Exit Capacity Development

Presentation to Ofgem Exit and Balancing Workstream

28 Jan 2004

National Grid Transco

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Background

- Weaknesses recognised in existing interruptible arrangements
- Amendment to Transco's GT licence introduced in April 2002 :

  "The licensee shall use all reasonable endeavours to ensure universal firm registration of NTS exit capacity with effect from 1 April 2004"

  "Universal firm registration means that all NTS exit capacity is registered free from exit capacity curtailment rights"
- Ofgem requested scope of reform widened to include LDZ interruptible arrangements
- Implementation date extended to "as soon as is reasonably practicable after 1 April 2004" (referring to 1 April 2005 as an indicative implementation date)

Ofgem Objectives for Exit Capacity
- Described in Letter to the Industry 27 May 03

- Cost reflective pricing, non-discrimination and removal of cross subsidies
  - Firm customers pay too much
- Transco determined (quantity of) interruption
  - Free-loading to be avoided by NGT rationing of interruptible contracts
- Increased customer choice
  - Flexible arrangements, probability or duration of interruption?
- Investment signals
  - Trade-offs between interruption, LNG and investment
- Safe and secure pipeline system
  - HSE should be satisfied that new arrangements are at least as good as old
- LDZ separation or sale
  - Robust to potential future divestment

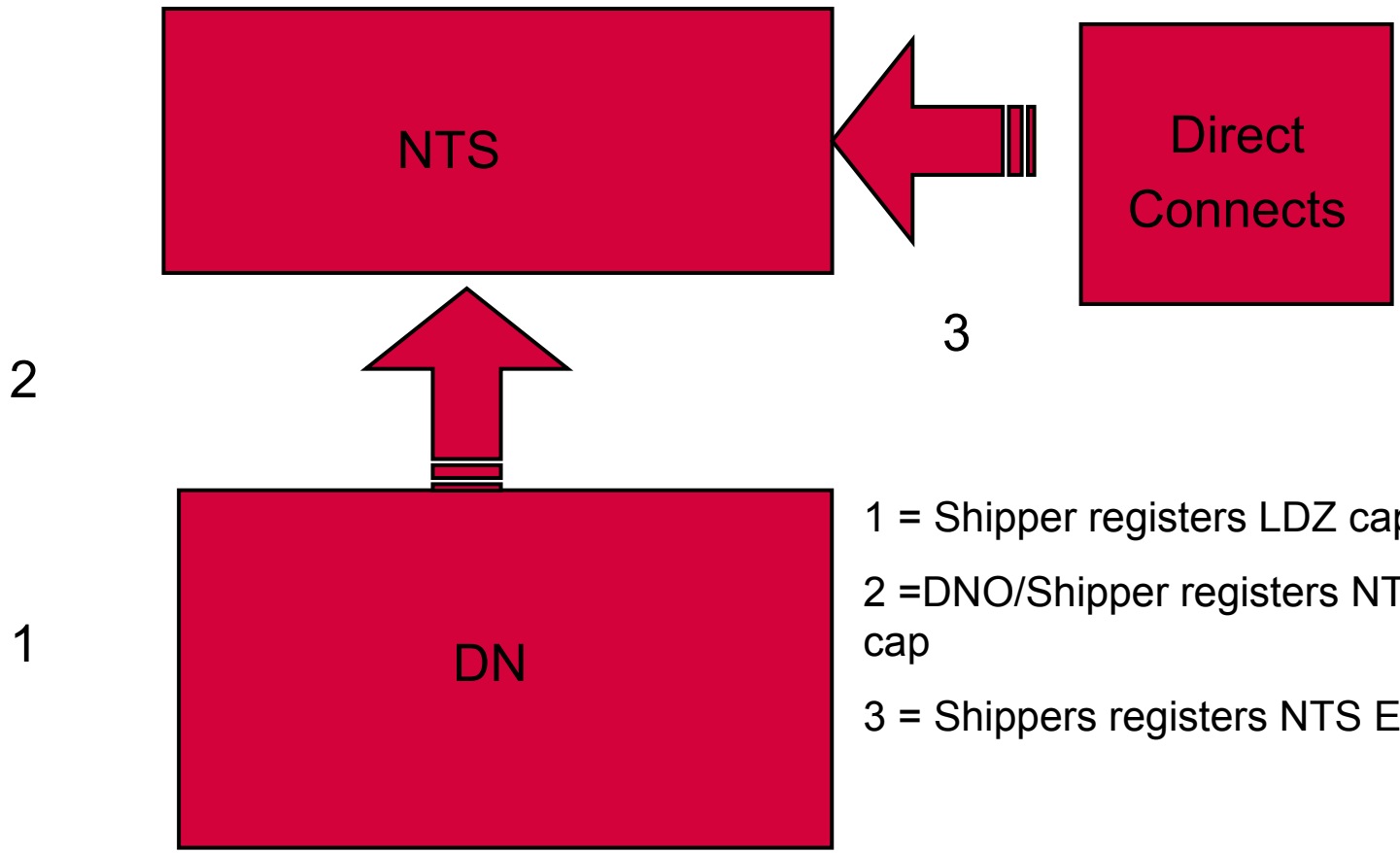
LDZ Interruption - Regime Reform History

