

OFGEM DECISION LETTER No. 0669
"Maximising Availability of Interruption for Security of Supply Purposes"
Version 1.0

Shippers, National Grid Transco and other
interested parties

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Dear Colleague

Network code modification proposal 0669 "Maximising Availability of Interruption for Security of Supply Purposes"

Ofgem¹ has carefully considered the issues raised in modification proposal 0669 to Transco's network code, "Maximising Availability of Interruption for Security of Supply Purposes". Ofgem considers that the modification proposal does not fall within the scope of the network code. This is because the proposal is concerned only with the operation of commercial shipper interruption rights and does not affect or relate to Transco's interruption rights which are governed by the network code. Given this, the Authority has no power to consider the modification proposal further or to direct that a modification is (or is not) made.

In this letter, we explain the background to the modification proposal and give reasons for making our decision.

Background to the proposal

The LTI Contracts

The legacy British Gas long term interruptible (LTI) gas supply contracts were originally signed between the integrated British Gas and counterparties between 1990 and 1995. These include contracts with a number of power stations which contain terms that allowed British Gas the right to interrupt for up to a specified number of days a year. In 1997, British Gas split into British Gas Trading (BGT), now part of Centrica, and BG (which included Transco), now part of National Grid Transco (NGT). As part of this process, the company had to make a transfer scheme for the division of assets and liabilities between BG and BGT. As part of this transfer scheme, these contracts, including the provisions for interruption, were assigned to BGT. However, in 1996 (albeit as part of the same process), Transco was given interruption rights for these sites under the provisions of its network code.

The Proposal

Modification proposal 0669 was proposed by Scottish and Southern Energy (SSE) on 13 November 2003. The modification proposal proposes to insert a new provision in Transco's network code that would restrict shipper interruptions under the legacy LTI gas supply agreements. Such interruptions would be prevented under any of the following conditions:

- ◆ over the electricity peak demand hours of 15:00 – 21:00;
- ◆ on any day or part thereof where NGC has issued a system warning; and
- ◆ on any day in respect of which the gas forecast total system demand exceeds 85% of System 1-in-20 peak day demand.

SSE stated that the purpose of the proposed modification is to promote security of supply by ensuring that shipper interruption under the legacy LTI contracts does not restrict or compromise Transco's ability to use its interruption rights to balance the system, manage constraints, provide reserve or maximise CCGT output. SSE believed that the proposed modification would improve NGT's ability to manage interactions between the electricity and gas networks in a way that promotes efficiency and security of supply.

Ofgem agreed the proposed modification as urgent on 14 November 2003. In making this decision, Ofgem took into account SSE's views regarding the likely impact on the safety and security of the network. Ofgem did not assess at this stage whether the proposal related to shipper or Transco interruption rights and noted that to the extent that the proposal related solely to shipper interruption rights, it might be the case that the proposal fell outside of the scope of the network code.

Respondents' views

There were eleven responses to this proposal, ten respondents were not in favour of the proposal and one respondent supported it (the proposer).

SSE stated that to the extent that the specific shipper interruption rights referred to in their proposal impacted on Transco's interruption rights they believed these were legitimate issues for the network code. However, seven of the respondents stated that they considered that the proposal fell outside of the scope of the network code and therefore should be rejected on that basis.

Five respondents considered that the proposal was discriminatory. For example, one party stated that acceptance of the proposal would lead to severe distortions in the market and would unfairly prejudice those parties who have paid for secure and robust supply arrangements and the proposal would provide an effective subsidy to all generators who have not been prepared to pay for the price of security. Another respondent noted that the proposal could undermine arrangements previously made by other generators, who have made commercial decisions, such as whether to opt for firm or interruptible gas supplies and whether to provide back up.

Four of the respondents noted that the proposal would not be expected to lead to an improvement in security of supply, of which two considered that security of supply may be expected to worsen. One of these thought that placing restrictions on a shipper's ability to interrupt might compromise security of supply in gas as commercial interruption may form an integral part of how a shipper plans to satisfy its firm load requirements. Another considered that if interruption under LTI contracts cannot be exercised then more storage may be used and this could increase the probability of Top-up Manager actions.

One respondent noted that the proposal could be seen as extending the scope of the network code in order to enable NGC to manage constraints and system imbalances in the electricity market and that this was in their view wholly inappropriate. Another respondent was of the view that consideration should be given to optimising arrangements across the electricity and gas regimes but thought that maximising output from CCGTs on interruptible contracts was not the best way to do this and nor should NGT have the power to effect this if so desired.

Two respondents considered that the proposer of the modification should instead use Shared Supply Meter Point (SSMP) arrangements that currently exist within the network code to ensure an uninterrupted supply from an alternative shipper.

Transco's view

Transco recommended rejection of the modification proposal. It considered that the LTI contracts referred to in the proposal were commercial agreements between the consumer and Centrica and, as such, did not fall within the scope of the network code. It felt that the modification rules of the network code should not seek to restrain the commercial application of these agreements and that such a proposal would therefore not facilitate competition between relevant shippers and between relevant suppliers as it could be seen to unnecessarily limit the commercial terms that could be provided by shippers and suppliers to their end consumers.

