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Dear Julian

Modification Proposal 0727: Publication of Near Real Time Data at UK Sub-terminals.

I refer to the above modification proposal raised by energywatch. It proposes that Transco publish on its website real time (or near real time) flow data for each sub-terminal which flow gas at rates greater than 10 mcm per day.

Shell Gas Direct (SGD) does not support this modification proposal as we are not convinced that the marginal benefit, if any, of these specific proposals outweigh the costs. We outline the reasons for this in relation to the proposal and energywatch's "Additional information paper" presented at the January meeting of the National Transmission & Trading workstream. Since this proposal was raised, Ofgem has published a document on offshore gas production information disclosure. We will be providing comments separately in response to that document.

The proposal

We agree with Transco's general premise that increased information provision should be allowed where clear net benefits can be quantified. There is no evidence that this will be the case with this modification proposal. As Transco sets out, any benefits that could be had from increased information provision have already been captured through the DTI information initiatives. M727 and the supporting document do not make it sufficiently clear why disaggregated data would provide any marginal benefit above that which has already been agreed.

In energywatch's proposal, a number of assertions are made regarding the benefits that its proposal would bring. These assertions are largely based on incorrect premises as outlined below:

* *Harmonising information provision across gas and electricity markets.* As has been discussed in several workstream meetings and raised in response to Ofgem documents, there are several significant differences between gas and electricity which

makes direct comparison misleading. Amongst the difference are that gas production is a resource extraction industry compared to the "manufacture" of electricity (from external inputs). The majority of gas produced in the UKCS is "associated" gas, ie it is produced as a by-product of the production of oil, a more valuable product. Other hydrocarbon products are also produced with gas. There is no equivalent to this in electricity. In gas, shippers buy gas from producers and deliver it to consumers;. Shippers balance their input and offtake portfolios. Shippers nominate gas for delivery to the trading point (NBP); generators do the equivalent in electricity. Shippers deliver gas from the NBP to the consumer; suppliers do this in electricity.

Relevant to this proposal, a more significant difference between gas and electricity is the use of gate closure in gas. There is no longer gate closure in gas following the implementation of M305[1]. This means that there is trading *between* industry participants (ie shippers) as well as with the system operator during the balancing period in gas. In comparison, there is *only* trading with the system operator during the equivalent balancing period in electricity (the half hour). energywatch implicitly acknowledged these differences during discussions in January on its paper by noting that traders knew that generators were going to deliver to their FPN, but do not know this in gas. This is due to the ability of shippers to renominate throughout the day unlike in electricity where the submissions before gate closure are intended to remain fixed. We have asked Ofgem on a number of occasions to discuss this issue in any document it produces on information provision. SGD has previously suggested that the re-introduction of gate closure would address some of the issues and misunderstandings that have developed in the gas industry as the result of the removal of gate closure from gas. We are disappointed that Ofgem's most recent document fails to address these issues: until it does so, we cannot see that it will be able to demonstrate that it has fully considered the issues nor be able to claim to have carried out a robust impact assessment which would allow it to make a decision on this proposal. We will address these concerns further in our response to the Ofgem document.

* *empowering gas consumers to make rational purchasing decisions.* To the best of our knowledge, the vast majority of gas consumers do not rely on market information when making decisions about gas purchasing. Domestic and smaller industrial and commercial consumers buy gas at fixed prices and are largely unaware of market conditions. We assume that energywatch means is that this will allow large industrial consumers who purchase gas flexibly the ability to make rational purchasing decisions. We consider that this premise is based on a false comparison with electricity (as above) and the assumption that by having access to the sub-terminal flow data, the consumer will be better informed about supply/demand and therefore the likely market direction. We find this unlikely: It highly likely that this information will significantly *increase* volatility. This is likely to undermine the customer's ability to make choices. We see no reason to believe that this new volatility will reduce over time. Given that flows overall will be known with Phase 3 implementation, this will provide information on the supply / demand balance on the day which energywatch states will help consumers so the value to consumers of having the data disaggregated remains unknown. We remain perplexed as to how sub-terminal flow data on the day can help with decisions on purchasing gas in future days or weeks.

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[1] "Removal of Requirement to Match Input and Output Renominations for a trial Period" implemented in March 1999 and made permanent in September 1999 through M313.

* *Levelling the playing field between producer-affiliates and non-integrated market players.* energywatch outlines in their additional paper that ex-post reasons for price movements including outages and maintenance which "is the privilege of offshore producers". This implies that only producers have access to data on outages and that all information upstream is available to all. This is not the case. For example, Shell had a serious accident on its Brent platform in October 2003 which had a significant effect on production. This information was swiftly released to the media, and Shell gave television interviews[2]. The evidence presented does not support the suggestiong that one can acribe all price movements related outages to "privileged" information. Furthermore, producers are subject to the provisions of the Competition Act and other UK and EC anti-trust legislation. Amongst other things, this prevents sharing of commercially sensitive information between different producers. Whether or not a market participants is a producer-affiliate is irrelevant in relation to a third party holding commercially sensitive information. All shippers, including non-physical players, will hold commercially sensitive information about their own positions. If this proposal is implemented, it would appear sensible to releasing others' sensitive data to "level the playing field".

