

CODE MODIFICATION PROPOSAL No 0149A
Gas Emergency Cashout Arrangements: Keeping the On the Day
Commodity Market open during a Gas Deficit Emergency
Version 1.0

Date: 17/05/07
Proposed Implementation Date: 1st October 2007
Urgency: Non Urgent

1 The Modification Proposal

For convenience in proposing this alternative the Proposer has adopted much of the text used by National Grid NTS in its original proposal 0149.

a) Nature and Purpose of this Proposal

Where capitalised words and phrases are used within this Modification Proposal, those words and phrases shall usually have the meaning given within the Uniform Network Code (unless they are otherwise defined in this Modification Proposal). Key UNC defined terms used in this Modification Proposal are highlighted by an asterisk (*) when first used. This Modification Proposal*, as with all Modification Proposals, should be read in conjunction with the prevailing UNC. For the purposes of this Modification Proposal, “Gas Deficit Emergency” or “GDE” or “NGS(GD)E” shall mean a Network Gas Supply Emergency Gas Deficit Emergency*.

The GB gas regime is becoming increasingly reliant on non UK Continental Shelf (UKCS) sources of supply, which are occasionally referred to as “merchant gas supplies”. Powers granted to the National Emergency Co-ordinator (NEC)* and the actions of the DTi are only able to “command and control” on-shore facilities, UKCS producers and Storage Operators*. Under the NEC Safety Case* arrangements, the use of the On the day Commodity Market (OCM) is suspended at the start of a Stage* 2 Network Gas Supply Emergency Gas Deficit Emergency* (NGS(GD)E). This means that all trading on the OCM, whether between National Grid and a Shipper User* or between Shipper Users, would be suspended thereby removing one possible “route to market” for non-UKCS gas supplies which could be brought to the GB market during an emergency. It should be noted that other market trading platforms and submission of trade nominations are unaffected by the declaration of a Stage 2 NGS(GD)E.

Ofgem recently chaired a series of workshops, under the heading of “Options for the design of gas emergency arrangements”, to consider, amongst other things, how the UK’s ability to draw upon or attract additional gas resources into the GB network throughout an Emergency event (Stage 2 and higher) might be enhanced.

This Proposal is being brought forward with the intent of opening the OCM to Shippers during a Stage 2 (and beyond) NGS(GD)E;

UNC TPD Section Q 3.2.2 (c) states that upon declaration of Stage 2 of an NGS(GD)E, the application of UNC TPD Section D (other than paragraph 2.4 thereof) will be suspended, National Grid NTS* will cease to take Market Balancing Actions* and that the provisions of Section Q paragraphs 4.1 and 4.2 shall apply. A key provision of Section Q paragraph 4.2 (4.2.4 (a) & (b)) pertains to the setting of the “relevant price*” that is used to clear a User’s Daily Imbalance* following an NGS(GD)E. Under this alternative proposal the “relevant prices” shall continue to be derived as per UNC TPD Section F paragraphs F1.2.1 and F1.2.2 and in each case they are set by reference to the Day* on which the NGS(GD)E (Stage 2 and higher) started.

It is proposed that upon declaration of a Stage 2 (or higher) NGS(GD)E Users, with the exception of National Grid NTS, shall retain the ability to trade on the OCM with other Trading Participants*. National Grid NTS will continue to suspend its use of the OCM in line with the transition to physical balancing of the supply and demand position via the NEC.

It is widely held view that the invoking of Emergency Procedures is an implicit acceptance that normal market conditions and the rules that apply under such conditions can no longer apply. This is reflected by the fact that it is deemed necessary for National Grid NTS to act beyond its residual role in an emergency (e.g. by interrupting customers for energy balancing as well as constraint management reasons).

Shippers will not necessarily be able to respond to so called ‘dynamic’ cash-out process in the same way as they would under normal market conditions. Financial incentives to balance only work if shippers have the ability to respond. A shipper may be faced with a substantial ‘short’ position only as a result of a major terminal failure which in turn resulted in the declaration of a NGS(GD)E. Why would such a party seek to obtain price sensitive ‘merchant’ gas from outside the UK jurisdiction, as this is likely to set a higher cash-out price and exacerbate his already significant financial exposure.

