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

Dear Jan,

We welcome the opportunity to comment on the issues raised in this consultation document. This response reflects the views of RWE npower and the UK based business of RWE Trading GmbH.

With regard to the two specific issues referred to in National Grid's letter of the 23rd May we would make the following comments.

Connecting Pipelines

Ofgem's shallow connections policy has previously been interpreted as implying that the point of connection for charging purposes is the point where the new connection pipes join the existing main, although it is not clear the extent to which this differentiates between entry and exit connection points.

To this extent, it does not seem appropriate to include the cost of any connecting pipeline to a new entry point in the assessment of the economics of providing incremental capacity at that new entry point. It would appear to us that this cost should be recouped from the new entry point developer, by way of a connection agreement.

As National Grid point out, as the economic test to release incremental capacity requires only 50% of the projected costs to be met by bids in the QSEC auctions, including connecting pipeline costs in the economic test could result in shippers collectively picking up 50% of the cost of National Grid providing a connecting pipeline to the new entry point.

However, this presumes that once incremental capacity is made available shippers that utilise the new entry point will not buy further capacity, in excess of that initially allocated, in future long, medium and short term auctions. This sounds unlikely, particularly if, as previously signalled, National Grid takes steps to align the reserve price of capacity sold in all entry capacity auctions

Whilst developers may be tempted therefore to request National Grid to build connecting pipelines on their behalf, doing so will transfer project risk away

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from themselves (where they should in theory be best placed to manage it) to National Grid. However, it is not clear to us the extent of this trade off between potential cost reduction and potential increase in project risk.

Also it is unclear the extent to which any strengthening of economic test has the potential to discriminate against new entry projects previously, or are shortly to be, commissioned.

In summary, the principles of strengthening the economic test in circumstances where National Grid provide a connecting pipeline to a new entry point, or removing the cost of connecting pipelines from the economic test and covering this within a connection agreement between National Grid and the new entry point developer, seem correct. However, we do not have a full understanding of the likely impact of such actions to be able to comment definitively on this issue.

Step Price Determination

In our response to NTS GCM01 we supported adopting an approach based on Option 2b, which specifically excluded spare capacity. This view has not changed, as indicated in our response to National Grid's supplementary pricing consultation NTS GCM06.

In the event NTS GCM06 is implemented, and capacity prices are therefore discounted at entry terminals where spare capacity (however that is defined) exists, we do not believe it is appropriate to extend that discount to the calculation of incremental step prices by basing these on the P_0 price prevailing under the NTS GCM06 methodology. Incremental step prices relate to the cost of providing capacity over and above obligated/baseline levels. To the extent parties signal capacity requirements over and above that which National Grid are required by their licence to provide spare capacity clearly does not exist. To base incremental step prices for new capacity on a P_0 price that has been adjusted downwards, due to the fact that existing capacity has not been fully utilised previously, is not cost reflective and potentially distortionary.

With regard to the statement itself, we suggest that the wording in paragraph 37 should be clarified to make it clear that incremental capacity will be made available from the "commencement of the quarter within which the 42 month lead time expires". This is implied by the example used to illustrate this point, but the wording "commencement of the nearest quarter" could imply that the following quarter should be adopted where expiry of the 42 month lead time occurs after the mid point of the relevant quarter.

Also we believe that the wording in paragraph 45 should be enhanced to make it clear that lead time reductions (which act as credits towards National Grid's limited number of opportunities to extend the 42 month lead time) are to apply pro rata from the commencement of the month National Grid is first able to make the full allocated incremental capacity available. It is important that the statement reflects the fact that only early release of the full allocated incremental capacity contributes towards National Grid's incentive (the statement is currently silent on this point) as National Grid may be able to achieve partial release from non obligated capacity, particularly following the recent baseline reductions.

We hope these views are helpful and if you wish to discuss them further please contact Charles Ruffell on 01793 893983 or myself on 01793 892068.

Yours sincerely,

Steve Rose
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