- 1998 – 99 Discussion Paper NCD1 published; Interruption Seminars; Interrruption Questionnaire
- Consultation Paper PC39 – Transco Review of Interruptible Services (May 1999)
- Ofgem Decision on PC39 (July 1999) – veto of proposals
- Ofgem Review of Interruptible Services (2000)
- Discussion Paper PD15 (Nov 2001) – variable and/or flexible service
- Ofgem SO proposals (2001/2) – 15 day regime
- Transco GT Licence – Universal Firm NTS Exit (Jul 02)
- Workstream Development (Sep 02 – date)
- Ofgem review (May/June 03)

Principles of reform

- Enable more flexible capacity management at exit
- Reveal 'value' of transportation interruprtion.
- Provide better investment signal
- More imaginative demand side solutions
- Licence compliance

Elements For Reform



1 = Shipper registers LDZ cap

2 =DNO/Shipper registers NTS Exit cap

3 = Shippers registers NTS Exit cap

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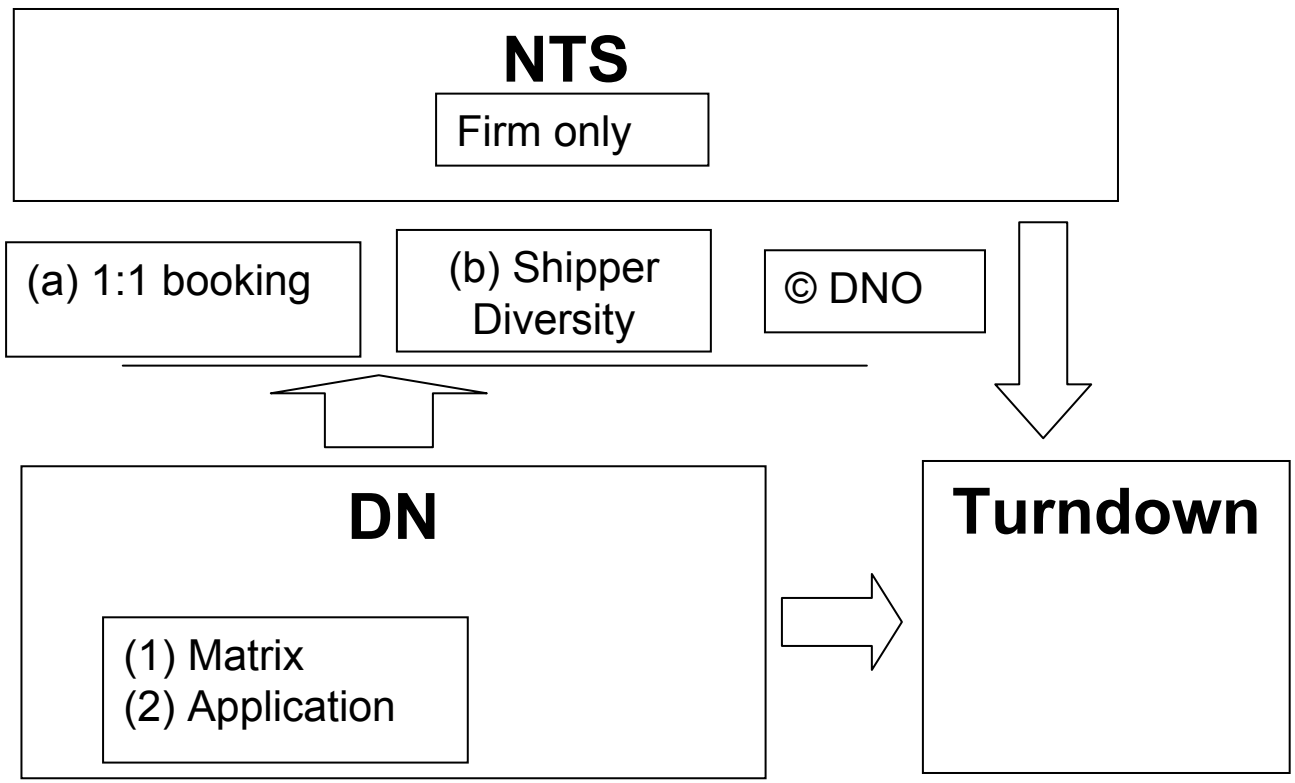
Development Permutations