Nevertheless we consider that it is important to keep the OCM open¹ as another route to market for shippers. In the event that a premium price has to be paid to attract price sensitive gas sourced from outside UK jurisdiction and that this is greater than the ‘frozen’ SMPsell price (i.e. the prevailing SAP at the time the NGS(GD)E was declared) any excess would be claimable under the Section Q post emergency claims procedures.

¹ It is our understanding this is simply an anomaly in the UNC that was accidentally introduced into the regime when the old flexibility mechanism (which facilitated transactions only between NGG NTS and shippers) was replaced with the OCM which also allowed shipper to shipper trades.

In support of their original Modification Proposal 0149 National Grid NTS have undertaken a review of the provisions set down in UNC TPD Section Q4.1 ‘Suspension of certain provisions of the Code’. Currently within this section there is listed a number of provisions which come into force upon declaration of a NGS (GD)E Stage 2 and higher. These changes are intended to resolve certain potential inconsistencies in Section Q of the UNC. The changes proposed also form part of this alternative Proposal and are set out below:

- Q4.1.1(b) shall be removed. For the avoidance of doubt, during a NGS(GD)E Stage 2 and higher all the provisions of UNC TPD Section C – Nominations shall apply;
- Q4.1.1(c) shall be removed as the provisions relating to the use of the OCM during an NGS(GD)E Stage 2 and higher will be described elsewhere in Section Q;
- Q4.1.1(d) shall be removed as the potential deferment of the Exit Close out date specified in UNC TPD Section E has no bearing on the operation of the system either during or after an Emergency;
- Q4.1.1(f) shall be removed. We believe that it is beneficial to maintain the NDM Process intact during an Emergency since although the quality of the information may be of a lesser standard than is normally the case it is preferable that Users have access to such information as is available;

b) Justification for Urgency and recommendation on the procedure and timetable to be followed (if applicable)

Not applicable.

c) Recommendation on whether this Proposal should proceed to the review procedures, the Development Phase, the Consultation Phase or be referred to a Workstream for discussion.

This alternative Proposal shall proceed in parallel with the original Modification Proposal 0149.

2 Extent to which implementation of this Modification Proposal would better facilitate the achievement (for the purposes of each Transporter’s Licence) of the Relevant Objectives

(a) “the efficient and economic operation of the pipe-line system”:

By enabling another “route to market” to be available for non UKCS gas supplies, which are occasionally referred to as “merchant gas supplies”, to enter the GB system Users may be able to provide greater cooperation with the NEC to reduce the depth and/or duration of a Stage 2 (or higher) NGS(GD)E.

(d) “so far as is consistent with sub-paragraphs (a) to (c) the securing of effective competition: (i) between relevant shippers;”:

Keeping the OCM open provides another route to market for shippers which (within the major constraints of the emergency situation) may help facilitate some improvement in wholesale market liquidity which may help better facilitate competition between shippers.

The continuation of the ‘frozen’ emergency cash-out prices will ensure that market participants will have greater certainty with respect to imbalance cash-out exposures, enabling them to focus on their duty to co-operate with the NEC in accordance with the relevant Gas Safety Management Regulations, rather than seeking to mitigate the arbitrary financial exposure that we believe is likely to arise from the establishment of a so called ‘dynamic’ emergency cash-out prices.

Parties that find themselves ‘short’ in an emergency will need to use all avenues available to reduce that ‘short’ position. By avoiding the imposition of ‘dynamic’ cash-out prices this proposal avoids exacerbating the financial woes of such parties. This will enable more parties to stay in business² than might otherwise be the case, thus facilitating greater competition in shipping and supply than might otherwise be the case once the full market arrangement have been restored.

(e) The implementation of this Proposal might improve “the provision of reasonable economic incentives for relevant suppliers to secure that the domestic customer supply security standards are satisfied as respects the availability of gas to their domestic customers” by ensuring that market based dynamic cashout prices are set throughout an NGS(GD)E.

3 The implications of implementing this Modification Proposal on security of supply, operation of the Total System and industry fragmentation

Implementation could have a positive impact on the extent and duration of an NGS(GD)E (Stage 2 and beyond) by increasing Users’ options to deliver additional quantities of ‘merchant’ gas into the System.

No adverse implications in respect of industry fragmentation have been identified.

