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8th May, 2009

Modification Proposals 0246, 0246A, 0246B: Quarterly NTS Entry Capacity User Commitment

We welcome the opportunity to comment on this modification proposal and its variants. This response is provided on behalf of the RWE group of companies, including RWE npower and RWE Supply and Trading GmbH. We support modification proposal 0246B and see some merit in 0246A. We do not support implementation of 0246. We also strongly believe that Ofgem must undertake a regulatory impact assessment that includes possible changes to National Grid's transporter licence as well the changes set out under the modification proposals.

The current arrangements for acquiring access to the transportation system have proved problematic both in terms of underwriting the liabilities associated with triggering new capacity and the ongoing commitment from users to pay. In principle, we believe that users should face fully cost-reflective liabilities ahead of utilisation of any entry capacity triggered in QSEC auctions. This will provide the correct economic signals for users that wish to deliver gas and, in turn, lead to efficient investment in transmission infrastructure. It also leads to an appropriate amount of risk sharing between "new" and existing users. If new users are only obliged to underwrite a proportion of the investment liabilities ahead of utilisation, it leads to a situation where the balance of any costs are recovered from existing users, which is an inefficient outcomes for these users. Once the infrastructure has been included in the RAV, then under (and over) utilisation is subject to a form of mutual insurance, in terms of annual or more regular review of transportation charges to align actual to allowed revenue.

We accept that this issue is complicated because of the way access rights onto the NTS are allocated. The release of financial rather than physical rights over different time frames means that capacity is allocated without a direct linkage to any actual investment undertaken which makes it difficult to target costs to specific projects. This framework is reflected in the capacity

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incentive mechanism within the NGG transporters licence, which allows NGG to trade-off investment against buy-back and for the System Operator to take incentive revenue for releasing capacity irrespective of requirement to undertake investment. We believe that there is merit in considering whether the current incentive arrangements remain appropriate or if a proxy for investment costs can be developed to sit within reformed to credit arrangements.

Review Group 0221 “Review of Entry Capacity and the Appropriate Allocation of Financial Risk”, deemed any amendments to the licence as out of scope and the resultant UNC modification proposal and its variants address incremental rather than fundamental reforms:

1. To close the loophole where a single-entry point user, having committed to Quarterly System Entry Capacity through long term auctions puts insufficient credit in place and effectively defers capacity delivery at no cost to them.
2. To close the delay between making a commitment to capacity and the need to demonstrate a financial commitment to this capacity.

Together these represent an improvement over the current arrangements. Requiring Users to underwrite their anticipated allocation of capacity prior to a QSEC auction and subsequently maintain this underwriting would provide an incentive on Users to bid their actual requirements in auctions. This may also increase the efficiency of auctions by minimising the risk of speculative bidding.

Of the proposals set out, we support 0246B since this retains the use of a wider range of credit tools that are already acceptable for other transportation security.   In our view, retrospective application of the credit arrangements will undermine the investment climate and, on this basis, the proposal should only apply to future QSEC bookings.

Given these arguments, we cannot support 0246 as the proposal to limit the range of credit tools appears to give rise to costs that far outweigh the value at risk being secured and is not a proportionate response to the problems that have recently arisen.   The industry at large, including Ofgem has always resisted making retrospective changes to the regulatory and commercial framework and we see no good reasons to change this position in this case. Although 0246A addresses concerns about limiting the available credit tools available, it still retains retrospectivity, which we do not support.

We note that all proposals suggest a “user pays” approach to implementation, which will be the first instance of such a proposal since implementation of Modification Proposal 213V. Whilst we would not dispute there should be an element of user funding associated with these proposals we are concerned at the exorbitant rough order of magnitude costs associated with a full system solution implementation. On the basis of these costs we would argue that a less costly manual solution is a more proportionate approach to implementation and we would expect this to be explored further in any RIA. Also we question why only entry users are being targeted under “user pays” as any under recovery from the sale of obligated incremental capacity is reflected, at least initially, in SO revenues that are borne equally by entry and exit users.

These comments represent our initial view and we expect that the RIA will provide further quantitative analysis to enable this view to be refined. Whilst likely to be included under TPCR5, we would expect that further consideration of the entry capacity incentive framework will also be included.

We hope these views are helpful and would be happy to discuss matters further.

Yours sincerely

By Email So Unsigned

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