

To all interested parties,

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Dear Colleagues

Joint response to the feedback on proposed changes to the ECR Methodology Statement

Thank you for submitting your feedback to the consultation with regards to changes proposed to the Entry Capacity Methodology Statement.

As part of evolving world events and our ongoing assessment of the network we have identified an increased risk which is likely to occur this summer at the Milford Haven ASEP and brought it to the industry and Ofgem's attention via this consultation. As a prudent System Operator, we have put forward a solution which, we believe, will mitigate the risk, and reduce the potential cost exposure of both our customers and ultimately gas consumers. If implemented, the solution needs to be in place ahead of the RMTnTSEC auctions held in May 2022. We acknowledge that there will be commercial consequences to the LNG industry, as well as to consumers, should this solution be implemented, and that the different views expressed in response to the consultation will need to be carefully weighed when the final determination is made.

We have noted that several respondents referenced National Grid as potentially proposing to withhold an unknown quantity of capacity. We would like to emphasise that, based on our capability assessment, the quantity of entry capacity at Milford Haven which we are committing to make available is clearly defined and it is in excess of any summer capacity flows we have seen historically (the highest flow in the last 3 years between June to October was seen in June 2020 – 38mcm). Furthermore, the current sold long term capacity level stands at circa 32mcm for the June to September and circa 77mcm for October indicating that for most months there is still a significant quantity of unsold capacity available to be utilised.

The feedback we have received regarding the capability assessment indicated that the results would potentially be more accurate if we had considered five years of the demand data (as opposed to three). This is because two out of three years of data could have been skewed by the pandemic. We have re-calculated the demand based on a 5 year period and the table below shows the outcome. Rather than taking the median of the whole dataset, we also propose that for each month, we release capacity equivalent to the maximum median¹ capability observed in the 5-year period. This will replace the median capability numbers included originally in the consultation cover letter appendix.

¹ The median relates to the middle value when all end of day flows for a month are ranked in a list from smallest to largest

Historic Milford Haven Capability / Monthly Capacity to be made available in RMNTnTSEC at Milford Haven Entry Point (May-Oct 2022)			
Month	Capability mcm/d	Year Observed	Capacity to be released kWh/day**
May*	68mcm/d	May 2017	N/A
June	63 mcm/d	June 2021	693,000,000.00
July	63 mcm/d	July 2018	693,000,000.00
August	62 mcm/d	August 2017	682,000,000.00
September	66 mcm/d	September 2017	726,000,000.00
October	68 mcm/d	October 2019	748,000,000.00

**We recognise that the monthly RMTnTSEC capacity auction for May flows has already taken place. However, May capability will play a role in the level of capacity released in the first Weekly NTS Capacity auction on the 20th May.*

***Minus all previously sold Firm NTS Entry Capacity*

National Grid would like to offer this joint response to address other concerns and questions raised in the replies we've received

1) The timescale for this consultation is very short.

We recognise that the timeline of this consultation is not ideal, but given the unprecedented circumstances, the rapidly changing events, and the auction timing, we believe that the timescales proposed were the only viable option to highlight and address the potential risk to the industry.

The unprecedented global events and their impacts have only come to the fore over recent weeks and as such this was not something that we had foreknowledge of. In our view, earlier discussions with the industry could have influenced the capacity booking behaviours for future months, driving higher bookings and potential flows which NTS may not have been able to accommodate.

The main factor contributing to our decision to make the ECR change was the recent start of the war in Ukraine and the changes in the European energy landscape which followed. It is now more likely that there will be higher summer LNG deliveries to GB than previously seen which the network is unlikely to be able to accommodate. This could not have been reasonably anticipated previously.

2) How is National Grid going to manage this problem in the long term?

In the long term we intend to work with Ofgem and the industry to discuss the issues further and, if required, develop a more enduring solution which would apply to the current situation.

We have considered alternative solutions before putting forward this amendment. None of the options considered would have been straightforward and would require a significant level of industry consultation, commercial development, and analysis of network impacts. We decided that the most appropriate way forward was to highlight the increased risk and put forward a solution which should mitigate the increased risk of high constraint management costs and be in place for this summer.

