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Dear Tim,

RE: Modification Proposal 0187 – "Alterations to the RMSEC Auction to Accommodate Transfer and Trade of Capacity between ASEPs" &

Modification Proposal 0187A – "Alterations to the RMSEC Auction to Accommodate Transfer and Trade of Capacity between ASEPs"

E.ON UK is able to offer **comments only.**

Although both Mods have been brought forward following workshops on the "enduring" trade and transfer process, we consider that many fundamental concerns about the proposed arrangements have not yet been adequately resolved by National Grid. Primarily, this has been due to a lack of symmetry in the information held by the Transporter and information made available to market participants. We also believe that many of the key concerns raised by Ofgem in its previous decisions on the trade and transfer process have not been addressed and, as a result, we believe it would be difficult for Ofgem to implement either proposal without further analysis and evaluation. Certainly, it has proved extremely difficult for us to gauge whether these Modification Proposals further the relevant objectives (or indeed improve on the *status quo*) given the lack of substantive evidence.

Overall, we believe that both Mods 187 and 187A represent a retrograde step in terms of accessibility and utility to shippers when compared to the interim arrangements. Whilst we would not say that the interim arrangements provided the optimal solution, we consider that the proposals for the "enduring" arrangements are considerably worse from a user's perspective. The purported advantages of the "enduring" arrangements all appear to be in terms of low risk and ease of management for National Grid. Consequently, the proposed arrangements are significantly less attractive to shippers when compared to the interim arrangements. Given

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that trade and transfer should be a customer-driven process aimed at helping shippers manage their risk, with National Grid acting as largely neutral facilitator, we would question the benefit of implementing either of these proposals. For instance, in both Mods we no longer have a two-round auction, capacity "zones", information ahead of the auctions, or *ex-ante* exchange rates – all components of trade and transfer that Ofgem has highlighted as important (and the reason for approving or rejecting Mods) in its previous decision letters:

On fixed exchange rates Ofgem has stated:
"[T]he use of a zonal system and a pre-specified transfer rate brings advantages of simplicity and transparency to the process, which would significantly reduce the administrative burden and implementation complexity. Further, the use of a 1:1 Transfer Rate has the advantage of maintaining system capacity." (Mod 156/156A/169/169A decision letter)

On *ex-ante* exchange rates Ofgem has stated:
"We…welcome the simplicity, transparency and predictability of using ex-ante exchange rates." (Mod 156/156A/169/169A decision letter)

On multiple-round auctions Ofgem has stated:
"Ofgem agrees that the use of multiple auction rounds…would allow for greater visibility of prices and price discovery. This would facilitate users in finding the market price for capacity which would be the most efficient price at which to allocate capacity." (Mod 156/156A/169/169A decision letter)

We remain fully supportive of Ofgem's position highlighted in the above statements yet we are unconvinced by the limited evidence brought to the table by National Grid that not retaining these features for the "enduring" arrangements will benefit the market. As you will be aware, E.ON UK was heavily involved in developing a workable interim solution for capacity trade and transfer. When considering whether to raise a proposal for the "enduring" arrangements we have found it frustrating to do so, given the narrow range of information available to shippers. We believe that the information required to support a robust alternative proposal will only be available if an independent audit/analysis of the interim arrangements is undertaken and the results shared with the industry.

We also continue to believe that there is significant merit in the introduction of bilateral trading of capacity between shippers, between ASEPs. For clarity, we do not believe that such a proposal would be inconsistent with either Mod 187 or 187A, if implemented.

Examining the actual detail of the Modification Proposals presented for consultation, we believe there are some meritorious aspects in both, but neither provides the optimal solution. Therefore, we offer the following advantages and disadvantages for your consideration:

Modification Proposal 187 (National Grid)

Advantages:

- Run on a regular, monthly basis (as E.ON UK advocated in Mods 150A/151A).
- Matching highest bids to most expensive capacity should lead to more efficient capacity allocation.

Disadvantages:

- Not truly integrated within the RMSEC auction; thus all the RMSEC bids at an ASEP will be allocated before the transfer of capacity at other ASEPs is even considered. This gives the incumbent at a particular ASEP a significant advantage.
- Arguably no less complicated than the interim arrangements.
- Does not provide sufficient flexibility for purchasing strips of capacity longer than one month (e.g. 6 months).
- Arbitrary limit on exchange rates of 10:1.
- No *ex-ante* or fixed exchange rates.
- Single round auction may not provide sufficient price discovery.
- Abandoning “zones” has not been proven to be advantageous.
- Insufficient information available to Shippers ahead of each auction.
- Bilateral trades are not provided for – sold capacity transfer is only through a National Grid-managed surrender process. We believe this is inconsistent with NG’s licence obligation.

Modification Proposal 187A (British Gas Trading)

Advantages (Relative to Mod 187):

- More commercially attractive to shippers as it offers flexibility to shippers to value their own holdings and set their own reserve prices for surrendered capacity.

Disadvantages (Relative to Mod 187):

- Provides little protection from the <u>potential</u> for hoarding of entry capacity at ASEPs. However, with the new distance-related ‘Transportation’ charging model, you don’t get such large differences between ASEPs close together than you did with Transcost (for example, Theddlethorpe is 0.0063p/kWh/d and Easington is 0.0075p/kWh/d). Therefore, any saving that may be made by purchasing capacity at a nearby, cheaper ASEP in order to transfer it to a more expensive ASEP is outweighed by the transfer risk.
- Some inefficiency in capacity allocation will be caused by trying to match up highest priced bids with lowest priced capacity.

In conclusion, we would advocate a capacity trade and transfer process driven much less by National Grid's requirements and one which is aimed more squarely at the actual needs of its customers. Whilst the current Modification Proposals offer to the market a tool to transfer capacity between ASEPs, the extent to which either allows shippers to effectively and efficiently manage their risk is highly questionable.

Yours sincerely

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