



**Comments in respect of
Modification 0042: Revision of the Emergency Cashout Price
Modification 0044: Revised Emergency Cashout and Curtailment
Arrangements**

The Association of Electricity Producers welcomes the opportunity to comment on these urgent modification proposals.

The Association notes that Transco has addressed many of the points in the Ofgem decision letter in respect of modification 0021 and in particular welcomes the introduction of an appeals process for the curtailment quantity amount, we consider this is as significant improvement over the original proposal and has reduced the extent of unmanageable risk associated with the ECQ quantity that shippers and potentially customers could face in the event of a gas deficit emergency being declared.

However the Association continues to have concerns over the processes which have led to this revised proposal, these seem to have been developed in relative isolation from the industry and its views. Notice of this topic being discussed at the Transmission Workstream was only given late during the previous working day, making it unlikely that participants if they were able to attend would be adequately prepared for the discussions. Also the suggestion by the industry that the cashout and curtailment quantity aspects of the proposal be raised as separate modifications was completely ignored, for reasons that are unclear. Finally Transco did not issue the draft modification for discussion at the workstream meeting on 11 August, preferring instead to raise it just one day before, given the criticism Transco faced over the processes around modification 0021 we simply do not understand why they chose to do this. The workstream process is to ensure adequate consideration of proposals by an informed group of stakeholders, not only to inform participants of proposals that have already been raised. By-passing these processes in this manner is clearly not efficient, creates opposition from the industry and seems to imply that Transco does not wish to receive any input from it's customers.

Indeed the Association is becoming concerned that the governance process in its entirety is falling into disrepute and is most certainly not operating in an efficient manner. In recent weeks there have been a series of poorly developed modification proposals which have not been properly developed, have been

subject to shortened consultation periods and have bypassed the workstream process entirely or taken no account of views expressed. In such circumstances it is difficult to see how proposals will gain the support of the industry.

In respect of the cashout element of modification 0044 and 0042, we are disappointed that Ofgem was dismissive of concerns raised over emergencies developing over different timescales and the impact the impact SMP BUY pricing could have in an emergency that progresses rapidly and does not provide time for shipper / customer response even though a high SMP BUY price may have been set. We expect Ofgem to explain more fully why it is unwilling to consider scenarios where an emergency develops rapidly.

The association also shares the concerns of some participants that a SMP BUY price could be set by a single bid possibly for a small volume at an extreme price. In a rapidly developing emergency the prevailing SAP would be more reflective of the true market value of gas than the SMP BUY, and would therefore strike an appropriate balance between providing stronger incentives to balance but avoiding a penal cashout price set by a single outlier trade. Indeed in the absence of an outlier bid, if there was any kind of consensus in the market as to the price of gas and significant volumes were traded at this price then SAP and SMP BUY would tend to be similar. In addition under the current claims process any shipper who has a long position and does not consider that the emergency cashout price has adequately compensated them for the costs of sourcing additional gas may submit a claim for the additional costs.

We also are not entirely clear on what actions on the OCM Transco would take in the run up to an emergency and during stage 1. Transco NTS has not taken the opportunity in the recent SMPS consultation to clarify this. It was our understanding that Transco would take all 'operationally suitable' offers in such circumstances, irrespective of price, which meant all trades that were likely to result in a change of gas flow, hence locational and physical trades rather than title trades. However discussions at the Transmission Workstream suggested that some small locational trades might not be taken if this were to set a price much higher than the prevailing SMP BUY price, and that this would be consistent with its licence objectives to operate efficiently and economically, as the volume of this trade would not be sufficient to impact on the emergency situation. Whilst we accept that there are essentially conflicting objectives here we are concerned that the messages received by the industry may be in conflict. Currently we are hearing that demand side response will be an important aspect of ensuring security of supply this winter in the event of severe conditions and the Demand Side Working Group is actively considering how customer response can be facilitated and yet we are also hearing that even if demand side offers are placed on the OCM they may not be taken. We consider further clarity is required in this respect, or some of the more expensive demand side response may fail to materialise as offers on the OCM.

0044 AEP.DOC

For these reasons we support the prevailing SAP price being used to set the emergency cashout price, but consider further development and refinement of cashout in an emergency situation should be considered in the future.

With respect to the curtailment quantity we continue to support the principle of this and agree that it is logical that this should be extended to firm load where firm load shedding is initiated at stage three of a gas deficit emergency. We also consider that this might encourage enhanced demand side response during the early stages of an emergency. We welcome the clarification of the ECQ methodology that Transco NTS plans to use and the provision of site specific ECQ information to shippers after the day. Whilst we continue to believe that this should be included in the Code, we accept that this could be achieved at a later date. We do however have some ongoing concerns over the complexity introduced by the P70 process in an emergency situation, which may be the only time this is used for firm sites. There is potential for this to deflect attention from the more important issue of managing the physical balance of the system, in particular demand reduction, whether that be initiated by Transco, a shipper or a consumer. The most significant change is the introduction of an appeals process for the ECQ quantity, this addresses many of the concerns we had over this aspect of the proposal. As long as this process is managed sensitively and recognises that in an emergency it is the physical response that is all important and commercial issues can be addressed subsequently via an appropriate audit trail then this should offset some of the commercial risks that were created under the previous proposal. We are therefore now able to support this aspect of the proposal.

To summarise we believe that modification 0042 should be implemented with the ECQ parts of modification 0044

22.08.05