3) We are dealing with extraordinary circumstances and we would encourage National Grid to be consistent with the UK Government's British Energy Security Strategy ("BESS").

We don't believe this proposal goes against the UK Government's BESS. As already mentioned, in the consultation cover letter and the Milford ASEP capability assessment, we've committed to release an amount of monthly capacity which exceeds the highest flows we have ever seen over the period. We have identified the potential risk and have brought it to the attention of the Authority and industry to allow any views to be expressed.

It is our intention to maximise the existing system capability to facilitate as much flow at Milford Haven as possible over the period. We recognise the criticality of our role in ensuring the UK and European gas industry functions in an efficient and effective manner whilst meeting customer requirements. Please be assured that we are working as a priority to ensure we can continue to facilitate gas flows into and out of our network, to the extent that we are able, and are engaging with a number of stakeholders in support of this.

It is worth noting that the proposed ECR changes do not change the capability of the network or our ability to accept flows. We believe that the proposal provides greater certainty to all parties whilst minimising customer and consumer costs. Some respondents (2) agree with this view, but we recognise that the majority of respondents (8) have put forward a different view whereby, if our proposal were approved, it would potentially result in the industry incurring greater costs than those the proposal is seeking to reduce.

4) [Can National Grid publish the daily and weekly maintenance plans for the maintenance months rather than a blanket capacity limit for the whole month?](#)

We appreciate the need for more granularity to be included in our maintenance plans and are considering the best way to take this forward.

Our maintenance plans will not impact the Milford Haven ASEP Capability this summer. This summer our capability at the Milford Haven ASEP is primarily demand and not maintenance driven. It is the lower demand in the area during the summer which is driving our network capability lower. Please note that maintenance is critical to the overall ability of the network to meet customers' flow requirements and can impact capability, but this is not the case this summer.

We will be monitoring closely the supply demand patterns and assessing the network on an ongoing basis. We will discuss with the Authority any deviations from the initial assumptions shared with them and the industry in the Milford Haven ASEP capability assessment.

We have reviewed our maintenance plans and have already deferred, cancelled or rephased maintenance activities at the critical compressor stations in the Milford Haven area to ensure that flows can be maximised throughout the summer.

5) [The manner in which National Grid will assess the monthly SEC availability is unclear. It is not clear that either of the indicative numbers take account of the increased demand from the interconnectors exporting to Europe.](#)

We initially used historic data over the last three summers to give an indication of likely demands May-October at the Milford Haven ASEP. For each network offtake we have reviewed the end of day demand figures on a daily basis and then aggregated all the medians of all the individual demand components for a given month. Based on the responses and questions received we have reviewed this approach utilising historic data over 5 years and will release the highest median capability for each month minus firm capacity already sold for each month ahead (RMTnTSEC), weekly (WSEC) and daily auctions (DSEC). Should the capability level increase, we will seek to release and maximise any additional capacity that we can make available in the weekly and daily auctions.

We noted that the current geopolitical and industry environment is unlikely to directly impact demand in the West Midlands and Wales which is the key factor impacting capability.

When considering the capability of the entry point at Milford Haven, all entry flows must either be directed into one of the areas of demand or pass through the various compression assets in the West of the UK. Of all the compression assets listed in the technical design of that part of the network, Churchover Compressor Station represents the station with the lowest available power and hence, the lowest maximum attainable flow rates. Milford Haven entry capability can be accurately calculated by aggregating demand (from Pembroke Power Station, and the Wales South and West Midlands LDZs) and adding this to the maximum flow capability of Churchover Compressor Station. Increased demand on the Bacton side of Churchover Compressor Station will not increase the maximum flow capability of the compressor.

6) Can NGG consider separating the capacity of Milford haven between South Hook and Dragon so that there is transparency and an increased degree of certainty for the capacity holders?

The decision to split the capacity between South Hook and Dragon would need to be directed by the Authority. This would ultimately mean splitting the ASEP's baseline capacity, which would require a change to our Licence and potentially the UNC. A change like that could provide a degree of certainty, but would also have the potential to be restrictive, reducing flexibility.

