Statoil (U.K.) Limited

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Dear Steve,

Re: Interruptible Charging Methodology Options for UNC Mod 0090, pricing discussion paper PDDN01

Thank you for the opportunity to comment on the above discussion paper. Statoil (UK) Ltd (STUK), have been active members of the Mod0090 working group and have therefore been party to the industry discussions regarding the proposed changes to the DN Interruption regime and as such would like to make the following comments:

Whilst STUK supports development of the UK regime and accepts that modification proposal 0090 was raised by the DNs in response to licence obligations, it is not in support of the implementation of modification 0090 and the proposed changes to the DN interruption regime. A change to the interruption regime will result in less sites being interruptible and those that are successful in the tender process (should mod 0090 be implemented) being interrupted more frequently. Sites which are currently interruptible but lose their interruptible status could be left with stranded assets as their dual fuel capability is no longer needed. The reduction in interruptible sites will also reduce the volumes of gas able to be taken off during stage one of an emergency, therefore increasing the speed at which stages 2 and 3 of the Network Gas Supply Emergency procedures are progressed, meaning that firm load shedding would happen earlier in the process. Given the current tight supply and demand position in the UK and its reliance on gas imports, STUK do not believe that a measure that reduces the amount of dual fuel capability in the UK is appropriate and the introduction of the proposed interruption regime could be detrimental to the security of the system. STUK also believe that if the regime is not targeted correctly and too complex a regime is created, deterring participation, there is a real potential for unnecessary investment being made in the networks resulting in a ‘gold plated’ system.

In response to pricing discussion paper PDDN01, STUK believe that it is difficult to offer a clear opinion on the Interruptible Pricing Methodologies proposed without any indicative pricing being made available. Without an idea of the value being placed on interruption by the DNs, particularly for options 1 and 3 it is hard to determine which option will best reflect a consumers or shippers needs. Also as no information is available on the structure of the interruption zones, it is hard to determine the levels of competition that could be seen or the potential participants in different areas. This information will affect the success of the pricing methodologies and without these details it is difficult to offer full support to any of the Options proposed.

The stated objectives of the interruptible reform proposals are:

- to enable shippers to place value on the interruption they provide
- To provide shippers/consumers with greater choice in the interruptible contracts available to them
- To achieve a fairer distribution of the transportation charges by making operationally unnecessary interruptible sites firm

Pricing discussion paper PDDN01, discusses three options for pricing methodologies by which Interruption contracts could be supplied:

- Option 1 - Administered price
- Option 2 - Open tender
- Option 3 - Hybrid approach

Considering the 3 options, STUK do not believe that the administered price option (option 1), will meet the stated objectives. By allowing consumers and shippers little choice, with opportunity to only accept or reject a price, there would be no price discovery and no opportunity to discover the true value of interruption services. The setting of the administered price before knowing the demand for interruption in an area would likely lead to an inefficient outcome. The administered price would need to be set at such a level that it encouraged participation in the regime without making investment into the system a more economic option. Setting a price too low would discourage participation in the regime and lead to inefficient investment, setting it too high could lead to the over selling of interruption rights fail to meet the stated objectives.

An open tender (option 2) would allow shippers/consumers to state what they consider to be the true value of their interruption and offer tranches of interruption for periods that are most suitable. There is however the real risk that the Transporter may become a distressed buyer in zones where there is little competition for interruption, specifically in the case of sites that were previously NSLs. There is also a risk that a fully open tender process will discourage some smaller consumers from entering the interruptible market. Larger sites will be able to accurately place a value on their interruption service and have the resource and time available to actively participate in the tender process, whilst the potential complexity of this option may deter a smaller site from participating especially if they also have the option of participating in a commercial interruption contact with their supplier.

STUK believes that the hybrid approach (option 3) with a maximum tender price for each maximum duration has the most merit as it offers consumers and shippers the benefits of option 2, a choice in the pricing and duration of contracts, whilst eliminating some of the downsides. Simplifying the process by including maximum tender prices for maximum durations, could potentially encourage more participants to the regime allowing DNs more choice in the contracts they offered and enabling them to achieve the most efficient outcome. As mod 0090 suggests that the requirement for Partial Interruption contracts and Interruptible Firm allowances will no-longer be necessary, the hybrid proposal will enable shippers and consumers the flexibility to tender different volumes at different prices (within boundaries) and durations to replicate the partial interruption / IFA process.

STUK believe that there will be an increased administration cost to shippers and consumers under all approaches, although it is conceivable that the level of detail required to participate effectively in an open tender approach would be more time consuming and costly than the other proposed options. There is a concern that shippers administering this regime on behalf of their customers 3 years ahead of the contracts start could have little reward should the customer change supplier in the meantime. This could act as a deterrent for shipper participation especially if they had alternative commercial interruption contracts to offer. Asking a shipper/consumer to value their interruption is a complex process and something that many small consumers will not have the resource or will to do. The introduction of a complex tendering regime could discourage participation and result in inefficient investment in the network.

It is acknowledged that different parts of the network are more constrained than others and as such it is appropriate that the introduction of a market based mechanism to source interruption contracts would lead to differing price levels in different areas. A variation in price would represent the avoided investment costs and the amount of competition in different zones.

STUK believe that the structure of the Option and Exercise scheme should be left open to allow participants to decide which method of payment most suits their needs. There will be those customers that require a 100% option payment to allow them to invest in dual fuel capability and others that will be prepared to accept a higher portion of exercise payment to compensate for their losses at the time of interruption.

There is a real risk that once the required level of interruption is not successfully sought for a specific area and investment is made, the chance for a site in that area to become interruptible is lost, unless there are dramatic developments in the supply demand balance in that area. Although there will be sites that wish to tender for long periods of interruption it is important that auctions are held at least annually to allow new entrants to apply for their required level of interruption and for sites to signal any changes in their interruption requirements. It can be argued that sites willing to enter into longer term contract (5yrs) should be offered a further method of compensation as they are reducing the level of risk borne by the transporters, that interruption will be available for them to manage constraints on their networks.

STUK is not in support of a reform of the DN interruption arrangements and would prefer the status quo of arrangements to remain to aid stability and help to ensure security of supply. STUK also believes that there are vital elements of the proposed regime missing (indicative pricing, and definition of interruption zones) to enable shippers and consumers to make an educated decision over the suitability of the suggested pricing options. However, given the three options proposed STUK believe that the Hybrid approach (option 3) would achieve the objectives identified, giving consumers and shippers flexibility in the interruption contracts they choose, whilst offering some protection from potentially high prices spikes in areas with little competition preventing unnecessary investment in the networks.

STUK trust that our comments will be given due consideration and should you wish to discuss any aspect of this response further please contact me on the above number.

Yours sincerely,

Shelley Rouse
Regulatory Affairs Advisor

* Please note that due to electronic transfer this letter has not been signed