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Date: 20 May 2008

Dear Andrew

### **NTS Exit Capacity Release Methodology Statement in respect of the Interim and Transitional Periods**

Ofgem<sup>1</sup> has considered the submission of the NTS Exit Capacity Release ("ExCR") methodology statement in respect of the interim and transitional periods by National Grid Gas NTS ("NGG NTS") on 20 March 2008 pursuant to Special Condition C18 (the "Condition") of NGG NTS's gas transporter licence (the "Licence"). Having regard to the principal objective and statutory duties of the Authority<sup>2</sup>, and for the reasons set out in this letter, Ofgem has decided that it will approve the ExCR methodology statement.

This letter outlines the reasons for the decision.

#### **Background**

New National Transmission System (NTS) exit arrangements were first raised in the context of the Gas Distribution Network (GDN) sales process ("GDN sales") which was completed in June 2005. At the time of GDN sales it was considered important by the Authority that the fragmentation of ownership of the gas transportation network did not create the potential for inefficient investment or inefficient operational decisions at the new commercial interface between the NTS and the GDNs. When the Authority gave its consent to GDN sales it included the introduction of a proposed enduring offtake framework as a condition of this consent.

In June 2005 the Authority decided to delay the introduction of enduring offtake arrangements to allow for further consultation in parallel with the Transmission Price Control Review (TPCR). As a consequence of this, a set of transitional offtake arrangements was put in place in the 'transitional period' which would precede the 'enduring period'. Prior to the introduction of the transitional period existing arrangements were employed for allocation of exit capacity in this 'interim period'.

Previously NGG NTS was required to prepare and submit an Incremental Exit Capacity Release (IExCR) methodology statement before 1 July each year. This considered how incremental exit capacity was made available for sale to shippers and GDNs, but this did not consider existing exit capacity. The TPCR resulted in a number of modifications to the Licence. One such modification involved the Condition. The Condition now requires NGG

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<sup>1</sup> Ofgem is the Office of the Gas and Electricity Markets Authority. The terms 'Ofgem', 'the Authority', and 'we' are used interchangeably in this document.

<sup>2</sup> Set out in Section 4AA of the Gas Act 1986, as amended.

NTS to prepare an ExCR methodology statement and submit this to the Authority for approval, before 1 April each year. The ExCR methodology statement describes the process by which NGG NTS determines how it will release NTS exit capacity to gas shippers or GDNs.

Prior to submitting the ExCR methodology statement NGG NTS is required to consult for a minimum of 28 days on any changes from the current methodology. The Authority then has two months in which to decide whether to approve the ExCR methodology statement, as submitted, or not.

On 31 January 2008 NGG NTS initiated its consultation as part of the annual review of the ExCR. It received three responses to the consultation. NGG NTS then submitted to the Authority the final version of the ExCR methodology statement, in respect of the interim and transitional periods, for approval on 20 March 2008. The Authority therefore has until 20 May 2008 to make a decision.

### **Changes to the ExCR methodology statement since the last approval**

The new Licence now requires that an ExCR methodology statement be submitted by NGG NTS instead of an IExCR methodology statement. The ExCR methodology statement, submitted by NGG NTS for approval, is similar to the IExCR methodology statement that the Authority approved on 10 August 2007. However, there are a number of key changes including that:

1. The Initial Volume Allocations (IVA) table is removed
2. References to IExCR are changed to ExCR
3. References to 1 July are changed to 1 April
4. Reference to the end of transitional period is extended from 30 September 2011 to 30 September 2012
5. A paragraph is included on interruptible capacity
6. A paragraph is included on the low probability that incremental exit capacity will be allocated in the interim period
7. A section is included on how existing exit capacity is released in the interim and transitional periods
8. For interim and transitional periods clarification is provided that existing NTS exit capacity does not necessarily equate to the NTS baselines in the Licence
9. Greater detail is given on allocating incremental exit capacity in the transitional period within investment lead times
10. A definitions section is included

### **Ofgem's View**

Ofgem agrees with the changes proposed by NGG NTS to the ExCR methodology statement.

The modifications to the Condition on 5 September 2007 as a result of the TPCR resulted in NGG NTS now being required to prepare and submit an ExCR methodology statement, stating how NTS exit capacity is to be released, by 1 April each year instead of an IExCR methodology statement by 1 July. Therefore, the updating of references to the IExCR and 1 July in the ExCR methodology statement submitted on 20 March 2007 reflect the changes to the Licence. The new licence requires details as to how existing NTS exit capacity is released. Therefore, the inclusion of the section on existing NTS exit capacity and interruptible exit capacity in the ExCR methodology statement reflects the modification to the Condition. Furthermore, the description of how existing NTS exit capacity is released reflects the procedures as set out in the Uniform Network Code (UNC) and these changes are therefore appropriate. The removal of the IVA table reflects the fact that there is no longer reference to IVAs in the Licence as a result of the changes to the Licence following the TPCR. One respondent raised concerns with this in that the GDNs will not know if they are requesting incremental entry capacity in the 2011/12 gas year. NGG NTS addressed

this following the consultation by revising the definition of incremental exit capacity. The respondent is now content that the associated risks have been addressed sufficiently.

On 1 May 2008 Ofgem directed that the UNC modification proposal UNC198 be implemented. This resulted in the extension of the transition period to 30 September 2012, and consequently delayed the start of the enduring period until 1 October 2012. Therefore, the changes to the ExCR submitted on 20 March 2008 reflect implementation of UNC198.

Ofgem notes that the interim period ends on 30 September 2008 and therefore that the next Offtake Capacity Statement (OCS) process applies after the interim period and that there is little time, though theoretically possible, in which to allocate incremental NTS exit capacity in the interim period. Therefore, inclusion of the paragraph on the low probability that incremental exit capacity will be allocated in the interim period seems appropriate.

One respondent queried the inclusion of the clarification that for the interim and transitional periods existing NTS exit capacity does not necessarily equate to the NTS baselines in the Licence. However, this clarification appears to reflect the wording in the Licence in Special Condition C8E(3).

The greater detail on how incremental exit capacity is allocated in the transitional period, within investment lead times, merely sets out the actual methodology in words as opposed to referring the reader to the section on how this was done in the interim period, as was done previously in the IExCR methodology statement. As the wording reflects the wording used for how allocation of incremental exit capacity is done in the interim period then this change is appropriate.

One respondent welcomed the inclusion of a definitions section which Ofgem agrees with as has the potential to improve transparency and clarity. The definitions themselves seem appropriate as they either reflect the wording in the UNC or Licence or are effective means of reducing repetition of long tracts of text in the document which makes the document easier to read. Two respondents sought clarification on the definition of 'existing system exit capacity' and one sought clarity on the definition of 'incremental entry capacity' which NGG NTS addressed in the final version of the ExCR methodology statement it submitted for approval.

### **Authority's Decision**

Following consideration of the documentation provided by NGG NTS pursuant to paragraph 1 of the Condition and having regard to the Authority's principal objective and statutory duties and for the reasons set out above, the Authority hereby approves the ExCR methodology statement as was submitted on 20 March 2008.

We note that as the ExCR methodology statement relates to the interim and transitional periods approval of the ExCR methodology statement does not fetter the discretion of the Authority regarding arrangements for the enduring period.

Yours sincerely,



Steve Smith

**Managing Director, Networks**

**Signed on behalf of the Authority and authorised for that purpose by the Authority**