

The Joint Office, Relevant
Gas Transporters, shippers and other
interested parties

Andrew Fox
Senior Commercial Analyst
Gas Charging and Access
Development

andrew.fox@uk.ngrid.com
Direct tel +44 (0)1926 656217
Direct fax +44 (0)1926 656604
Mobile +44 (0)7768 104846

www.nationalgrid.com

08 May 2007

Dear Colleague

Review of Incremental Entry Capacity Release (IECR) Methodology Statement 2007

Special Condition C15 of National Grid's Gas Transporter Licence in respect of the NTS, "the Licence", sets out obligations to prepare and annually review the Incremental Entry Capacity Release (IECR) Methodology Statement. As part of the review, National Grid NTS is obliged to consult with shippers on proposed changes. This letter therefore notifies of the proposed changes to the IECR Methodology Statement and invites views on those revisions. Some of the proposed changes to the IECR are required to ensure consistency with changes proposed by the Authority to the Licence.

Due to time constraints, specifically the requirement to have an approved methodology statement in place prior to the September QSEC auctions, National Grid NTS is consulting on its proposed IECR prior to agreement and implementation of the revised Licence. Should the relevant conditions of the Licence be significantly at variance with National Grid NTS's expectations then sections of this statement will need to be amended (which may or may not require further industry consultation).

Sections of this document that are subject to confirmation of the new licence include paragraph 14 (capacity substitutions) and paragraphs 36-45 (investment lead times). National Grid will notify Shippers prior to the QSEC auctions if any parts of this document are not to apply. In this eventuality, the relevant sections of the current IECR (version 6.1 dated June 06) shall apply.

Consultation on the IECR should not be seen as acceptance by National Grid NTS of the proposed licence conditions.

As part of this year's review National Grid NTS has made substantial changes to the layout of the document as well as updating various references and terminology. For this reason a marked up version of the IECR is of minimal benefit and is not provided. However, a copy of the current IECR and the proposed IECR accompany this letter. The key changes made are as follows:

1. Modification to the methodology to determine incremental price steps;
2. Reference to Capacity Substitutions;
3. Investment Lead Times;
4. Role of planning and User Commitment in the triggering of investment;
5. Layout, format and references.

Modification to the methodology to determine incremental price steps

The IECR has been revised to include calculation of incremental price steps using a Transportation Model following the non veto of National Grid NTS's Charging Methodology proposal (GCM01)¹ which implements such an approach for the determination of NTS Capacity charges.

The trigger for release of capacity, i.e. passing an economic test based on NPV of the revenue from auction bids, remains unaltered as a result, but the determination of appropriate costs and charges have. Baseline (P_0) reserve prices are determined in accordance with GCM01 and the same methodology is used to determine incremental price steps (P_1 , P_2 etc.). This charging methodology has previously been widely consulted upon.

National Grid NTS is currently consulting on further changes to the obligated baseline price determination process within the Charging Methodology (GCM06) in response to comments made by the Authority in their decision not to veto GCM01. This consultation and potential change to the charging methodology should not impact upon this IECR methodology statement as the IECR has been drafted such that references to Baseline reserve prices are in accordance with the Gas Transmission Transportation Charging Methodology, hence any future changes to the charging methodology will automatically flow through to incremental price setting.

Reference to Capacity Substitutions

The Authority's proposals for the Licence include a new obligation in respect of the substitution of NTS Entry Capacity. This condition will require National Grid NTS to use reasonable endeavours to undertake capacity substitution where proposing to release capacity incremental to the prevailing level of obligated entry capacity. This is intended to promote the economic and efficient sizing of the NTS by seeking to minimise the amount of investment that is required to satisfy incremental demand. Unsold capacity could be identified as suitable for substitution from "donor" locations where it appears not to be required due to the absence of signals in the long term (QSEC) auctions. The release of incremental capacity will not be affected by this new condition; release will still be subject to the tests defined in the methodology statement. However it will impact on whether National Grid NTS invests to meet the incremental demand and may impact on the availability of capacity at the donor locations in future auctions.

Investment Lead Times

In its final proposals² in respect of the Licence Ofgem proposed a default lead time of 42 months for the completion of reinforcement projects to support incremental entry release. In addition, incentives and allowances have been proposed whereby National

¹ Alternative Methodologies for Determining NTS Entry and Exit Capacity Charges: GCM01.

² Transmission Price Control Review: Final Proposals. Ofgem document ref 206/06

Grid NTS can request an extension to the 42 months or is rewarded for earlier release. These proposals have been included in the revised statement.

Role of planning and User Commitment in the triggering of investment

National Grid NTS undertakes a wide ranging planning process to aid understanding of the requirements for the future development of the NTS. However, investment by National Grid NTS is committed in response to clear unambiguous auctions signals provided by Users. The IECR stresses that release of incremental entry capacity is driven by User commitment and that National Grid NTS will only use planning data (in the absence of User signals) where this is necessary to meet wider statutory obligations or a clear commercial case has been made.

Responses to the proposed IECR should arrive at National Grid by 17:00 on 5th June 2007. They should be sent to:

Jan Gascoigne
NG House
Warwick Technology Park
Gallows Hill
Warwick
CV34 6DA

Alternatively they can be sent by e-mail to:
Boxtransmissioncapacityandcharging@uk.ngrid.com.

Yours sincerely

Andrew Fox