7) This issue has only served to further highlight the pre-existing shortfall in transmission system capability versus the firm capacity baseline.

NGG's capacity baselines are set out in the Licence and this defines the level of available firm capacity we should release at each entry point for each gas day. For most Entry Points the baselines are based on the principle that they should closely reflect the maximum theoretical physical capability of the point under peak conditions, and as such, cannot necessarily be met 365 days of the year. As Milford Haven was a new Entry Point, Shippers provided an investment signal via capacity auctions (and bookings) where capacity was typically booked in the winter periods. This, combined with forecast lower flows (via FES or its forerunner) in the summer, and a Licence requirement for us to be economic and efficient, led to greater winter capability.

Importantly, it's also worth noting that the sum of all the entry baselines is roughly double the 1:20 peak day demand and as such all baselines cannot be delivered on the same day. The capability on any given day is dependent upon a number of variables including supply and demand (specifically localised demand) and asset availability and as such capability is not fixed.

Our publications have highlighted that the possibility of constraints at Milford Haven exists both now and into the future in scenarios, especially where national and as such local demand falls and is not matched by a corresponding decrease in the regional entry flows as LNG dependence increases². The South West is a region where, historically, short term physical and commercial actions (constraint management contracts and locational sells on the open market) have been sporadically used to manage flows above physical capability³ since Milford Haven became operational.

Historically we have recognised and managed that risk successfully with constraint management actions. However, due to the current geopolitical situation and its consequential market impacts, we believe that

² Network Capability Annex: <https://www.nationalgrid.com/gas-transmission/document/134776/download>

³ Annual Network Capability Assessment Report (ANCAR): <https://www.nationalgrid.com/gas-transmission/document/135991/download>

there is an increased likelihood of higher LNG flows for a prolonged period of time to support the export of gas to Europe. This could result in flows from Milford Haven exceeding capability for an extended period and as a result, increase uncertainty and costs to customers and ultimately consumers.

8) Why does this proposal include October, which is not traditionally viewed as a summer month?

We have received a number of responses seeking to ascertain why our consultation document included the provision for withholding capacity for the month of October, with a number of respondents citing that this is considered as the commencement of the winter period.

Whilst we acknowledge that this month typical sees industry actors switching to winter contracts, we believe that from the perspective of the physical network the risk associated with potential capacity constraints does not materially reduce between September and October. We have made this judgement based on the broadly equivalent demands observed on the UK gas network between September and October over the last 5 years.

Additionally, should European bulk strategic storage not be at levels considered appropriate for the commencement of winter and/or not be at levels dictated by individual member states, then we believe that October could continue to see extremely high continental export with associated high deliveries of LNG into the UK.

It is worth noting that the level of long term sold capacity in October at the Milford Haven ASEP is much higher than in the summer months and currently stands at 855GWh. This already exceeds the network capability levels for that month.

9) Under this proposed ECR change, it appears that by withholding firm capacity from the market, National Grid is passing the entirety of its constraint management cost risk on to gas shippers and end consumers. This is presented in the change proposal as an overall cost saving.

The aim of the change proposed is to protect our customers and end consumers from excessive constraint management costs. The current gas prices being experienced are unprecedented. In a constraint scenario where we have to take constraint management actions (either locational trades and/or buybacks) for several days, we are likely to exceed the constraint management incentive collar (post sharing factor) of £5.2m within days. Any costs (post sharing factor) incurred above £5.2m will be passed on to our customers (and ultimately end consumers) in its entirety. The details of the cap and collar within the Capacity Constraint Management (CCM) Incentives were decided upon as a part of RII02 discussions. The CCM incentive was not designed to accommodate the unprecedented scenario that we find ourselves in and no one anticipated the war in Ukraine and its impact when the level of risk/cost National Grid participates in was determined. Our key concerns are the potential costs incurred by the industry and consumers and providing greater certainty to the market.

