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Dear Paul,

**User Commitment for National Transmission System Quarterly Entry Capacity –  
Initial Impact Assessment on Modification Proposals**

Thank you for providing Scottish and Southern Energy with the opportunity to comment on the above consultation. We have detailed our responses to the consultation questions in an attached annex, however would like to take the opportunity to highlight our overall view.

We believe that a system which enables NGG to recover a potential of £44 million, in respect of the new Fleetwood entry point, in relation to an investment made of only around £10 million, is fundamentally flawed and should be reviewed.

However, we believe that the introduction of UNC246, UNC246A or UNC246B will not be sufficient to alleviate the problems. We believe the suggested level of securitisation is inappropriate as it still leaves 90% of the liabilities associated with a defaulting shipper to be paid by the remainder of the market, which will ultimately be borne by customers. In addition it will place additional costs on the industry at a time when significant investment is already required.

We also strongly object to the use of retrospective regulation, as demonstrated in UNC246 and UNC246A, as it will deeply undermine investor confidence in the market, and completely change the competitive dynamics of today's market.

Instead, we believe the most apt methodology for Ofgem to adopt is to review the appropriateness of existing mechanisms at NGG's next price control review.

I hope that our comments are helpful. If you would like to discuss any of the points raised in more detail, please do not hesitate to get in contact.

Yours sincerely,

Claire Rathey  
Regulation Analyst

## **Annex 1: Consultation Questions**

### **Q2.1 Do you have any additional views on the merits/disadvantages of the options for securitization of capacity to add to those of the review group?**

No. Our views have already been captured via the review group.

### **Q2.2 Do you have views on the ability for NGG to cover the potential of shipper default through commercial insurance instruments?**

We do not believe that NGG should purchase commercial insurance to cover the potential of shipper default, as it will not solve the inherent problem and will create long term additional costs for the customer.

### **Q3.1 Do you agree with the analysis of the risks involved? Are there any quantifiable risks that have been omitted?**

A 5 year capacity profile has been used in the modelling for UNC246, UNC246A and UNC246B; however QSEC bookings can be made for up to 16 years. We believe that the 5 year assumption leads to an underestimate of the associated costs.

### **Q3.2 Is the level of securitization being proposed appropriate? If not, why?**

We believe the suggested level of securitisation is inappropriate as it still leaves 90% of the costs associated to be paid by the market.

### **Q3.3 Do you agree with the benefits as presented here? Are there any other ways in which the quantitative benefits could be presented?**

It remains a matter of judgement whether the ongoing annual securitisation cost introduced by these proposals is worth the reduction in risk that may be seen or whether such defaults will occur even with revised security arrangements in place. We believe the proposals will be ineffective in encouraging the necessary behaviour and in fact, will encourage more incidents similar to Fleetwood to occur.

### **Q3.4 How do the risk ranges presented for each of the proposals rank against your perceived risk of default for future capacity bookings?**

It is difficult to comment on the absolute risk ranges presented as we do not believe that measures used to encourage specific 'behaviours' can be accurately quantified.

### **Q3.5 Do you have any preference amongst the proposals on the basis of the quantitative analysis?**

We do not believe that the proposed UNC alteration will change behaviour in the market. However if Ofgem choose to introduce one of the UNC proposals, we believe the lowest cost option, modification UNC 246B, should be used.

### **Q4.1 Do you think that the implementation of any of these proposals would have an adverse effect on competition? Please give reasons for your answer.**

We believe that the requirement for providing security in advance of bidding in the allocation process may act to create a barrier to entry for small players.

### **Q4.2 Do you think any of these proposals are unduly discriminatory?**

Competition in the market would be fundamentally altered if retrospective regulation were introduced. We do not support UNC 246 or UNC246A modifications because of the retrospective element that requires users to securitise all existing QSEC capacity holdings.

Existing capacity holdings were bought by users on the basis of the rules and costs in place at the time of purchase. The proposed UNC246 and UNC246A modifications would change the costs faced by users in respect of existing capacity holdings, without a corresponding increase in the value of that capacity. Retrospectively introducing additional costs increases regulatory uncertainty and will discourage future investment. This would be counter to the attempts to introduce a regime of user commitment and would be damaging to the industry at a time when significant investment is required.

**Q4.3 Do you think the proposals are sufficiently simple and transparent?**

Yes.

**Q4.4 What is your preference on the basis of the qualitative issues?**

We do not believe that the introduction of proposed modifications to the UNC will change behaviour in the market. However, if Ofgem choose to proceed with a UNC modification, we believe the lowest cost option, modification UNC 246B, should be used to manage the default risk.

**Q5.1 Do you think that shipper termination is a tool that should be more widely used to deal with credit default issues?**

No. We believe the shipper termination tool is overly onerous, adds risk and uncertainty, and affects competition by default risk.

**Q5.2 Do you agree that the Income Adjusting Event clause in the gas transporter licence should be reviewed? If so, what manner of changes would you recommend?**

We believe the most apt methodology for Ofgem to adopt is to review the appropriateness of existing mechanisms at NGG's next price control review.

**Q5.3 Do you agree that the revenue driver mechanism for gas entry capacity could be improved? If so, how?**

Yes. We believe additional flexibility should be built into the methodology for triggering capacity delivery to enable the system to be more reactive to shipper / developer needs and reflect the reality of project development i.e. the revenue driver is not triggered until there is greater certainty that the project is in reality going ahead and that NGG will in fact need to deliver the requested capacity.

**Q5.4 Do you have a view as to whether the Authority's role in the approval of NGG NTS proposals to release incremental capacity is no longer required?**

We believe that the Authority's role in the approval of NGG NTS proposals to release incremental capacity should remain, as it provides a useful review step, however we would request that Ofgem publish guidance on the exact assessment criteria used to ease any regulatory or financial concerns that may exist in the market regarding it.

**Q5.5 Are there any other options, outside of the UNC, that could be considered for making the entry capacity credit arrangements more robust?**

We believe the most apt methodology for Ofgem to adopt is to review the appropriateness of existing mechanisms at NGG's next price control review.