Representation For. 0044

"Revised Emergency Cash-out & Curtailment Arrangements"
Version 1.0

Date of Communication:	22/08/2005
External Contact:	John Costa (Edf Energy Plc)
Slant:	Against
Strictly Confidential:	No

Abstract

EDF Energy Response to Modification 0044 'Revised Emergency Cash-out & Curtailment Arrangements'

Date: 22nd August 2005

Dear Julian,

Thank you for giving EDF Energy the opportunity to respond to Network Code Modification Proposal 044 'Revised Emergency Cash-out & Curtailment Arrangements'.

EDF Energy notes that Transco has raised this urgent modification in response to Ofgem having rejected their previous modification 0021 on the same subject. We note that both proposals are fairly similar, albeit the latter proposal has been tweaked to reflect Ofgem's concerns with 0021. Therefore, for the same reasons we did not support Transco's earlier modification we do not support this proposal as we do not feel it has been properly developed with the industry or proven to better facilitate Transco's relevant objectives. We believe that there are many different types of emergencies caused by different parties including Transco, which have not been thoroughly discussed or thought through fully.

We are supportive of improving cashout arrangements in an emergency to strengthen shippers incentives to balance on such a day. However, this modification has flaws in that more penal and extreme dual cashout prices on such a day may actually exacerbate an emergency situation, allow manipulation of the system by different parties, and lead smaller shippers to incur large losses or even bankruptcy. This is because it changes the commercial incentives between the many different types of shippers. For example, shippers who have little or no offshore gas supplies will be limited in how much response they can make in an emergency and how effectively it can achieve a balance on the day, especially where an emergency is called at short notice and runs straight into stage 2 or 3 where the market is suspended. For this reason this modification is discriminatory as it could adversely penalise smaller shippers or shippers that rely wholly on the market for their supplies. A single cashout price in an emergency is therefore much more equitable. This is in line with Ofgem's response to BSC modification P135 where they state that a neutral cashout price is more appropriate where the market has been broken.

We do not agree with Ofgem's view that a single cashout price based on the average of the previous 30 day's SAP does not sufficiently incentivise shippers to flow extra gas in an emergency and achieve a balance. Indeed, many shippers, and more precisely offshore shippers will be incentivised to flow all or as much gas as they can onto the system to avert an emergency as they will not want only 30 days average SAP for their gas. We do not believe that any shipper will purposefully or commercially withhold gas on such a day as the consequences of the market being suspended or firm load shedding is not in any market participant's interest.

We note that due to the removal of Top-up and the introduction of storage monitor levels that an emergency can be called at a moment's notice if any monitor level is breached by as much as 1KWh. When considering that in the short-term the most likely monitors to be breached would be LNG storage, which could take many days to replenish, then we are talking about lengthy emergency periods where extreme cashout prices would be in place despite the industry's inability to refill LNG storage. Therefore, we can't see how dual cashout prices in this situation would help restore LNG storage levels.

We can see that where an emergency happens gradually, with the depletion of larger storage facilities, then there is some merit in having greater incentives on shippers to balance, which take into account the volatility of price changes. However, the question of what level of price needs to be factored into cashout prices needs to be examined and justified. We do not believe that simply imposing dual or extreme cashout prices, as in any normal day, can be justified in this context as an all fixing panacea. For example, if an emergency happens suddenly, through a major terminal going down, then shippers will have no time, choice or incentive to balance yet they will be forcibly cashed out at what will probably be extreme and penal prices. Also, it is not clear how this modification deals with de minimis balancing actions. A high system Buy cashout price (SMPB) may be set through Transco lifting an outlying bid for a small volume but with a high price tag. This may set an extreme SMPB price regardless of the fact of whether shippers could be able to trade themselves into balance. We therefore question the purpose and efficiency of dual cashout prices in an emergency and believe that de minimis bids less than 50,000 therms do not feed into cashout prices.

It is worth noting that Shippers have strict credit limits in place which restrict the amount of value and counterparties they may trade with in the market. For Transco to assume that shippers can avoid penal cashout prices by trading themselves out of an emergency is unrealistic in practise.

Emergency Curtailment Quantity (ECQ)

We note that this ECQ trade is very similar to the Emergency Interruption Volume (EIV) which Transco introduced in their modification 0021. We do not believe that there has been sufficient discussion of how this calculation will work or be applied in practice. For example, it appears that the decision on whether interruptible gas loads, either commercial or self interruption, should form part of the ECQ rests upon the shipper submitting a P70 form, indicating to Transco that the site has already been interrupted and the volume is no longer available. We do not believe that this procedure will work efficiently in an emergency, especially one where it has developed rapidly; Transco would not have time to process a large number of forms to decide who, and when, to interrupt. This could cause Transco miscalculate how much gas is actually available. The appeals process as part of this proposal is welcomed but we believe that it's best to get it right from the start rather than going through some complex dispute or appeals process which could take months to resolve.

We welcome Transco's explanation of the P70 note but it is not clear whether a shipper can sell all its interrupted firm load in the market or just a partial amount. We refer to paragraph 2.a and ask that Transco provide some further clarification if this modification is implemented.

Also, it would be more useful if Transco called the various stages of calculating the ECQ as 'steps' rather than stages so as not to confuse the industry's interpretation of 'stages' in an emergency under the UNC. We believe that the industry would also draw greater comfort from having the methodology published in the UNC.

EDF Energy does not support the implementation of this proposal as it stands, primarily because of the greater risks it imposes on shippers to understand and effectively respond in an emergency such that they can mitigate this extra risk exposure. However, we do believe the modification has some merits which are worth exploring further.

EDF Energy believes there is merit in looking at cashout arrangements with a view to updating them in light of recent market data as they have been around since network code started in1996. However, we are concerned that the risks associated with this modification have not been adequately identified or assessed. We do not believe that it has been proven that this modification increases the incentives on Users to balance over current arrangements in a Gas Deficit Emergency (GDE). Therefore we do not believe it furthers Transco's relevant objectives.

Modification 0042

We believe that the current 30 day average SAP prices, in the absence of Transco designing better, less discriminatory emergency cashout prices, should remain in place as they are clear and fair and the whole industry understands the associated risks. However, we believe that E.On's modification 0042 to introduce simple SAP on an emergency day is a far better and equitable than the dual or extreme cashout prices proposed under this modification.

For these reasons we believe this modification does not further Transco's relevant objectives as it creates more risk for shippers whilst introducing greater discrimination between certain types of shippers. The industry spent months discussion the issue together with Transco at the Ofgem led Cashout Review Working Group (CORWG) this year, and in previous years, yet the group failed to identify a suitable improvement to current arrangements. We do not believe that raising a 'slap-dash' proposal through the Urgent route this near to Winter is the best way to approach changing Emergency arrangements which could have serious consequences for the whole UK Gas industry and consumers.

We suggest that any future modification relating to emergency situations in gas should be thoroughly developed with the industry with tried and tested through scenario planning so that Transco and the industry can understand exactly what the impact and risks are to the industry. We believe that whilst the current cashout arrangements in an emergency may not be perfect they are clear and understandable, thereby minimising shippers risks and that of an emergency itself actually materialising and or being prolonged; we can not say the same regarding this proposal.

We hope our comments have been useful but please contact me if you need further clarification.

Regards

John Costa
Energy Market Strategy
0207 752 2522