Transco stated that it did not consider that commercial gas supply contract clauses which allow for additional "shipper interruption" over and above that required to meet the user's network code obligations have an adverse impact on Transco interruption rights. Transco believed that the LTI contracts meet the requirements of network code and that the modification proposal did not seek to change the ability of Transco to secure interruption when it calls for it.

Transco observed that the proposal would oblige a user to deliver gas to an offtake at a time when the user would wish to interrupt its service. To the extent that the user is unable to adjust its supplies to cover the increased demand, Transco noted that this would force the user into a negative imbalance position exposing the user to imbalance charges and adversely affecting its ability to meet the requirements of its "firm" supply contracts. Transco stated that this may also lead to an operational balancing requirement which in turn could set cashout prices for the rest of the users on the system. Transco therefore did not consider that the proposal would facilitate the achievement of the efficient and economic operation of the system nor provide reasonable economic incentives for relevant suppliers to secure that the domestic customer supply security standards are satisfied with respect to the availability of gas to their domestic customers.

Transco was further concerned that the proposal discriminated in favour of both power generation loads on the system and, within this sub-group, only those power generation loads supplied under legacy LTIs. Transco also considered that the proposal could distort market price signals in the energy markets as commercially interrupted CCGTs would be released from their "shipper" contractual commitments at a time when the highest price signals are likely to be set.

Transco noted that in establishing the storage monitor levels for this winter it assumed that NTS connected interruptible loads will not be supported by the use of storage. However, to the extent that implementation of this proposal would result in these loads being supported by additional storage withdrawals it noted that there would be more likelihood of an infringement of the existing storage monitor levels.

Transco observed that although SSMP arrangements are only available for those supply points which comply with the conditions set out in network code section G 1.7, it believed that many of the supply meter points covered by the legacy British Gas LTIs are also SSMPs and so can secure alternative supplies in times of “shipper interruption”. It also considered there were other options open to dealing with SSE’s contract concerns such as contract renegotiation or recourse under the Competition Act 1998 if the proposer felt the restriction was anti-competitive.

Ofgem’s view

Ofgem notes the concerns raised by respondents that it is not appropriate to address the issue dealt with under this modification proposal via Transco’s network code. Transco’s network code defines the rights and responsibilities for all users of its gas transportation systems. It is a legal document, required by the terms of its Gas Transporter Licence, between Transco and the Shippers whose gas it transports. In order to decide whether this modification falls inside the scope of the network code, Ofgem has considered whether Transco’s interruption rights under the network code are affected by the operation of the shipper interruption rights under the LTIs. If Transco’s rights are affected then, in Ofgem’s view, it would be appropriate to address the issue dealt with under this modification proposal via Transco’s network code.

In order to understand how the interruption rights in the LTI contracts work, Ofgem has reviewed the demerger files with respect to the split of British Gas Trading from the rest of British Gas plc. Ofgem has also reviewed the explanation of the LTIs contained in the 1993 MMC report². The main findings from these reviews were as follows:

- ◆ The LTIs were intended to fulfil two functions:
 - Supply / demand matching (particularly at peaks), and
 - Capacity management.
- ◆ The contracts were awarded, in full, to BGT at demerger.

As part of the consideration of this proposal, Centrica and Transco confirmed how they considered the interruption rights operated under the LTIs. Centrica and Transco both confirmed that Transco’s rights to interruption (which are governed by the terms of its network code and so allow for 45 days of interruption rights a year unless the sites are TNI Supply Points³) take precedence over Centrica’s contractual interruption rights. The total number of available days of interruption therefore remains as was stated in the original contracts. While these days may not be formally divided between Centrica and Transco, it is the case that Transco is contractually entitled to use up to the number of days of interruption allowed for under the network code. Centrica is, therefore, contractually obliged via the network code to provide the level of interruption required by Transco irrespective of its own interruption rights under the contract. The use of any interruption rights that Centrica may hold cannot affect or change Centrica’s obligation to provide the level of interruption required by Transco.

Ofgem therefore considers that the shipper rights to interruption under the LTI contracts do not interfere with Transco’s interruption rights under the network code. Given this, it is Ofgem’s view that modification proposal 0669, which is concerned only with the operation of shipper interruption rights under the LTI contracts, falls outside of the scope of the network code. Ofgem would note that it is for shippers to manage their compliance with obligations under the network code and to ensure that any commercial contracts with customers enable them to comply with their obligations under the network code.

Ofgem’s decision

For the reasons outlined above, Ofgem has decided that network code modification proposal 0669 does not fall within the scope of Transco's network code since the modification proposal is concerned with the operation of shipper interruption rights which do not interfere with Transco's interruption rights. Given this, the Authority has no power to consider the modification proposal further or to direct that a modification is (or is not) made.

If you have any further queries in relation to the issues raised in this letter, please feel free to contact me on the above number or Matthew Buffey on 020 7901 7088.

Yours sincerely

Steve Smith
Managing Director, Markets

¹ Ofgem is the office of the Gas and Electricity Markets Authority. The terms 'Ofgem' and the 'Authority' are used interchangeably in this letter.

² "Gas and British Gas plc", Monopolies and Mergers Commission, 1993

³ Transco Nominated Interruptible Supply Points are defined in section G6.5 of Transco's network code.