Improving Transco's performance incentives to lower costs regarding balancing. This proposal will not provide any additional information to Transco, so it is difficult to seeing what impact it could have on its balancing actions. The "costs" of Transco's actions are neutral to it and smeared to shippers; these costs do not feed through to consumers. A shipper which can outperform its competitors in its balancing performance will benefit financially. Thiss has been discussed in detail,[3] Transco is incentivised to avoid balancing actions and allow shippers to balance the system. On many days, Transco takes no action whatsoever. This proposal will have no effect on Transco's ability to balance the system nor on neutrality costs.

Energywatch additional information paper

BETTA comparison

In making its benefits case, energywatch compares the benefits of BETTA with that of further information provision. Amongst the many reasons that this is comparison is not tenable is the different market structures and degree of integration between the industries. Producers sell gas either at the beach to a third party shipper or, increasingly, at the NBP by its own shipper-affiliate. (This activity *by shippers* is equivalent to that done by generators in electricity.) The electricity market is more vertically integrated than that of gas, particularly in Scotland which, we understand, is the focus of BETTA benefits calculation. But to compare gas production and electricity generation in terms of integration to supply/demand side: the top 6 domestic electricity suppliers have at least 50% of the generation market[4]; of the same 6 domestic gas suppliers, only one – Centrica – has any significant share of gas production (~ 10 to 15%). Gas supply to non-domestic customers[5] has more producers-affiliates some of whom have more than 10% of certain market segments. However, Powergen, a non-producer, has more than 15% is small and large firm and GDF, a new entrant[6] has been able to get over 15% in both firm and interruptible markets. For electricity, all

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[2] See, for example, http://news.bbc.co.uk/1/hi/scotland/4141689.stm
[3] Notably, through the M513 "Review of Energy Balancing" process.
[4] Cornwall Consulting, "Business Energy Markets" energywatch, November 2004.
[5] Ofgem, "Review of competition in the non-domestic gas and electricity sectors", July 2003
[6] GdF does have some, recently acquired, production assets.

supply to non-domestic customers is by integrated generators, with the same top 6 domestic suppliers taking at least 80% of each sub-market – this is not the case with gas supply to non-domestic customers. We will expand further on comparisons between gas and electricity in our response to Ofgem's consulation. We emphasise here only that applying benefit analysis of BETTA, which extends the electricity trading arrangements in England and Wales to Scotland, appears at best highly tenuous.

Buy – sell spreads
energywatch also claims that this would benefit the market by reducing the spread between buy and sells. In gas, the buy-sell spread within day is largely driven by the SMP-buy and SMP-sell prices set by Transco buy and sell actions on the OCM. As set out above, Transco often takes no actions or very few actions on each day (often one only). In all cases, the difference between SMP-buy and SMP-sell has to be at least at the level of the fixed differential, which was introduced to incentivise shippers to balance. SGD does not advocate that this fixed differential is changed but unless it is removed, the scope to reduce the spread within day is significantly restricted making the benefits claimed impossible to achieve.

Outages
The paper also states that significant cost savings "could be achieved from the better coordination of outages". As stated above, producers are subject to competition law which restricts, amongst other things, the ability to cooperate in this manner. For producers to be able to do this, would require negotiation with the Office of Fair Trading (OFT). We had thought that planned outages should be based on each company's own business-related decisions. Ofgem has often promoted having Transco respond to market signals to decide on its own maintenance scheduling, eg in relation to its buyback incentives. energywatch appears to be promoting the view that a regulated (or coordinated) outcome would be more efficient than a market driven one contradicting the economic theory its paper is based upon.

Liabilities and other legal issues
It appears that energywatch assumes that these issues can be easily and cheaply resolved. During industry discussions, energywatch's representative stated that producers have lots of lawyers experienced in upstream contracts. While this is the case, it ignores the substantial and substantive issues which would need to be resolved before a lawyer was engaged to amend the terms of a contract. It is devoting resources to resolve complex issues on liabilities, data accuracy, etc that most costs will be incurred. We note Transco's reservations about these issues and further note that although these issues have been aired previously, energywatch appears not to have understood them or has not seriously consideedr how they could be addressed.

Conclusion
Shell Gas Direct (SGD) does not support this modification proposal as it will not further the Relevant Objectives of the Network Code. We do not consider that benefits have been established which would outweigh the costs of implementation. We do not see that there will be improved competition between shippers and suppliers. In deciding on whether to direct that this modification is implemented, the Authority will need to take to compare the regulatory and information provision environment at the point that this modification would become effective. Given that this environment will include the full implementation of the DTI Information Initiative, this should be the baseline of comparison the Authority should use when making its decision.

Yours sincerely

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