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Julian Majdanski
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Dear Julian

Urgent Modification Proposal: 0042: Revision of the emergency Cash-out price

Thank you for providing Scottish and Southern Energy plc (SSE) with the opportunity to comment on the above urgent modification proposal.

SSE understands that this proposal has been raised following Ofgem's rejection of urgent proposal 0021 and seeks to address some of the points raised by respondents and commented on by Ofgem in its rejection letter. Whilst understanding the rationale for following the urgent route, we continue to have concerns that UNC modification proposals addressing serious issues regarding the commercial incentives placed on Users during an emergency are being progressed on an extremely fast-track basis. We believe that this does not afford sufficient time for parties to properly consider all the implications of the changes. A more balanced approach would be to reconvene CORWG which would permit the many issues that have been raised in recent weeks to be properly debated in this forum.

Notwithstanding the above, in the time available we would offer the following comments:

- Emergencies may be different, depending on circumstances. Some are progressive, whilst others are sudden. Where an emergency is rapid, we completely agree with the proposer that to set the emergency cashout price at the prevailing SMP Buy could unfairly penalise Users. To do so could result in small trades setting a penal cashout price which could potentially send companies out of business. It could also create a perverse incentive for parties to hold more gas in reserve for themselves in the lead up to an emergency, because of the fear of a penal cashout, rather than encouraging them to "help" either by releasing excess gas to the market or by placing demand side bids on the OCM. This could actually exacerbate the development of the situation and lead to the declaration of an emergency.

- Under existing UNC arrangements, at the time that Transco's use of the OCM has been suspended, a Gas Deficit Emergency (GDE) would have been declared and the "command and control" arrangements would come in to force. These arrangements oblige Users under UNC, licence and law (GS(M)R) to cooperate with requests by the NEC/any Transporter to maximise flows on to the system and to reduce/cease offtake of gas from the system at relevant offtakes.

- As stated above, once a GDE has been declared, Users are subject to "command and control" management by NEC/Transporters. In addition, the provisions of TPD Section C are suspended, except where required for communication between Transco NTS (arguably all Transporters) and Users. At this stage Users will be unable to execute NBP trades. Physically, gas flows onto and offtakes from the system are subject to command and control by the NEC/relevant Transporter. In our opinion this means that the User's ability to balance its portfolio will be extremely limited. Furthermore, Users' portfolios in any event will be subject to significant uncertainty in terms of demand and supply during the emergency. It stands to reason therefore that to continue to impose "incentives" on Users to balance would introduce an unmanageable risk when there is no market to utilise. It is our understanding that this reality is implicitly recognised by the adoption of the "neutral" single cashout price which underpins Section Q and has been in place for many years.

- As stated above, by the time the emergency cashout arrangements take effect, a User will be extremely limited in its ability to balance its position. In addition we agree with the view expressed by the proposer that it is highly unlikely that any change to emergency cashout prices would provide any greater incentive for gas to be delivered to GB from the continent or via LNG imports. The experience earlier this year leads us to conclude that the physical flow of gas is subject to other influences outside the remit of UNC. We believe that concerns in this area are more appropriately addressed by for example changes to European market arrangements and security of supply obligations or via the interconnector agreements.

In summary, SSE continues to believe that the most appropriate approach to the derivation of emergency cashout prices is to maintain the concept of the single "neutral" price for imbalances whether a shipper is long or short. This approach would seem to be in keeping with the principles expounded by CORWG, namely that cash-out prices in an emergency should be hold a party neutral. We note that under the UNC there is an appeals process for parties who are long that believe, ex-post, that the emergency cashout price would not adequately compensate them for the costs they incurred delivering gas to the system.

We are not convinced that modifying the existing emergency cashout arrangements would better facilitate any of the relevant objectives. We do not consider that to move to a prevailing SAP would incentivise the "right" behaviour as it would not take account of the User's inability to balance once a GDE has been declared. **We therefore do not support implementation of this proposal.**

However, we do welcome this proposal as a pragmatic alternative to both 0021 and 0044. We are fundamentally opposed to the implementation of a dual emergency cashout price for the reasons stated above and in our response to urgent proposal 0044. Although we have considered each proposal in its own right, and do not support either, we would reluctantly lend our support to this proposal 0042 in preference to 0044 as we firmly believe that the single "neutral" emergency price is the most appropriate way of cashing out Users who are out of balance during a GDE.

I hope that our comments have been helpful. Please do not hesitate to contact me in the first instance if you wish to discuss any of the points raised in our response.

Yours sincerely

Katherine Marshall
Market Development