerned that the proposal to use the powers under the Gas Act 1986 to direct changes to the Uniform Network Code may preclude the development and consideration of such alternatives. Had Ofgem been of a mind to issue a more generic direction, as has been the case in electricity with the outcome of the Project Transmit SCR, then that would have allowed industry to develop a more optimal solution, while still requiring your final approval. It is appreciated that the reason given for opting for this route was to bring the matter to a speedy conclusion and provide certainty to industry but with the time that has elapsed already since the launch of the SCR neither of those reasons appears particularly compelling. By now it would appear to be of much greater priority that the right solution is eventually adopted. For that reason we welcome Ofgem’s decision not to suspend MOD0435 at this time and to consider the concept of a DSR auction in conjunction with the other impending announcements. However we would urge Ofgem to go further and to allow the modification proposal to be fully developed through due process to identify its full merits.

- The implications of the proposed decision on credit arrangements do not appear to have been given adequate consideration. Numerous respondents to your previous consultation highlighted the potential issues arising from cash out charges of £20 per therm. The only response to those concerns appears to be that these arrangements are a matter for the industry to ensure that they remain robust and fit for purpose. However that appears to fail to appreciate the scale of the difficulties that may arise, particularly for small shippers and the inequitable consequences that would arise for the remainder of the market in the event of resultant shipper failures.

We have had sight of the work of the Uniform Network Code’s Energy Balancing Credit Committee and the analysis that it has carried out into the potential impact of the proposed final decision. That analysis has highlighted a range of major concerns particularly over levels of security that would have to be maintained, likely shipper defaults and failures, as well as the potential impact on the wider market with credit and security issues creating barriers to entry.

We share those concerns and have misgivings that these issues may not have had the benefit of adequate consideration and analysis in reaching the proposed final decision or in the Impact Assessment that accompanied it.

In conclusion, we would urge Ofgem to defer any final decision on the implementation of these proposals until such times as there has been an opportunity to consider them fully in light of the foregoing comments, particularly the other impending policy announcements and the development of other industry initiatives.

I hope you find these comments useful and should you wish to discuss any of these points further then please do not hesitate to contact me.

Yours sincerely,

**Gerry Hoggan**  
**Commercial and Trading Arrangements Manager**