4 The implications for Transporters and each Transporter of implementing this Modification Proposal, including:

a) The implications for operation of the System:

² During the 2005/06 Winter a number of smaller shippers went out of business because of very high wholesale gas prices. Any shippers finding themselves ‘short’ in an emergency against a backdrop of rapidly escalating ‘dynamic’ cash out prices could get into financial difficulties. Failed businesses pass on their imbalance debts and customers to the remaining shippers which would have knock-on financial consequences for those shippers. Complete market failure could follow.

Implementation increases User options to deliver gas to the System during a NGS(GD)E (Stage 2 and beyond) and may therefore assist the Network Emergency Co-ordinator to minimise the extent and/or duration of an emergency.

b) The development and capital cost and operating cost implications:

No development or capital costs have been identified.

However by providing an additional 'route to market' for merchant gas supplies this Proposal may lead to a reduction in the depth and/or duration of an NGS(GD)E and may therefore lead to a reduction in the operating costs incurred during an Emergency.

c) Whether it is appropriate to recover all or any of the costs and, if so, a proposal for the most appropriate way for these costs to be recovered:

No proposal is made for the specific recovery of implementation costs.

d) The consequence (if any) on the level of contractual risk of each Transporter under the Uniform Network Code of the Individual Network Codes proposed to be modified by this Modification Proposal

No such consequence has been identified.

5 The extent to which the implementation is required to enable each Transporter to facilitate compliance with a safety notice from the Health and Safety Executive pursuant to Standard Condition A11 (14) (Transporters Only)

No such requirement has been identified.

6 The development implications and other implications for the UK Link System of the Transporter, related computer systems of each Transporter and related computer systems of Users

No such implications have been identified.

7 The implications for Users of implementing the Modification Proposal, including:

a) The administrative and operational implications (including impact upon manual processes and procedures)

No such implications have been identified.

b) The development and capital cost and operating cost implications

No development or capital costs have been identified. However, costs would be incurred by the relevant Transporter if an Emergency were declared. Therefore if implementation of the Proposal were to reduce the extent and duration of an NGS(GD)E (Stage 2 and beyond) there could be a

reduction in the costs associated with managing such an Emergency event.

c) The consequence (if any) on the level of contractual risk of Users under the Uniform Network Code of the Individual Network Codes proposed to be modified by this Modification Proposal

Unlike the original Modification Proposal 0146 the financial risk on shippers under this alternative Proposal does not increase as the imbalance cash-out prices remain 'frozen'. In fact the additional route to market helps parties better manage there imbalance exposure.

8 The implications of the implementation for other relevant persons (including, but without limitation, Users, Connected System Operators, Consumers, Terminal Operators, Storage Operators, Suppliers and producers and, to the extent not so otherwise addressed, any Non-Code Party)

As stated above, it is possible that implementation of this Proposal could reduce the extent and duration of an NGS(GD)E at Stage 2 and beyond and, if this were the case, this could reduce the costs faced by Consumers as a result.

9 Consequences on the legislative and regulatory obligations and contractual relationships of the Transporters

No such consequences have been identified.

10 Analysis of any advantages or disadvantages of implementation of the Modification Proposal not otherwise identified in paragraphs 2 to 9 above

Advantages

It would provide an additional means for Users to deliver 'Merchant' gas to the System during an Emergency event, potentially reducing the extent and/or duration of the Emergency;

Disadvantages

The Proposer has not identified any disadvantages.

11 Summary of representations received as a result of consultation by the Proposer (to the extent that the import of those representations are not reflected elsewhere in this Proposal)

12 Detail of all other representations received and considered by the Proposer

13 Any other matter the Proposer considers needs to be addressed

14 Recommendations on the time scale for the implementation of the whole or any part of this Modification Proposal

It is recommended that the Modification Proposal is implemented by 1st October 2007.

15 Comments on Suggested Text

Legal text has not been provided for this alternative Proposal. The Proposer would anticipate that much of the suggested text contained in National Grid NTS's original Proposal 0146 would be used save for any elements that relate to the introduction of the 'dynamic' emergency cash-out prices.

16 Suggested Text

See comments under section 15 above.

Code Concerned, sections and paragraphs

Uniform Network Code

Transportation Principal Document

Section(s) Sections D & Q.

Proposer's Representative

Peter Bolitho

Proposer

E.ON UK