Mr John Bradley
Secretary, Modification Panel
Joint Office of Gas Transporters
51 Homer Road
Solihull
B91 3LT

4th December 2009

Dear John

RE: UNC Modification Proposal 0275 – "*Reduction in DM LDZ Exit Capacity for Supply Points with Significant Change in Usage*"

British Gas does not support the implementation of this modification proposal and is disappointed that National Grid Distribution have failed to address many of the flaws which were identified with its predecessor, MOD0244, and have ignored the requirements specified by Ofgem for any modification in this area in their note to Uniform Network Code (UNC) Review Group 0264[1].

The proposer agrees that this modification fails to meet Standard Special Conditions A11.1 (a), (b), (c), and (e). We also believe that it fails to meet Standard Special Condition A11.1 (d) for a number of reasons. Our reasoning is set out below.

Standard Special Condition A11.1 (d): *so far as is consistent with sub-paragraphs (a) to (c) the securing of effective competition: (i) between relevant shippers; (ii) between relevant suppliers; and/or (iii) between DN operators (who have entered into transportation arrangements with other relevant gas transporters) and relevant shippers;*

1. No evidence of need.

We disagree strongly with National Grid Distribution that this modification is required and note that whilst their proposal is based on the effect the "*current economic climate*" is having on an unspecified "*number of industrial and commercial customers*", The International Monetary Fund (IMF) is predicting[2] that by the time this urgent modification would be implemented the UK economy will have exited recession.

[1] Email from Karron Baker to Joint Office entitled "UNC 264 Review Group", on 28th September 2009.
[2] "*In the United Kingdom, real GDP growth is expected to turn positive in the second half of 2009*", World Economic Outlook, IMF (October 2009) page 77.

This flaw in the rationale for this modification makes it all the more important that the proposer demonstrates clear "*evidence of need*"; the first requirement Ofgem set out in their note to UNC Review Group 0264. Crucially, following a request to Shippers to assess the likely level of take-up of this service, none were able to provide this evidence of need. We also note that in their consultation response to Modification Proposal 0275 that the Major Energy Users Council accept that even they "*do not have any real evidence to support the need for the change*"[3].

Without clear evidence of need it is not possible to show this modification will lead to "*effective competition*" and we therefore disagree that this proposal meets this relevant objective.

2. Unfair reallocation of costs from Daily Metered (DM) to Non-Daily Metered (NDM) market.

As we identified in our response to Modification Proposals 0244, 0244A and 0244B, this modification proposal will have a detrimental effect on the accurate targeting of costs, because reducing charges at one Exit point would need to be balanced with increases in charges more generally so as to allow Transporters to recover their allowed revenue. This would mean that NDM customers, including those in the domestic sector, would need to pay more so that others could pay less.

In addition, and because the likely take-up of this change remains unknown (see point one, above) industry participants are unable to assess the scale of this redistribution of costs from the DM to NDM markets. We agree with Ofgem when they say that any modification in this area must be accompanied with evidence to show that "*allowing DM sites to reduce their capacity … would not give rise to* [an] *inappropriate increase in the share of GDN costs … paid by NDM customers*"[4]. As Ofgem themselves have said, "*it is … important to determine whether there are good reasons justifying this differential*"[5], and we are disappointed that such evidence has not been forthcoming during the modification process.

This modification proposal will simply redistribute capacity charges from one exit point to another; cross-subsidising the DM market at the expense of the NDM market. This will lead to a less accurate distribution of costs, damaging Shippers' ability to engage in "*effective competition*". We therefore believe this proposal fails to meet the UNC relevant objectives.

3. No ability to calculate the costs of this proposal for industry participants.

Because National Grid Distribution have been unable to submit the evidence Ofgem requested in relation to points one and two (above), industry participants are unable to assess how much cost will be redistributed from the DM to NDM market. Implementation of this modification proposal without

[3] Email from Eddie Proffitt to the Joint Office, 30th November 2009, in response to MOD0275 consultation.
[4] Email from Karron Baker to Joint Office entitled "UNC 264 Review Group", on 28th September 2009.
[5] Ofgem Decision Letter on Modification Proposals 0244, 0244A and 0244B, page 5, 20th May 2009

such evidence would therefore be tantamount to providing NDM shippers with an unquantifiable risk in their balance sheet. This uncertainty will be to the detriment of "*effective competition*" and we therefore believe it is contrary to the relevant objective it seeks to meet.

We believe that the apparent urgency of this modification should not be used as an excuse for a lack of substantiation and we request that this modification be rejected and then resubmitted once a proper cost benefit analysis can be completed.

4. Creates a cross subsidy between DM users.
In the course of assessing the likely take-up of any process which may result from this modification, we have established that none of those DM sites in our portfolio who responded were likely to do so. We are concerned that as investments in the network are generally recouped from those who initially request it, and that as this modification makes it more likely that usage will fluctuate, the DM customers on our portfolio will end up paying the costs associated with network investment they are not able to make use of.

This was recognised by Ofgem in their decision letter on Modifications 0244, 0244A and 0244B thus: "*the proposals could increase the level of stranded investment unless the assets can be utilised by other users. To the extent that assets become stranded as a result of a short term decrease in usage, the costs of these assets may need to be recouped from other users. This potentially leads to cross subsidies as other network users are required to fund the network investment, even if they did not trigger it*"[6]. We are disappointed that this modification proposal fails to address this known issue and believe that as such it is fundamentally flawed.

The cross-subsidy this proposal would create between DM users would distort competition between those Shippers and we believe that this modification is therefore contrary to the relevant objectives.

5. Potential for abuse.
We do not believe that sufficient safeguards have been put in place by the proposer to ensure that Shippers do not artificially reduce their costs at the expense of other Shippers. Whilst we recognise that the modification will allow for a retrospective increase in capacity charges following an erroneous withdrawal, we consider that the proposed processes which support this lack transparency lack sufficient assurance, and certainly do not lead to the proposal meeting the UNC relevant objectives; not least the objective of securing "*effective competition*".

6. Reduced predictability of costs.
In the short term these proposals will result under recoveries of costs as charges are reduced for some sites, followed by over recoveries for the network owners to recover their allowed revenue. Costs will therefore be more volatile and less predictable.

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[6] Ofgem Decision Letter on Modification Proposals 0244, 0244A and 0244B, page 6, 20th May 2009

This uncertainty over cost will be to the detriment of "*effective competition*" and therefore contrary to the UNC relevant objectives.

7. Costs outweigh benefits.

The proposer acknowledges that this modification will result in "*systems and process implementation costs*"[7] for Network Operators without reducing the overall burden of costs, for example Transportation charges, faced by the industry. The net effect is this change is a cost to the industry as a whole, falling unequally between those who pre-dominantly supply DM sites wanting to take up this proposed process and those who supply DM sites not minded to take up this process and NDM sites. This inequality is detrimental to "*effective competition*" and the proposal therefore fails to meet the UNC relevant objectives.

Finally, we also note that this proposal is counter to the rationale for the introduction of the revised capacity and commodity split (DNPC03). The move to an increased proportion of revenue recovered from capacity charges brought with it the issues highlighted in modification proposals 244, 244A and 244B. It was however decided that the certainty provided by increased recovery of charges through capacity was more desirable than the previously higher reliance on commodity driven recoveries. We want to point out that this proposal is targeted at large organisations who, overall, are in favour of capacity and commodity split.

If you have any queries relating to this representation, please do not hesitate to telephone me on (07789) 570501.

Yours sincerely

David Watson
Regulatory Manager, British Gas

[7] Modification Proposal 0275, section 5(b), page 6.