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Your Reference:

Re: Consultation on the NTS Exit Capacity Release Methodology Statement (ExCR) in respect of the Transitional and Enduring Exit Periods

Dear Andrew,

Thank you for your invitation to comment upon the above consultation.

National Grid Gas plc (Distribution) (NGD) understands the importance of creating appropriate signals with respect to investing within the NTS. We support the sentiment behind the proposals however we do not support some of the detailed points, which we believe need to be addressed.

Principles that we believe should apply

In principle we believe that it is right that a party genuinely requiring additional capacity should pay for it.

We believe that all classes of consumer should be treated the same unless there are strong exogenous reasons, e.g. License obligations, for treating them differently.

Given the lifetime of the assets involved both the regime, and the charges that it generates, should remain stable for as long as possible, so that parties investing in equipment may have a reasonable expectation of recovering their investments as this will tend to reduce their cost of capital ultimately to the benefit of consumers.

Whilst taking into account all relevant factors the regime should be as simple as possible as this reduces the risk of unintended consequences as well as reducing administrative costs.

Key points

<u>Covering letter – User Commitment</u>

The proposed User Commitment regime in combination with the initialization of capacity results in Distribution Network Operators being required to ask for incremental capacity at offtakes where no real increase is required (in fact peak demand may be declining) and then be committed to pay for four years. This has the potential of locking in higher charges that will be passed on to LDZ connected consumers in situations where no investment is in fact required by NTS to support provision of the capacity.

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Within the covering letter there is a reference to a potential solution to the User Commitment issue however it is not clear what the bullet “does not require a revenue driver” means. We support the alternative approach outlined but think that no User Commitment should be required unless NTS can demonstrate clearly that investment is required to support the provision of this incremental, but in practice currently used, capacity.

Page 28 – capacity substitution

Paragraphs 12 to 15 of the consultation discuss exit capacity substitution. Paragraph 15 states that it will be deferred until the obligations become effective and it is unclear what rules will be applied. This is sub-optimal because the potential to transfer demand from one Exit Point to another is an essential tool in managing the development of gas transportation systems whether NTS or LDZ. For example, a new large consumer may wish to connect within a LDZ close to a particular offtake and at the same time another similar consumer elsewhere may cease trading. In this circumstance the Distribution Network Operator would like to substitute their booking from one site to another. If they cannot do this they will be forced to pay for unused capacity at one site, whilst booking incremental capacity at the other. Unless NTS are actually obliged to invest to provide such capacity this is a perverse outcome that will systemically result in higher charges on LDZ connected consumers.

There appears to be a link to this point on page 30 (paragraph 24) where there is a pledge in respect of making available unwanted capacity to other Users, however it is not stated how this is to be done. Presumably the substitution rules could be applied had they been developed.

It is our belief that an appropriate substitution regime should be introduced at the same time as the new rules for Exit Capacity and this will also facilitate the release of unwanted capacity and prevent inappropriate charges being levied and / or inappropriate investment signals being generated.

Page 40 – indicative prices in respect of User Commitments

Paragraph 76 refers to the indicative prices that underlie the User Commitment. It would be useful for it to be made clear that if we commit to an increase in Y+5 or later then it is the indicative price in Year Y that is used.

In addition there should be a requirement on NTS to publish indicative charges by the 1st of May in each year.

This is important to us because of the DN incentive arrangements in our Licence

Not adequately addressed in the consultation – the treatment of Offtake pressure

Flat Capacity, Flexibility Capacity and pressure are intimately connected, however the first two of these are treated separately in these proposals and the third not adequately addressed.

The proposed regime is most highly developed around Flat Capacity with prices and quantities, whereas Flexibility Capacity is quantified and the regime in respect of pressure ill defined by the rules. However, whilst Direct Connects, and by extension the Shippers with an interest in them, have limited interest in pressure (provided it is above a minimum level) this is not the case in respect of Distribution Network Operators.

The offtake pressure available defines the amount of capacity that a Distribution Network Operator can extract from their existing pipeline network without investment and therefore all Distribution Network Operators have an incentive to want higher offtake pressures.

In contrast NTS have the reverse incentive wishing to provide as little pressure as possible because then they will be able to access that driving force to enable them to maximise their capacity whilst also reducing their compressor fuel use.

This interaction is very important across the NTS to LDZ system operator boundary, possibly the most important trade off of all, and yet has not been addressed appropriately throughout this process probably because of participant's unfamiliarity with the issues involved.

We believe that it would be possible to directly relate pressure with capacity provided such that they reduce to one metric, however this would take some development. Without this it is likely that access to pressure will remain arbitrary, lacking in investment signals and generally unsatisfactory.

Other points

Para 18	Refers to Licence SC C8E – Do Users have access to NTS' Licence to see what this means?
Para 36	States that NTS require a revenue driver in their Licence for an exit point before obligated capacity can be released because this will inform their investment decision. However it appears to us that if a User will commit to obligated capacity then NTS has either to invest or risk having to buy capacity back. The revenue driver is irrelevant to this decision.
Para 60	The rules in respect of deemed capacity following an overrun are still to be clarified. For some Users this could affect their decision about capacity booking levels (i.e. whether and to what extent they risk booking capacity below an uncertain peak) because the amount of risk exposure is not known.
Para 66	The timing for revised applications where an initial reduction request is rejected is very tight and leaves little or no opportunity to revise other bookings. (In fact the relative timings are generally tight particularly in relation to Flexibility Capacity bookings.)
Para 67b.	The text refers to charges paid by the relevant Shipper – we believe that this should read User, so as to include Distribution Network Operators.
Para 77	It is stated that, for stepped increases, the final quantity will be used for the User Commitment for all years (which will be more than 4). We believe that the final quantity should only be used for the Commitment covering the last four years with the lower quantities used for earlier years before the maximum capacity is obtained.
Para 80	Increases are processed as "increase by" (i.e. relative amount), whereas decreases are processed as "decrease to" (i.e. to an absolute level). It is not clear why there is a different approach to increases and decreases.

Summary

There are a number of issues that need to be addressed, particularly in relation to pressure, the treatment of User Commitments, initialization and capacity substitution. Provided that these and the above listed issues can be appropriately resolved we would be prepared to support these proposals.

Please do not hesitate to contact me if you wish to discuss anything further.

Yours sincerely,

By e-mail

Jonathan Dennett
Strategy Manager