gaslink
Gas System Operator

Mr. Tim Davis
Chief Executive
Joint Office of Gas Transporters
First Floor South
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1st November, 2011

Re: **UNC Workgroup 0356**

Dear Tim,

Gaslink has been following developments in the UNC Workgroup 0356 and would like to contribute to finalisation of the Workgroup Report via the teleconference arranged for 2nd November 2011. Ahead of the teleconference we would like to record our views on certain aspects of the Modification Proposals. Gaslink makes these comments in its capacity as operator of the network downstream of Moffat.

1. Price levels

Minutes of the 14th October workgroup meeting suggest that the modification proposals "appear to be producing similar prices" and that "discussions today suggested there was little to choose between them [the modifications]".

Gaslink would like to highlight that this is patently not the case from a Moffat perspective – Mod 356A Moffat prices are up to around 5 times greater than Mod 356 prices (for example 0.0106 p/kWh/day compared to 0.0022 p/kWh/day in 2013/14), and even the lowest Mod 356 prices represent a 20 fold increase on current price levels.

Clearly price levels generated by the two Modification Proposals remain an important issue for Moffat users and industry participants downstream of Moffat, and the need to scrutinise the underlying rationale for both modifications is no less important because for certain exit points similar prices are generated.

2. Consistency of peak day flow assumptions

Mod 356 uses National Grid forecast flows across all exit points, and indeed all entry points, for price modeling purposes. Whilst certain parties have expressed concerns regarding the transparency of forecasts, the approach uses data derived by National Grid

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in accordance with its licence obligations and applies this consistently for pricing purposes.

On the other hand, under the Mod 356A approach there is an inconsistent and selective use of bookings, zero flow assumptions and forecast data. Bookings are used for the majority of exit points, but then zero flow is assumed for storage and bi-directional interconnector points, whilst forecasts are used for entry flows. No explanation for these differing treatments is provided within Modification Proposal 356A.

The approach results in starkly different treatments for certain exit points, for example the Moffat Interconnector and the Bacton (IUK) Interconnector exit points. The Moffat exit price is based on booked capacities of around 435GWh/d whilst the exit price for the Bacton (IUK) Interconnector (which we understand has booked exit capacity of over 550GWh/d) is based on zero assumed peak day flow. Whilst we appreciate that an argument can be made that exit flows at the Bacton (IUK) Interconnector or indeed storage sites on the peak day are unlikely to be at the level of booked exit capacities, we would similarly argue that the exit bookings at Moffat are unrealistically high and unrepresentative of likely peak day flows, and that special treatment is required to address this.

Furthermore, we believe that fixing assumed bi-directional interconnector exit flows at zero under Mod 356A is far too restrictive and would not allow the price modeling to reflect changes in market conditions – market prices either side of a bi-directional interconnector should dictate the direction and level of flows. Mod 356 deals with this point because it uses forecasts for bi-directional interconnector exit flows, albeit that the current forecast is zero.

We therefore believe that the Mod 356A approach has an element of arbitrariness and inconsistency in that it applies the bookings rule to the majority of exit points and the zero flow rule to certain selected exit points without any consistent rationale. Entry point flows, on the other hand, continued to be based on forecasts.

3. Levels of peak day flow assumptions

We look now at the extent to which the level of peak day flows assumed under the two approaches might be considered representative of actual peak day flows. For Mod 356, the forecasts generated by National Grid and used for pricing purposes are, irrespective of any shortcomings within the forecasting process, a genuine attempt to predict peak day flows as is required of National Grid under its licence.

By contrast, under Mod 356A the use of booking data (for those exit points where bookings are used) will almost certainly underestimate the peak day flows, because daily bookings and annual bookings in the immediately preceding application window are not taken into account. In our view this feature may inappropriately incentivise shorter term bookings, as it results in lower prices where short term or off-peak bookings predominate, and conversely discriminates against exit points where long term bookings predominate. This is counter to the intention of exit reform which was to provide investment signals via long term bookings.

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In summary we contend that use of forecast data under Mod 356 is a far more consistent and appropriate approach to exit price setting. By contrast under Mod 356A the combined use of booking data in certain cases, and zero or forecast flow assumptions in others, is inconsistent and arbitrary. In the case of Moffat, the Mod 356A approach will lead to use of unrealistically high peak day flow assumptions, whilst other exit points where short term bookings predominate will have unrealistically low peak day flow assumptions. Inevitably this will lead to Moffat users cross-subsidising certain others.

We do not believe that use of forecast data for calculating unit prices should be seen as undermining the user commitment model either for exit or entry capacity, as the fundamental principle that booking levels are used to guide investment decisions is maintained. For pricing purposes we believe it more important to ensure through consistency of approach that perverse incentives are avoided. In our view Mod 356 satisfactorily achieves this whereas Mod 356A, for the reasons stated above, does not.

Please do not hesitate to contact me if you would like to discuss any aspect of this.

Yours sincerely,

Celine Hayes

Celine Hayes,
Manager- Transportation Projects