There will still be risks that will need to be handled by National Grid as we will still be managing asset availability and will be releasing capacity at Milford Haven based on the median capability value for each month. Over the last 5 years there have been a large number of days where capability was lower than what we are proposing to release. We will also continue to assess the capability and as such, whether we can release additional capacity in the WSEC and DSEC auctions. For the avoidance of doubt in the WSEC and DSEC auctions we will look to maximise the availability of capacity and therefore access to the network based on the capability at that point.

10) In today's high-priced - and highly-volatile - market environment, shippers' inability to deliver volumes due to short-term capacity reductions will have large financial impacts. This risk, combined with operational uncertainty and constraints, will likely lead to cargos being diverted away from the UK market.

It is not our intention to discourage the supply of LNG to the UK. It is National Grid's opinion that releasing forward capacity up to these levels would offer the most flexibility and certainty to the market, whilst reducing the significant industry cost potential of an ongoing constraint the Milford Haven Entry Point. It is also worth noting that this proposal does not change the capability of the network.

We recognise that the majority of the respondents have a different view and believe that the proposal adversely impacts customers and consumers as the cost of the proposal is greater than the costs of the risk being mitigated by the proposal.

11) Under the terms of the Gas Transporter Licence Special Conditions, NG is required to use reasonable endeavours to release Obligated Entry Capacity at each NTS Entry Point in all available allocations up to the end of the day to which the capacity relates. We consider the removal of this requirement and the isolation of a single entry point to be highly discriminatory against users at that entry point.

The Licence obliges National Grid to run the network in an efficient, economic and coordinated manner (SC 9.19 Part A). Given the unprecedented events and increase in risk, the lack of certainty for customers and the potential impacts on end consumers, National Grid does not believe it economic or efficient to sell capacity where there is such an increased risk of a constraint and increased likelihood that constraint actions need to be taken.

NG's Licence, SC 9.18.5 requires that "The licensee must have in place an Entry Capacity release methodology statement setting out how [NG] offers for sale Obligated Entry Capacity to Relevant Shippers". The proposal is to modify the methodology so that entry capacity is offered on the basis of a reduced capability for the reasons mentioned in the consultation letter.

As there are potentially increased LNG flows this summer to help meet EU storage requirements there is a likely increase in flows at Isle of Grain as well. An increase in flows at the Isle of Grain (or any other entry point), does increase the constraint risk, but the risk is considered within the normal operational management of the network. This is because the particular conditions and circumstances prevailing at Isle of Grain are different from those at Milford Haven (for example higher Bacton Exit flows increase localised demands which in most circumstances increases the capability of the Entry Points in that part of the network). As a result, we believe that applying the change proposed at Milford Haven to Isle of Grain would serve no useful purpose and put unnecessary restrictions on NTS Users.

12) The benefit of this change identified by National Grid will be to reduce the constraint management costs and therefore ultimately lead to reduced costs for consumers, this ignores the potential impact upon supply to the UK and therefore possible increases in wholesale gas prices which could have a far more significant impact.

We acknowledge that when considering the risk related to higher LNG flows at the Milford Haven ASEP, we have predominantly focused on the costs of managing the network in constraint conditions for a prolonged period of time and the impact that might have on our customers and end consumers.

The purpose of the consultation was to flag the increased risk and to allow the industry to provide further information so that any decision is as well informed as possible. We thank the industry for providing

additional supporting information in this area which, undoubtedly, will be considered by Ofgem in the decision-making process.

We understand that the impact on the wholesale price is made upon the assumption that the LNG cargo deliveries coming to the UK will be reduced beyond the technical capability of the entry point. Although LNG deliveries are an element that impacts the GB gas price, we note that such impact is uncertain and variable and highly dependent upon global market availability and demand. For example, the current NBP forward price is trading significantly below TTF as a result of the UK market being oversupplied and constrained in its ability to export to the EU. We also note that a concern was raised in responses regarding the impact of a reduction in the amount of capacity being made available. This has the potential to create a perception of scarcity in the capacity market which could cause a price premium to be paid. We acknowledge that this could occur and could increase costs, however, this needs to be considered against any potential constraint costs.