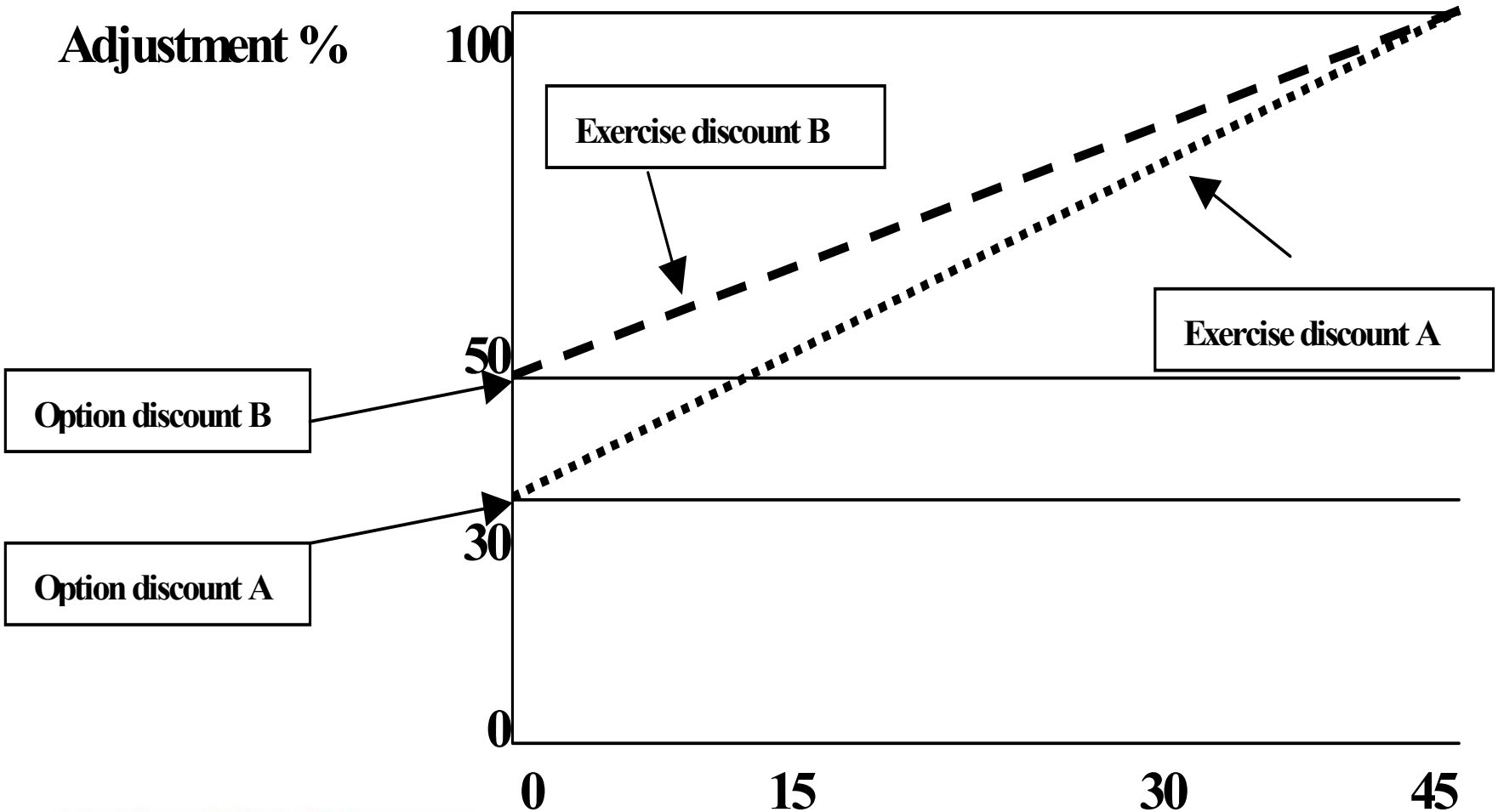
DN Solution

- Retain administered charge approach.
  - Conditions for a market approach not favourable.
- Process operated ahead of gas year.
- Matrix approach requires Transco to choose the number of days exposure to interruption for each site.
- Application approach requires shipper to nominate preferred exposure and Transco accepts/amends or rejects the application.
- Both approaches require transition arrangements in the event that an interruptible site is no longer required.

