

To all interested parties and stakeholders,

Email: energy.securityofsupply@ofgem.gov.uk

Date: 7 September 2022

Decision further to National Grid Gas plc's request for Derogation from Special Condition 9.22 (Implementing and maintaining the Demand Side Response Methodology for use after a Gas Balancing Notification) of its Gas Transporter Licence

We¹ write further to National Grid Gas plc's ("NGG") application to Ofgem, dated 5 September 2022, requesting a derogation pursuant to Special Condition 9.22.12 of NGG's Gas Transporter Licence (the "Licence")² in respect of the Gas Demand Side Response ("DSR") Methodology.

This letter sets out our decision to grant the requested derogation for NGG to consult on revisions to the DSR Methodology for not less than 10 days instead of for not less than 28 days as currently required under Special Condition 9.22.5 of NGG's Licence, in accordance with Special Condition 9.22.12 of NGG's Licence. The direction, which appears annexed to this letter, will give effect to this derogation decision (subject to the conditions specified therein).

Background

Part B of Special condition 9.22 in the Licence sets out the requirements and process NGG must follow in reviewing and revising the DSR Methodology. NGG may only revise the DSR Methodology in accordance with Part B of Special Condition 9.22 unless a derogation from these requirements is applied for and granted under Special Condition 9.22.12.

¹ References to the "Authority", "Ofgem", "we" and "our" are used interchangeably in this document to refer to GEMA, the Gas and Electricity Markets Authority. The Office of Gas and Electricity Markets (Ofgem) supports GEMA in its day-to-day work. This decision is made by or on behalf of GEMA.

² National Grid Gas plc, Gas Transporter Licence, Special Conditions:
<https://epr.ofgem.gov.uk/Content/Documents/National%20Grid%20Gas%20Plc%20-%20Special%20Conditions%20Consolidated%20-%20Current%20Version.pdf>

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NGG has identified the need to revise the DSR Methodology and has requested a derogation in respect of Special Condition 9.22.5, which requires that before revising the DSR Methodology the Licensee must consult for a period of 28 days in which interested parties can make representations to the Licensee.

UNC822

On 5 September 2022, NGG raised Uniform Network Code³ ("UNC") modification UNC822: '*Reform of Gas Demand Side Response Arrangements*'.⁴ UNC822 is a proposal to modify the UNC with the intention to include provisions within the UNC for NGG to administer an invitation to offer process for DSR, introduce option payments to Users who will subsequently arrange with consumers to provide DSR, and extend the lead-time within which NGG may accept DSR offers.

The current DSR arrangements provide a mechanism for large consumers of gas to offer to reduce their demand in return for a payment during times of system stress, which the Licence defines as being when a Gas Balancing Notification ("GBN") is in operation. At this point, a User may post a quantity of DSR, known as a DSR Market Offer, onto the On-the-Day Commodity Market ("OCM") on behalf of a consumer.

However, NGG has informed us that the stakeholder feedback they have received suggests that the current arrangements do not sufficiently incentivise Users to reduce their demand. Therefore, reform is needed to make the DSR product more attractive to encourage its take-up so that the scheme can be utilised within this winter and subsequent winters if required.

Derogation request

NGG has requested a derogation in accordance with Special Condition 9.22.12 of NGG's Licence from the requirement to consult for 28 days as stipulated in Special Condition 9.22.5 of NGG's Licence. NGG have requested to reduce the consultation period to 10 days in order to consult on changes to the DSR Methodology on the same timetable as UNC822.⁵

Our Views

We agree that it is appropriate to consider options to enhance the DSR tool on a shortened timescale so that the DSR tool is more likely to be effective if needed this winter and beyond. We acknowledge the uncertainty created by the Russian invasion of Ukraine and of

³ The Uniform Network Code sets out the transportation arrangements between licensed gas transporters and gas shippers, as required by Standard Special Condition A11 of the Gas Transporters Licence: Network Code and Uniform Network Code.

