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19 September 2008

Dear Andrew,

NTS Exit Capacity Release Methodology Statement in respect of the Transitional Period

Ofgem¹ has considered the NTS Exit Capacity Release (ExCR) methodology statement in respect of the transitional period which was submitted by National Grid Gas NTS ("NGG NTS") on 22 August 2008 pursuant to Special Condition C18 (the "Condition") of NGG NTS's gas transporter license (the "Licence"). Having regard to the principal objective and statutory duties of the Authority², and for the reasons set out in this letter, Ofgem has decided that it will approve conditionally the ExCR methodology statement. The approval is conditional on revising paragraph 23 of the ExCR methodology statement to make reference to UNC TPD section B3.2.

This letter outlines the reasons for this 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 change in ownership of the gas transportation network did not create the potential for inefficient investment or inefficient operational decisions, particularly at the new commercial interface between the NTS and the GDNs. When the Authority gave its consent to GDN sales it required the introduction of a proposed enduring offtake framework.

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, transitional offtake arrangements were put in place in the 'transitional period', the period preceding the introduction of enduring arrangements

The ExCR methodology statement describes the process by which NGG NTS determines how it will release NTS exit capacity to gas shippers or GDNs during the 'transitional

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

² Set out in Section 44A of the Gas Act 1986, as amended

period'. Paragraph 5 of the Condition allows NGG NTS to propose revising the ExCR methodology statement at any time and submit this to the Authority for approval.

On 7 May 2008 RWE Supply and Trading GmbH raised a UNC modification proposal³. This proposal was intended to make Advanced Reservation of Capacity Agreements (ARCAs) available beyond their current scope. After discussion between NGG NTS and RWE Supply and Trading GmbH it was agreed their desired outcome could be better achieved through a consultation on the ExCR methodology statement without the need to modify the UNC.

On 18 July 2008 NGG NTS initiated its consultation on the proposed changes. It received 8 responses, all of which supported the proposed changes. NGG NTS then submitted to the Authority a revised version of the ExCR methodology statement for approval on 22 August 2008. The Authority has until 19 September 2008 to decide whether to approve the revised ExCR methodology statement as submitted, or not.

Changes to the ExCR methodology statement since previous approval

The key changes to the proposed ExCR methodology statement, as compared with the statement the Authority approved on 20 May 2008 are:

1. All references to the interim period⁴ are removed;
2. Additional paragraphs explaining that shippers and developers may request an ARCA for existing system exit capacity beyond the 6 month timescale envisaged by the UNC;
3. Additional paragraphs explaining that shippers and developers may request an ARCA for incremental system exit capacity within investment lead times beyond the timescales envisaged by the UNC;
4. Additional paragraphs explaining that shippers and developers may request an ARCA for incremental system exit capacity beyond investment lead times if specific reinforcement is not required for a development but the incremental exit capacity request is for more than 20 million therms per annum;
5. A revised definition for ARCA and new definition for "developer" in Appendix 1.

Ofgem's view

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

The consultation received eight responses all of which supported the proposed changes. One of the principal changes is extending the availability of ARCAs to permit shippers and developers to request an ARCA where capacity is, or can be made, available without specific reinforcement.

This change will extend and provide more secure reservation rights to Shippers and Developers for exit capacity. At present Shippers and Developers are allocated exit capacity on a first come first served basis regardless of when that capacity is required. The changes will extend provisions, which are already available to Distribution Network Operators, to Shippers and Developers, allowing them to request an ARCA for capacity required more than 6 months in advance. This will create a more consistent approach for the reservation of offtake capacity from the NTS. Ofgem is content this change is consistent with promoting effective competition within the gas transmission network and so should benefit consumers.

Ofgem would note however that this decision is made on the basis of information provided to Ofgem by NGG NTS that there are no constraints on the provision of NTS exit capacity rights within the transitional offtake period. To the extent that constraints do exist on the

³ Reservation of Firm NTS Capacity at New NTS Exit Points in the Transitional Period – proposal 0214. This can be found on the Joint Office website at <http://www.gasgovernance.com>

⁴ The 'interim period' means the period up to 30 September 2008

NTS (or subsequently arise) with respect to the provision of exit capacity, then Ofgem would have concerns at an approach that allows parties to "lock-in" existing capacity rights through ARCAs on a first come first serve basis. Such an approach could have detrimental impacts upon competition to the extent that it prevents parties, such as new entrants, from competing to secure capacity.

Ofgem notes the revised effective date of 1 October 2008 and, as such, all references to the interim period are removed. The removal of this redundant term is in keeping with NGG's obligation to keep the methodology updated as appropriate.

Ofgem has identified one minor issue with the draft as submitted for approval. Paragraph 23 of the ExCR methodology statement describes circumstances when a shipper can request an ARCA to be made available for the allocation of existing system exit capacity. We note that the paragraph should refer to UNC TPD Section G2 and B3.2. As it is currently drafted the paragraph fails to make reference to UNC TPD Section B3.2.

Ofgem has raised this issue with NGG NTS who confirmed paragraph 23 should include both UNC references. As this oversight will require only a minor amendment to correct it the Authority will give approval to the revised ExCR methodology statement subject to paragraph 23 being amended. In addition to adding the reference to Section B3.2 the UNC reference should also include the reference to TPD, in keeping with references to UNC in the remainder of the document. Paragraph 23 should read as follows:

'Notwithstanding paragraph 21, where a Shipper User requires capacity to first be released beyond the maximum timescale envisaged by UNC TPD Section G2 and B3.2 (i.e. more than 6 months) and the NTS exit capacity request is more than 20 mtpa then the Shipper User may request that National Grid offers an Advanced Reservation of Capacity Agreement "ARCA". The Shipper User shall not be obliged to request, nor sign, an ARCA.'

Authority's decision

Following consideration of the documentation provided by NGG NTS pursuant to paragraph 5 of the Condition and having regard to the Authority's principal objective and statutory duties the Authority approves the NTS Exit Capacity Release Methodology Statement, subject to the amendment of paragraph 23 as outlined above.

As noted above, this decision is made on the basis of information provided to Ofgem by NGG NTS that there are no constraints on the provision of NTS exit capacity rights within the transitional offtake period. To the extent that NTS exit capacity constraints do arise then NGG NTS should consider whether the NTS Exit Capacity Release Methodology Statement should be modified to address this scenario and any potential concerns regarding the provision of ARCAs for existing NTS exit capacity.

We look forward to receiving the revised NTS Exit Capacity Release Methodology Statement reflecting this amendment by 26 September 2008.

Yours sincerely



Stuart Cook

Director of Transmission

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