DN Arrangements

- Firm exit capacity booking arrangements to apply
- Interruptible to firm switching
  - existing arrangements to apply outside of annual application process
- Firm to interruptible switching only to occur in the annual application process
- Interruption prices based on option exercise scheme
  - Option fee is upfront cost
  - Exercise fee payable on each occurrence of interruption
  - Pricing methodology to be published in the Transportation Statement

Option and Exercise Regime



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Application Process

- (Shipper) choice of option fee can differentiate the probability that supply point will be called or interruption
- Applications for interruptible LDZ Capacity and management of interruption continues on a supply point basis
- Applications for interruptible LDZ capacity occur each year ahead of Gas Year e.g. June for an October Gas Year

High Level Principles

- Shippers are able to apply for “n” days of interruption
  - [n could be 5, 15, 25, 35, 45 for instance]

- Transco can reject number of days requested where n < 45 if in aggregate insufficient days of interruption have been applied for
  - Transco then consider each application in turn and adjust applicable days to a default (previous year accepted value) starting with highest price and progress through stack until volume has been attained
  - No other terms will be adjusted

- Transco can reject an application for interruptible capacity if it is not required to maintain its required transportation

DN Default Conditions etc

- All DM sites (firm and interruptible) can apply for interruptible capacity
  - Mandatory for existing interruptible sites to be considered in the annual process
  - Shippers can nominate terms (option/exercise) or default conditions can apply
  - Default – terms in place for the present year form the application for the next year
  - Default application in first year
    - 0% discount factor
    - 45 days duration
    - 1 year contract period
- Shippers can register for multiple year [5] interruption terms
- The number of days for interruptible rights may be determined by Transco where this is greater than the duration requested by the Shipper

DN – Acceptance criteria

- Transco can reject an application for interruptible capacity if it is not required to maintain its required transportation capability
  - By ranking applications in price order
  - Price = option discount * exit capacity charge
  - Accept lowest priced application first
  - Progress through stack until required volume obtained

- Revised interruption arrangements described here do not supersede the established emergency arrangements in Section Q of the Network Code

Application Acceptance – Broad Principles

Application sequence	% discount	Option Price	Exercise Price	Exercise sequence
Accept last	100%	P_6	E_1	Exercise first
	80%	P_5	E_2	
	60%	P_4	E_3	
	40%	P_3	E_4	
	20%	P_2	E_5	
Accept first	0%	P_1	E_6	Exercise last

Contracting Across NTS/network Boundary

- Consider 3 different scenarios :

Scenario A - limited change

ie. Transco books NTS (firm) & LDZ (firm & int.) Capacity on behalf of shippers, at a level equal to the aggregate of capacity requirement for supply points (ie E SOQ)

Scenario B – DM diversity

ie. Transco informs shippers of their registered SOQ values, and shippers book level of NTS & LDZ capacities, taking into account diversity

Scenario C – NGT contracts with DNO (downstream network operator)

Contracting Across the Boundary

- DNO option has found most favour so far.
- DNO aggregates demand within its DN.
- Takes a view on how much NTS exit capacity is required.
- Books the capacity.

- Charging methodology required to pass costs through.
- Incentive to book efficient levels of capacity?
- Tension between shipper/operator role?

Universal NTS Firm

- Need for universal firm is not widely accepted.
- NTS only.
- Interruption replaced with turn-down contracts.
- Administered prices continue.
- Specific rules introduced for NTS CSEPs, storage sites & shared supply meter points (SSMPs).

NTS Direct Connects – Proposed Process

1. Shippers book.
2. Annual duration (12 monthly blocks) / monthly duration.
3. Booked capacity $\not>$ phys.Max. (In NExA), but > BSSOQ.
4. No voucher scheme.
5. Overrun charges apply (for SSMPs on an aggregate basis.
6. Daily product available ?

Turn-down Contracting

- NGT to contract with shippers/consumers, via tender process
- Level of NTS exit capacity unchanged
- 3 years out (not agreed by NC workstream)
- Ranked in price ascending order
- Governance contained in procurement guidelines
- Novel solutions may be considered.

Contractual/regulatory Changes

- Gas act
- GT licence
- IECR (inc. Entry …)
- Procurement guidelines
- Network code
- Transportation charging statement
- Safety case

Debating Points

- Why change?
- Should the NTS be firm only?
- Should/ how can consumers be involved?
- Should administered price process apply in DN?
- Should market approach necessitate a 3-year lead time for contracting?
- Should the DNO have a role?