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From: Stephen.Macey@corusgroup.com
[mailto:Stephen.Macey@corusgroup.com]
Sent: 10 September 2004 16:45
To: Kyran Hanks
Subject: Review of Top-up Gas

Dear Kyran,

Corus is a major end-user of gas, consuming around 350m therms annually, and our response to your August 2004 document follows. Whilst we recognise the potential effect on market prices that could result from the current top-up arrangements, we do not believe the proposed solution - abolition of top-up gas - would be an appropriate response at this time. This is because top-up provides a strategic national reserve, akin to an insurance policy, for exceptional circumstances including a 1 in 50 winter. This is particularly important as the commercial response from suppliers may be to take the risk for such a low probability occurrence. The present 'problem' with top-up does not appear to be its presence, per se, but rather the rules surrounding it, which facilitate gaming through the effect of "UIOLI" on Transco counter-nominations. This could result in Transco having to call an emergency. In this respect we are most concerned that Transco is proposing to identify a group of customers who could be physically isolated. These would include DM firm loads. No doubt for expediency, Transco would isolate the larger sites first. This would have a severe impact on large manufacturing sites such as steelworks. Ironically most large manufacturing sites do not have weather-related loads and therefore not cause the system peak, yet they would be targeted for protection (!!!) by isolation. We are also disturbed to hear that flows through the Interconnector to Belgium would not be affected. There is also a presumption in the document that there may be significant demand side reduction in response to high prices by customers selling gas back to the market. This may be the case in theory but demand side mechanisms in gas are much less developed than electricity where end-users can and do contract with NGC for ancillary services and can lodge standing BM unit offers in the electricity balancing mechanism. Also, electricity load reductions tend to be offered for relatively short periods (less than a day) whereas gas reductions in severe weather conditions may be needed for a number of days. (Is there a case here for development of products that enable customers to offer load reductions for a few hours?) It must be remembered that selling back to the market of electricity and gas is not a core activity of manufacturers who have tight production schedules to make things for their customers, often on a just-in time basis. Given the effect that events such as a November cold snap could have on the market, it is important that Transco has a measured response designed to minimise the impact on short term gas prices. Priority should be given to improving and making transparent the Transco methodologies in this area. In its May document Ofgem recognised that it may not be possible to remove top-up completely ahead of this winter. This view was echoed by a number of respondents. The position now is that a final decision on Mod 710 is not due until 30 September. In our view this is far too late sensibly to abolish top-up even if it were clear that this would be the best approach - which we doubt. Our proposed package to address the existing problem is

Do not abolish top-up, certainly not for this winter.

Revisit the 'UIOLI' rules in respect of Transco counter-nominations
via
an urgent Modification.

Develop appropriate mechanisms to enable Transco to minimise the
impact
of early winter cold snaps on prices.

Develop demand-side mechanisms between end-users, Transco and
suppliers/shippers. This could be facilitated by Ofgem.

I trust you will find our comments helpful. Please acknowledge receipt
of this message.

Regards, Steve.