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Dear Jan

Discussion Document NTS GCD 03:
Recovery of TO Allowable Revenue from Exit Users from 1 October 2010

Thank you for providing Scottish and Southern Energy plc (SSE) with the opportunity to provided answers to the specific questions raised in the discussion document.

> The derivation of NTS TO Exit Commodity Rates, applicable to flat capacity utilisation or alternatively to both flat and flexibility utilisation, in light of capacity sale and auction derived revenues, as an appropriate mechanism to ensure National Grid NTS can comply with its revenue restriction licence obligations;

1. It has been proposed that once LRMC's have been converted into prices using a tariff model, no adjustment or scaling is to be made to meet allowed revenue. Following discussions with NGG we understand this under-recovery to be approximately 50 % of allowed revenue or £130 m, assuming all baseline volume is sold at reserve prices.

2. SSE considers that devising a set of charges to under-recover at this magnitude to be unacceptable and consider it questionable in terms of licence obligations to knowingly set charges to under/over recover allowed revenue. Exit capacity charges and reserve prices should be adjusted to recover the total TO exit capacity charge revenue. The proposal means that a TO Exit commodity charge will be required to recover 50 % of capacity allowed revenue. This introduces further complexity and cost to managing the network and is neither economic nor efficient. As throughput is not a constant fraction of peak capacity at offtakes it will also result in a re-distribution of revenue that may not be cost reflective.

3. SSE believes that information should be made available to help inform a decision on how allowed revenue should be recovered. At this stage SSE would like to understand the impact on TO exit capacity charges of recovering all of the allowed TO exit capacity revenue by scaling and adjustment of the capacity charge. This approach has been suggested in the transitional arrangements and is considered to be a more appropriate proposal. SSE believes that most exit capacity will be purchased through prevailing rights at the reserve price with competition

rarely occurring at a node. The prevailing rights mechanism will be more closely aligned to an administered scheme rather than a true auction where competition can be expected at nodes. We also consider that re-distribution of revenue through Commodity charges is just as likely to influence participants' auction behaviour (albeit in another way) as re-distribution through Capacity.Therefore, SSE consider it more appropriate to adjust or scale capacity prices to recover allowed revenue.

4. Applying TO exit commodity charges to both Flex and Flat utilisation will add further complexity and cost of implementation, furthering the point that the proposal is neither economic nor efficient. SSE has expressed the belief in its response to GCD 02 that the flex commodity charge is arbitrary and potentially not cost reflective, to add further commodity charges to flex usage would appear to compound this issue. SSE also reiterates its response to GCD 02 that adding further costs to the usage of flex will add further risk and cost to the electricity BOA & PGBT markets, ultimately increasing electricity prices.

If exit buy-back costs were recovered through the proposed exit capacity neutrality mechanism, the introduction of an Exit Buy-back mechanism in light of capacity sale and auction-derived revenues, as an appropriate over recovery mechanism to ensure National Grid NTS can comply with its revenue restriction licence obligations;

Once charges have been adjusted or scaled to recover 100 % of allowed revenue. If in a subsequent prevailing allocation mechanism an under or over recovery occurs then a TO exit commodity charge may be an appropriate charging recovery mechanism. SSE supports the introduction of a buy back mechanism as described in the discussion paper as an appropriate mechanism to manage over recovery and comply with revenue licence obligations.

The derivation of a negative NTS Exit Commodity Price, applicable to flat capacity utilisation or alternatively to both flat and flexibility utilisation, in light of capacity sale and auction-derived revenues and if over recovery was in excess of buy-back costs, as an appropriate over recovery mechanism to ensure National Grid NTS can comply with its licence obligations;

Once charges have been adjusted or scaled to recover 100 % of allowed revenue. If in a subsequent prevailing allocation mechanism an under or over recovery occurs then a TO exit commodity charge may be an appropriate charging recovery mechanism. SSE support the concept of negative TO exit commodity charge to manage excess revenue over buy back costs and hence comply with revenue licence obligations.

The NTS TO Exit Commodity charge when negative is collared to prevent the aggregate of NTS TO and SO Exit Commodity charges from being negative

Once charges have been adjusted or scaled to recover 100 % of allowed revenue. If in a subsequent prevailing allocation mechanism an under or over recovery occurs then a TO exit commodity charge may be an appropriate charging recovery mechanism. SSE support the concept of a collared charge to prevent the aggregate of TO & SO exit commodity charges from being negative and creating a perverse incentive of being paid to use gas.

The NTS TO Exit Commodity Rate would be set at a level which when combined with revenue recovered from the NTS TO Exit (Flat) Capacity and NTS TO Exit (Flexibility) Capacity charges would recover 50% of the TO allowable revenue.

SSE support the proposal in principle. However, It is the balance of revenue recovery between the TO exit capacity charges and the TO Exit Commodity charges that is our key concern.

In summary, SSE believe that TO exit capacity charges should be recovered via appropriately set capacity charges as per licence obligations. SSE has yet to be convinced that exit TO commodity charges are appropriate because unlike at entry, exit arrangements are very unlikely to result in competitive bidding at nodes. This is because in most cases only one party is likely to need the capacity and this can be procured in the prevailing rights allocation at reserve prices. However, if used for balancing to make up small percentages of allowed revenue then TO commodity charges may be appropriate.

If you would like to discuss any of the above points please do not hesitate to contact me.

Yours sincerely

Jeff Chandler
Energy Strategy
Scottish & Southern Energy