⁴ <https://www.gasgovernance.co.uk/0822>

⁵ The Authority has granted urgency to UNC822 with a 10 day industry consultation period: <https://www.gasgovernance.co.uk/0822>

the current high and volatile gas prices and consider it is prudent to take additional mitigations, at pace, in case a margins notice and/or GBN is issued by NGG. Further, we understand that the DSR tool, in its current form, may not be effective in incentivising DSR Market Offers and that enhancing the tool could provide valuable demand reduction preventing or lessening the impact of a Gas Deficit Emergency. Therefore, we consider this to be a potentially valuable tool for security of supply and consider it appropriate to shorten the timetable to allow any changes, if approved, to be in place for this winter.

We have considered the impact and effect on consultees of a 10 day consultation period. We acknowledge the industry engagement that NGG has conducted with both UNC parties and representatives from large manufacturing industry to inform its development⁶ and consider that 10 days provides a sufficient period for consultees to provide reasoned views on NGG's final proposals. We consider that the potential benefits of a change to DSR for this winter are sufficient to warrant the shortened consultation period. All possible efforts should be made to ensure that the time is used well, that stakeholders who might otherwise experience difficulty engaging in the consultation are proactively approached, and that the analysis is sufficient to properly inform an Ofgem decision.

We have decided to grant NGG's derogation request so they may consult for a period of not less than 10 days, so that the review of the DSR Methodology can mirror the shortened timetable of UNC822. Nothing in this letter in any way fetters the discretion of the Authority in relation to our decisions as to whether to approve UNC822 and the DSR methodology when sent to the Authority for decision. UNC822 will be assessed according to the UNC Relevant Objectives once the FMR is sent to the Authority for decision. The DSR Methodology will be assessed according to the Licence once it is sent to the Authority for decision.

Our decision

We have reviewed NGG's derogation request submitted to us on 5 September 2022 and, in accordance with Special Condition 9.22.12, we have decided to grant the requested derogation to NGG to consult for less than 28 days on its proposed revisions to the DSR Methodology, but no less than 10 days as specified in our direction annexed to this letter. The direction, which is issued in the Annex to this letter, will give effect to the derogation decision.

⁶ Pg 4 of Modification 0822: <https://www.gasgovernance.co.uk/0822>

This letter constitutes notice for the purpose of section 38A of the Gas Act 1986 of the Authority's reasons for its decision to grant the derogation by direction, and a copy has been made available on our website.

Dr Adrian Richardson

Head of Energy Security of Supply

For and on behalf of the Gas and Electricity Markets Authority

ANNEX - Direction Notice

To: The Company Secretary, National Grid Gas plc

Derogation by Direction issued to National Grid Gas plc by the Gas and Electricity Markets Authority pursuant to paragraph 9.22.12 of Special Condition 9.22 Part D of the Gas Transporter Licence in respect of implementing and maintaining the Demand Side Response Methodology for use after a Gas Balancing Notification.

1. This derogation by Direction is issued by the Gas and Electricity Markets Authority (the "Authority") under paragraph 9.22.12 of Special Condition 9.22 Part D of the Gas Transporter Licence in respect of the NTS (the "Licence"), granted or treated as granted under section 7 of the Gas Act 1986 (the "Act") to National Grid Gas plc (the "Licensee").
2. Paragraph 9.22.2 of Special Condition 9.22 provides that the Licensee must have in place and maintain a Demand Side Response Methodology approved by the Authority.
3. Paragraph 9.22.5 of Special Condition 9.22 provides that the Licensee must allow a period of not less than 28 days in which interested parties can make representations to the Licensee.
4. Paragraph 9.22.12 of Special Condition 9.22 provides that the Licensee may apply to the Authority for a derogation relieving the Licensee of any of its obligations under this condition.
5. The Authority hereby directs under paragraph 9.22.5 of Special Condition 9.22 of the Licence as follows, that the Licensee must:

"allow a period of not less than 10 days in which interested parties can make representations to the Licensee;"
6. The considerations and reasons for the Authority's decision, in accordance with the Authority's duty under section 38A of the Act to give reasons, are set out in the Authority's decision letter to the Licensee, dated 7 September 2022.
7. The Direction shall take effect on and from 7 September 2022 and remain in effect until the conclusion of the governance process for UNC822, unless revoked earlier or varied in writing by the Authority.

8. The Authority may revoke or vary this direction upon reasonable notice in writing to the Licensee.

Dated: 7 September 2022

Signed for and on behalf of the Authority

Dr Adrian Richardson

Head of Energy Security of Supply

Authorised for that purpose by the Authority