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*Promoting choice and value for  
all gas and electricity customers*

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Date: 29 May 2012

Dear Andrew

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

On 30 March 2012, National Grid Gas (NGG) submitted to Ofgem<sup>1</sup> the National Transmission System (NTS) Exit Capacity Release Methodology Statement (the "Statement") in respect of the Transitional and Enduring Exit Periods. This was submitted pursuant to Special Condition C18 of your gas transporter licence (the "Licence").

Having regard to our principal objectives and statutory duties, we have decided to approve the Statement for the reasons set out below. This letter also directs that, pursuant to paragraph 2 of Special Condition C18, the next Statement, due in 2013, be accompanied by a statement from "appropriate" auditors. It also outlines our opinion on who constitutes an appropriate auditor.

#### **Background**

In January 2009, we directed the implementation of Uniform Network Code (UNC) modification 195AV<sup>2</sup> which introduced reform of the booking arrangements for NTS exit capacity. These exit arrangements apply to capacity from 1 October 2012 which means there are two phases for the release of exit capacity:

- the transitional exit period for capacity reserved or allocated to users in the period up to and including 30 September 2012; and
- the enduring exit period which applies to capacity reserved or allocated in the period commencing 1 October 2012.

The Statement describes the methodology you employ to release exit capacity in both periods. Special Condition C18 states that you must submit for approval before 1 April in each formula year a copy of the Statement. Before submitting the Statement to us, you must also ensure that gas shippers are consulted and have a period of not less than 28 days to make representations about the Statement.

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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> UNC 195AV: Reform of the enduring NTS capacity arrangements, 19 January 2009. A copy of the decision letter can be found on the Joint Office of Gas Transporters website: <http://www.gasgovernance.co.uk>

On 24 February 2012 you initiated your consultation on proposed changes to the 2012 Statement. The version of the Statement submitted to us on 30 March 2012 took account of the issues raised during the consultation.

The Condition also states that we may direct you to have the NTS exit capacity release methodology audited by appropriate auditors to demonstrate that it has been developed in line with relevant Gas Act and Licence duties. On 27 May 2011 we directed you to conduct an audit of the methodology as set out in the Statement due to be submitted in 2012.

In the sections below we outline the major changes proposed to the Statement and respondents' views expressed in response to your consultation.

## **Proposed changes to the Statement**

### *Changes to Part A*

Part A of the Statement outlines the arrangements and methodology NGG employs to release exit capacity in the transitional period. The transitional period ends on 30 September 2012.

You propose to delete most of Part A from the Statement. The deletions include removing sections which explain the procedure for allocating existing and incremental exit capacity in the transitional period. You consider this text can be removed as it is unlikely new capacity will be released within the remainder of the transitional period.

### *Changes to Part B*

Part B of the Statement sets out the arrangements and methodology for the release of exit capacity in the enduring period. You propose a number of changes to this section to tidy up and remove extraneous or out of date language. This includes removing a number of references to NGG having "sole discretion" when applying some aspects of the Statement.

You also propose to add text to take account of the approval of UNC modification 376S<sup>3</sup>. UNC 376S allows shippers to book capacity from the start of any month between Y+4 and Y+6 (previously capacity bookings started from the 1 October only) and reduces the threshold for applications to increase holdings of Enduring Annual NTS Exit (Flat) Capacity from 10 GWh/day to 1 GWh/day.

UNC 376S has been approved for implementation but, at the time of writing, an implementation date has not been agreed. You have added footnotes explaining the effect of UNC 376S on the Statement after it is implemented.

You also propose to remove text as a result of the approval of UNC 381<sup>4</sup>. The approval of UNC 381 removed the deemed application process for increasing Enduring Annual NTS Exit (Flat) Capacity allocations. You propose to remove sections of the Statement which refer to the deemed application process.

Additional text has also been added explaining the process you will use if you receive two or more capacity reduction requests for the same NTS exit point in response to an ad hoc capacity reduction invitation or via the capacity reduction window. The current text states that where requests received are for a quantity greater than that required, requests in respect of capacity without a user commitment will be accepted before those with a user commitment. Where this criterion does not differentiate the requests, the additional text

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<sup>3</sup> UNC 376S: Increased choice when applying for NTS exit capacity was approved on 19 January 2012. A copy of the decision letter can be found on the Joint Office of Gas Transporters website: <http://www.gasgovernance.co.uk>

<sup>4</sup> UNC 381: Removal of the NTS Exit (Flat) capacity deemed application process was implemented on 14 November 2011. A copy of the decision letter can be found on the Joint Office of Gas Transporters website: <http://www.gasgovernance.co.uk>

proposes to rank requests based on the proximity of the effective date of the reduction request to the date of release of the incremental capacity in respect of which the reduction invitation has been initiated. Reduction requests with an effective date the same as the date of release of the incremental capacity will be accepted first. Reduction requests with an effective date before the date of release of the incremental capacity will be accepted next<sup>5</sup>; reduction requests with an effective date after the date of release of the incremental capacity will be accepted last<sup>6</sup>.

## **Respondents' views**

There was one response to your consultation.

