

DISCUSSION PAPER REPORT ON PDDN01

Interruptible Charging Methodology Options for UNC Mod 0090

1. Overview

PDDN01 was published on behalf of all of the Distribution Networks.

PDDN01 set out three alternative mechanisms for contracting interruptible rights. Within the paper views were sought from shippers, consumers and other interested parties on the five questions set out below.

1. Which of the three main approaches outlined in Section 5 is favoured?
2. Given that shippers/consumers will need to determine their own value for interruptible rights to some extent under all the approaches, are the shipper's/consumer's costs for the tendered price approaches significantly greater than for the administered price approach?
3. The varying level of operational requirements and competition for interruptible rights in some zones could lead to greatly differing levels of price achieved for interruption rights in different zones, Is this seen as a potential drawback or as an appropriate outcome?
4. What are respondents preferences for the structure of the option and exercise scheme outlined in Section 6?
5. If interruption rights are offered for multiple years ahead, say for years 4 to 8 from the time of the purchase, this may lead to infrequent purchases and so put extra emphasis on achieving the best outcome possible at each purchase time. To what extent does the frequency of purchases of interruption rights impact on the decision about the method chosen to purchase them? If rights are purchased for 5 years, or longer, does this justify the possible extra complexity in the tender-based purchasing methods outlined, and potentially extra decision-making costs for respondents, since the decisions reached on who has interruptible rights and at what price have a more significant impact?

2. Summary

There were 7 responses to the discussion paper.

RWE npower	RWE
Edf energy	EDF
Gaz de France	GDF
STATOIL	STO
Scottish & Southern Energy	SSE
Association of Electricity Producers	AEP
Chemical Industries Association	CIA

There was a wide range of opinions expressed in the responses to the questions. In general most respondents (5) favoured some form of tender, with Option B – open tender, the most popular.

Whilst all parties acknowledged that the DN interruption reform will involve additional work for shippers, and consumers, most respondents (5) did not believe that there will be a significant additional burden under a tender approach.

All respondents agreed that it is right that the cost of interruption should vary between zones.

Six of the respondents agreed that the payment should be split between option and exercise. However there were differing views of the level of flexibility that should be allowed.

There was not a clear consensus on the interaction between the length of contracts and the method of purchasing the interruption rights.

3. Detailed Responses

Which of the three main approaches outlined in Section 5 is favoured?

Four respondents (EDF, GDF, AEP & SSE) favoured the Open Tender approach because they felt that it best meets the objectives of DN interruption reform. However AEP also noted that whilst an open tender may be suitable for large users, it may deter smaller consumers. AEP acknowledged that it may not be possible to run both processes in parallel and stated that this will need to be considered by Ofgem if they undertake an impact assessment.

STO oppose DN interruption reform but consider the hybrid option to be least bad alternative.

RWE favoured an administered charge.

CIA did not indicate which option they favoured. However they stated that option 3 – Hybrid Approach, should not be progressed in its current form because it places a cap on prices.

Given that shippers/consumers will need to determine their own value for interruptible rights to some extent under all the approaches, are the shipper's/consumer's costs for the tendered price approaches significantly greater than for the administered price approach?

All respondents agreed that DN Interruption reform will involve additional work with some variation between the different alternatives. GDF stated that they believe the tender approach "should provide an incentive for shippers and suppliers to develop innovative products and services, which would enhance competition in supply".

The varying level of operational requirements and competition for interruptible rights in some zones could lead to greatly differing levels of price achieved for interruption rights in different zones, Is this seen as a potential drawback or as an appropriate outcome?

All respondents agreed that it is right that the cost of interruption should vary between zones.

What are respondents preferences for the structure of the option and exercise scheme outlined in Section 6?

Four respondents, (STO, SSE, AEP, & CIA) stated that it was appropriate to grant full flexibility in selecting the relative proportions of option and exercise when submitting a tender.

GDF agreed that the tender should be on an option and exercise basis but the choice should be restricted to a limited number of alternatives. RWE were not convinced of the need to offer an option and exercise scheme but argued that if it is to be allowed the choice should be restricted to a limited number of alternatives.

EDF did not directly comment. However they did state that the option and exercise structure could be used to simplify the tender process if required.

If interruption rights are offered for multiple years ahead, say for years 4 to 8 from the time of the purchase, this may lead to infrequent purchases and so put extra emphasis on achieving the best outcome possible at each purchase time. To what extent does the frequency of purchases of interruption rights impact on the decision about the method chosen to purchase them? If rights are purchased for 5 years, or longer, does this justify the possible extra complexity in the tender-based purchasing methods outlined, and potentially extra decision-

making costs for respondents, since the decisions reached on who has interruptible rights and at what price have a more significant impact?

This question generated the greatest range of views. One area of common consensus in all of the responses was that an increased duration of the contract would lead to the supplier or consumer carrying greater risk which should be compensated for.

RWE believed that consumers are unlikely to want to contract interruption rights for more than three years. In addition to this they argued that any increased complexity in the tender process is likely to result in customers being “put off” from offering interruptible services.

EDF believed that the complexity of the process should not be determined by the length of the contract but the volume of interruption required. They also wish to see flexibility in early stages of interruption reform to allow for unforeseen circumstances.

GDF stated that they believe that a five year tender cycle is appropriate to balance the competing needs for stability and flexibility. GDF also stated that it is appropriate for a portion of the option fee element to be paid upon completion of the contracts to ease the cash flow burden associated with the work to set up the contracts.

STO argued that the tenders should be offered at least annually, although they accept that it may be beneficial for sites offering to be interruptible for up to five years to be offered further compensation for the additional risk that they are bearing,

CIA argued that many sites will not be interested in partaking in interruption reform. They are not sure that the additional length of contract justifies additional complexity.