13) Attention to this consultation was by a single notice issued by the Joint Office of Gas Transporters. While it may be argued that such a notice is adequate for GB gas shippers, we do not believe that it satisfies the requirement to also consult with any other interested parties as required by Special Condition 9.18.10(a)(iii) of National Grid's gas transporter licence. In this scenario, other interested parties are likely to include as a minimum LNG producers, importers and traders who may not be GB gas shippers and may not routinely receive notices from the Joint Office.

National Grid consistently uses the Joint Office of Gas Transporter as a means to distribute industry related communications. This includes consultations and messages related to UNC/methodology developments. We believe that this is a widely recognised form of communication with our customers and all other stakeholders. Any party with an interest in the GB gas industry (including LNG producers, importers and traders) is entitled to sign up to the Joint Office distribution list.

14) As a stakeholder in the ongoing PARCA process, which is being developed alongside the prospective expansion of the South Hook terminal, this proposal causes us significant concern. We now believe that Milford Haven will be proportionately more constrained after the terminal has been expanded and the network reinforced. This is because the network expansion will only meet the new terminal capability under limited circumstances.

As illustrated in the Annual Network Capability Assessment Report⁴, the network re-enforcement proposed as a result of the Milford Haven PARCA will provide more benefit at lower 'summer' demand levels than at higher 'winter' levels. Although the capability level, under unfavourable local demand conditions remains below baseline, we do not anticipate it to be 'proportionately more constrained' than it is at present. Recent analysis, assessment and operational experience under high flow/low demand conditions suggest current capability is likely to be slightly higher than the previously published graphs and there are also additional options under consideration that could further alleviate constraints. These options are being continually assessed through our Network Capability process against expected future flow forecasts to ensure we continue to run an economic and efficient network.

15) National Grid has only quoted one scenario in its consultation letter without sharing the basis of the parameters used to present expected costs ranging from £180m-£500m.

We have revisited the costs documented in the scenario detailing the potential impact high constraint management costs might have over a prolonged period on our customers, and ultimately end consumers.

⁴ <https://www.nationalgrid.com/gas-transmission/document/135991/download>

Gas prices have fluctuated significantly over the last year or so. The scenario we looked at (based on 30 days of constraints, a 20 mcm/d constraint and gas price at £3 per therm and buy/sell differential of £1) estimated the costs to range from £180m (based on locational sells and some corresponding buys on 80% of days) to £500m (buybacks).

We recognise that there are a number of variables that could impact constraint costs and the numbers given were illustrative to provide an order of magnitude and sense of scale associated to any potential constraint costs. The constraint quantity was based on a maximised flow view of circa 85 mcm/d vs a capability of circa 65 mcm/d, the number of days was based on a month. The gas price was based on the gas price at the time – circa £3 per therm. We recognise that gas prices can go up as well as down, and the costs could be impacted by an ongoing constraint (likely to increase costs) which this scenario does not cover. If the current gas price (circa £1.50 within day) was taken into account, the buyback cost would be circa £250m.

It is challenging to forecast the costs of managing constraints as the costs of locational trades and capacity buybacks are heavily dependent on day-to-day market conditions and participant behaviour. Individual participants may have varying motivations for accepting locational trades or capacity buybacks. This behaviour is difficult to predict and so is the physical impact of any commercial actions undertaken which would then impact potential further actions.

We believe that once a significant additional risk was identified it was necessary to articulate the risk alongside a potential solution to the industry in our role as a prudent system operator. We have considered the responses received from the industry and recognised the points and potential consequences raised by respondents. Other than the amendment to the capability numbers and therefore the level of capacity we commit to release, we have not changed our original proposal as in our view both approaches have set out a potential impact on customers and consumers and therefore, they both need to be set out for a decision to be made.

In this response we have tried to address most of the issues raised by the industry. We would appreciate further engagement on the topic via the industry meetings and direct correspondence.

Please note that this response, as well as all non-confidential consultation responses, will be published on our website on Wednesday, 4th May 2022 under: [0https://www.nationalgrid.com/gas-transmission/capacity/capacity-methodology-statements](https://www.nationalgrid.com/gas-transmission/capacity/capacity-methodology-statements).

Your sincerely

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