The respondent supported the changes proposed to the Statement. However, they also requested that changes be made to the Statement to take account of UNC 417<sup>7</sup>. This modification, which at the time of writing is entering the consultation stage, removes the requirement for gas shippers to give 14 months notice for applications to reduce Enduring Annual NTS Exit (Flat) Capacity holdings for which they have satisfied their user commitment amount.

The respondent requested that references to the 14 month period be removed from the Statement subject to UNC 417's implementation.

## **Audit statement**

An audit statement was submitted to us on 5 April 2012. We received details of the proposed audit scope on 13 December 2011 and approved this on 23 December 2011. However, due to a delay in the procurement of appropriate audit services, the scope of the audit had to be revised<sup>8</sup>. The audit sought to ensure that the correct procedures to release and reduce exit capacity, as described in the Statement, had been followed and properly recorded. Pursuant to Special Condition C18, we agreed to the scope and objectives of the revised audit on 4 April 2012.

The audit report identified no significant concerns with the procedures undertaken by NGG to release exit capacity or reduce the quantity of exit capacity held by system users.

## **Our views**

We consider the Statement meets the requirements of Special Condition C18 and have decided to approve the Statement. Below we give our views on issues raised by the respondent to your consultation and the changes proposed.

### *Comments on the consultation response*

We note the respondent's comments about the impact of UNC 417. In our view, it is not appropriate at this stage to amend the Statement to take account of UNC 417 as it has yet to be approved.

If, at a future date, UNC 417 is approved then it may be appropriate to amend the Statement to incorporate the necessary changes. However, the timescales for this fall outside the approval and implementation of the 2012 Statement. In this regard, UNC 417 has no bearing on the Statement submitted to the Authority on 30 March 2012.

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<sup>5</sup> This criterion is not available for reduction requests made at an ad hoc invitation.

<sup>6</sup> Reduction requests with an effective date after the effective date of the release of the relevant NTS obligated incremental exit capacity will be accepted at NGG's discretion.

<sup>7</sup> UNC 417: Notice for Enduring Exit Capacity Reduction Applications. A copy of the workgroup report can be found on the Joint Office of Gas Transporters website: <http://www.gasgovernance.co.uk>

<sup>8</sup> The audit was revised to exclude Advanced Reservation of Capacity Agreement (ARCA) and application of exit capacity substitution tests.

### *Comments on the audit statement*

We note the audit statement has not identified any significant concerns with the processes you have used to release exit capacity.

### *Comments on the Statement*

We consider it appropriate for you to remove the sections from Part A of the Statement. There will only be a four month period between the date the Statement comes into force<sup>9</sup> and the end of the transitional period. It is not possible within this time period for additional capacity to be made available under the principles and methodology described in Part A for the transitional period.

We note the changes to Part B to take account of UNC modifications 376S and 381. In particular, we are content that the addition of the footnotes explaining the effect of UNC 376S will allow readers to understand the current provisions of the Statement and how they will be affected after UNC 376S is implemented. We ask you to place the footnote text in the main body of the report as soon as is practicable after implementation.

We have considered the additional text explaining the process you will use in situations where more than one capacity reduction request is made at the same NTS exit point. Currently, the Statement outlines that the user commitment status of the reduction request will be considered. However, it is possible that reduction requests could still remain unresolved after the application of the user commitment criteria.

We are content with the additional text you propose and consider that it will benefit NTS users by outlining the process you will use when dealing with multiple capacity reduction requests.

We also note that you have removed the term "sole discretion" from a number of areas in the Statement. We advised you in our decision letter last year that alternative wording may be preferable given the obligations the gas transporter licence places on NGG. In our view, the removal of the term improves the readability of the Statement and better reflects the manner in which modifications to the Statement and wider charging regime should be encouraged and developed.

### **Audit of the Statement**

We are disappointed that, having instructed NGG in May 2011 to procure an audit, it took so long to develop a suitable scope for the work, and to procure the services of a suitable auditor. These delays frustrated the performance of the audit and a significant amount of effort was required on our part to ensure that a satisfactory audit, limited in scope, could be achieved in time. We want to avoid a similar situation arising in the future.

Therefore, pursuant to Special Condition C18, we direct that the next Exit Capacity Release Methodology Statement, due in 2013, be accompanied by a statement from appropriate auditors, confirming they have carried out an investigation and giving their opinion as to the extent to which the proposed methodology is in line with these duties. We would expect that an appropriate auditor would be a company independent and separate from National Grid Group. The auditor need not be the auditors of National Grid's accounts.

You should engage with us no later than November 2012 to ensure the scope and objectives of the investigation are approved in advance, and to ensure the audit objectives meet the expectations of Special Condition C18.

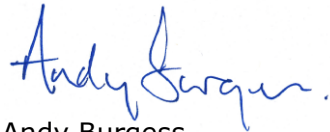
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<sup>9</sup> 1 June 2012

## **Authority's decision**

Following consideration of the documentation provided by NGG pursuant to Special Condition C18 and having regard to the Authority's principal objective and statutory duties, the Authority approves the NTS Exit Capacity Release Methodology Statement.

Yours sincerely



Andy Burgess

**Associate Partner, Transmission and Distribution Policy**