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Dear John,

### **National Grid Gas (NTS) System Operators Operating Margins (OM) Incentive**

Thank you for providing Scottish and Southern Energy plc (SSE) with the opportunity to comment on the above consultation.

SSE offers the following responses to the specific questions raised in the consultation.

*1. Are there any other activities that National Grid could reasonably do to promote a contestable market and to make a successful safety case demonstration?*

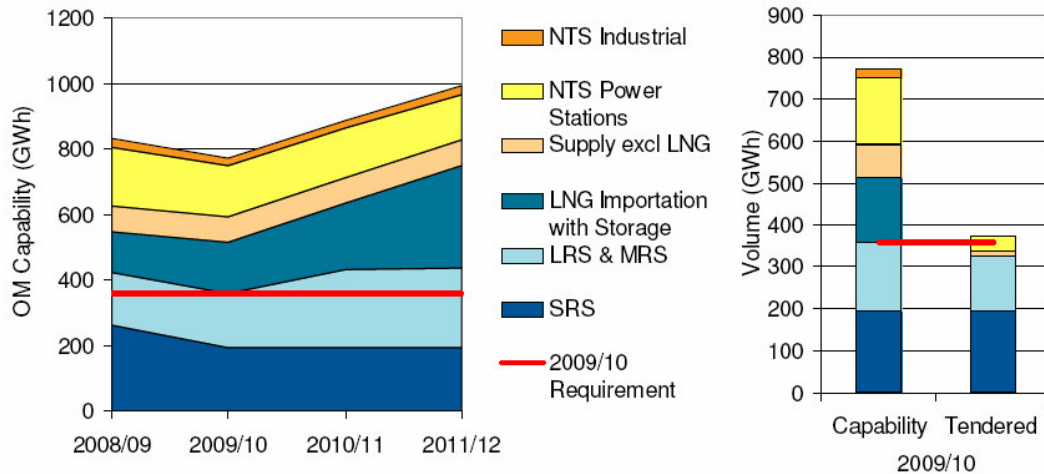
SSE believes NG NTS have been proactive in offering bi-lateral meetings, workshops and information to aid understanding and attract further competition to the OM market. The safety case information will be provided to the HSE who will make the final decision as to the suitability of demand reduction as a source of OM gas.

*2. What additional information would be useful if provided within National Grid's Invitation to Tender (ITT) documentation or Tender Information Report?*

Currently, we believe all reasonable data has been provided to enable bids to be made. If demand reduction bids are deemed acceptable and depending on experience once the 2010 tender has been completed we may have further comments.

*3. Has National Grid sufficiently articulated the requirement and potential market for OM services?*

Yes, we believe the graph below adequately shows requirements & potential sources.



4. Do you believe the new provider types, if approved through the HSE Demonstration case, could form a significant component of future providers of OM?

- NTS Industrial?
- NTS Power Stations?
- Supply Side (Excluding LNG Importation Facilities with Storage)?

Yes, if prices are competitive and sources are physically able to meet required OM response times through the individual NEXAs.

5. Have you any comments in relation to the potential interaction between demand side provision of OM services and the electricity market?

Power stations may also provide services to the electricity system such as frequency response & fast reserve. However, we believe these can be managed within commercial frameworks, since under normal operating conditions electrical output levels will vary in response to commercial and operation needs. In addition, there is no guarantee that the electricity network will be stressed at the same time as OM is required on the gas network.

6. Does National Grid's proposed 2010 OM tender timescale affect, either positively or negatively, the ability for providers to participate?

Once the HSE has determined on its safety case, as much forward notice as possible is required before the tender. This will then allow power station operators to consider if they want to offer demand reduction services. If too little time is made available the level of competition will be reduced as operators will not have had sufficient time to consider all factors and determine a price.

*7. Is there any additional information which could be provided by prior to the tender which would help potential providers in clarifying their position on whether to participate?*

See answer to 6 above.

*8. Is it appropriate to incentivise Operating Margins given the range of uncertainties? If so, what would be the most appropriate way (e.g. Cost minimisation) to incentivise Operating Margins?*

There are many uncertainties regarding the potential cost of OM services; different cost structures of providers, the level of competition in the market and uncertainty over whether or not regulated prices will apply to NG LNG facilities. However, as OM costs are ultimately passed through to customers it is important that NG contracts for these services efficiently through either incentives or regulatory scrutiny.

*9. Should the OM Incentive scheme continue to be separated into a 'Utilisation' and 'Availability' element?*

The introduction of demand reduction contracts will fundamentally affect the availability and utilisation incentives. Currently, storage services typically have high availability costs but the costs of exercising OM contracts are passed through to shippers without any incentive on NG. (Exempting utilisation costs for space only storage contracts). Whereas, demand reduction services would be expected to have low availability and a high exercise price. It would not be appropriate to continue to pass these exercise costs though without incentive. Therefore, an overall cost minimisation incentive across storage and demand reduction and availability and utilisation should be considered.

*10. Should National Grid be able to recover a return on the gas held in storage for OM purposes?*

This may favour gas in store contracts as opposed to space only or demand reduction contracts. There is insufficient detail in the proposal to describe how this inequality will be addressed. Until this is developed further we are against a gas in store return mechanism.

*11. What would be an appropriate length of an incentive?*

There is currently uncertainty over demand reduction services and regulated prices for NG LNG services. Until these are resolved, we would expect the incentive to operate on the basis of a single year. Once there is a period of stability and experience from several years of operation we might then support a multi year incentive.

Please do not hesitate to give me a call if you wish to discuss this further.

Yours sincerely

Jeff Chandler  
Gas Strategy Manager  
Energy Strategy

