

**Initial proposals on transitional incentive
schemes supporting the offtake
arrangements**

September 2005

Summary

This document sets out Ofgem's initial proposals on the scope, form and duration of the incentive schemes necessary to support the offtake arrangements proposed for National Transmission System (NTS) exit capacity in the period from October 2008 to September 2010 (the "transitional" period). This follows the sale by National Grid Transco (NGT) of four of its gas distribution network (DN) businesses and the Authority's decision, in June 2005, to delay the implementation of the enduring offtake arrangements to September 2007 for the release of NTS offtake rights from 1 October 2010¹.

Proposed transitional offtake arrangements

In August 2005, Transco NTS raised Uniform Network Code (UNC) Modification Proposal 0046 (and an associated consultation on changes to relevant supporting documents²), outlining details of a proposed process through which firm capacity (held by NTS direct connects) and NTS offtake capacity (held by DNs) could be allocated for the period 1 October 2008 to 30 September 2010³. It is important to note that the contents of these consultations should not be interpreted in any way as fettering the discretion of the Authority to accept or reject this modification proposal.

Under the proposals, DNs will be required to request their *total* requirements for NTS exit rights for the gas year 2008/09 (i.e. for the first year of the transitional period) in October 2005⁴ and for gas year 2009/10 (i.e. the second year of the transitional period) in June / July 2006.

In the event that these requests require Transco NTS to undertake any investment to deliver the level of NTS exit rights requested by a DN at any NTS offtake point (or group of NTS offtake points), then DNs will be required to enter into a contractual agreement with the NTS. This will outline the volume of NTS exit rights the DN requests from the NTS, the date at which these rights are required, and also outline the financial implications of either party defaulting on the terms of the agreement.

¹ 151/05, Ofgem open letter on enduring offtake arrangements, June 2005

² Consultation on the Incremental Exit Capacity Release (IExCR) Methodology Statement and SC4B Licence Statements to support the Transitional Gas Exit Capacity Arrangements proposed in UNC Modification Proposal 0046

³ UNC Modification Proposal 0046, Extension of the sunset clauses for registration of capacity at NTS exit points, August 2005.

⁴ or two weeks after implementation of the modification proposal if this is different.

Proposed transitional incentive schemes

Ofgem does not consider it appropriate to extend all of the incentive schemes currently applying to Transco NTS and the DNs into the transitional period at this time.

Accordingly,

- ◆ the current “greater than 15 day interruptions” DN incentive for the duration of the transitional period will instead be reviewed at the time of the next Gas Distribution Price Control Review (GDPCR); and
- ◆ NTS exit incentives for the transitional period will rather be defined at the time of the next Transmission Price Control Review (TPCR) (to be implemented in April 2007) to enable incentives to be set following the discovery of additional performance data through the operation of the interim scheme and to enable Ofgem to consider more fully all interactions between entry and exit.

However, Ofgem considers it necessary to specify incentives for the DNs for the duration of the transitional period to mitigate a tendency for DNs to overbook NTS exit rights. Ofgem proposes a single “sliding scale” incentive mechanism for each DN for the duration of the transitional offtake arrangements, with the specification of a single cost performance measure and target (for each DN) covering both NTS offtake (flat) capacity and NTS offtake (flexibility) capacity, as well as a defined cap, collar and sharing factors.

Ofgem proposes that cost performance targets, consistent with the 1 in 20 obligation of each DN, are specified for NTS offtake (flat) capacity and NTS offtake (flexibility) capacity for each DN (for the formula years 2009/10 and 2010/11), with both products priced at the prevailing (outturn) price of NTS exit capacity.

Ofgem’s initial proposal is that caps and collars for DN cost performance measures should continue to be calculated as a fixed percentage of each DN’s cost performance target reflecting the locational nature of both exit charges and demand and ensuring that incentive schemes are accurately targeted across the network. Furthermore, Ofgem’s initial proposal is that the incentive parameters that currently apply to the DNs are extended to cover the two years of the transitional period. These parameters are presented in Table 1.

Table 1 Parameters for DN incentive schemes

	Cap and Collar (% of each DN target)		Sharing factors	
	Cap	Collar	Upside	Downside
Proposed incentive parameters	7.5%	-7.5%	100%	100%

Way forward

Ofgem envisages publishing Final Proposals on the transitional incentive arrangements in early November 2005 following consideration of responses to this Initial Proposals consultation. This document will include a formal consultation under section 23 of the Gas Act on proposed licence modifications necessary to implement these proposals, allowing the transitional incentive arrangements to be finalised by the end of November 2005.

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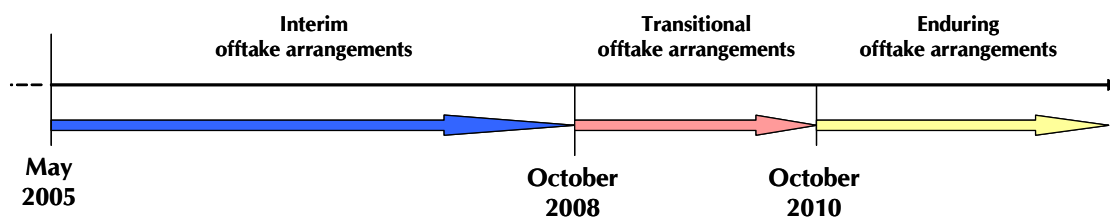
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1. Introduction

Overview

- 1.1. This document sets out Ofgem’s initial proposals on the scope, form and duration of the incentive schemes necessary to support the offtake arrangements proposed for the National Transmission System (NTS) in the period from 1 October 2008 to 30 September 2010. This follows the implementation of “interim” incentive arrangements for NTS offtake rights for the period to 30 September 2008 and the Authority’s subsequent decision, in June 2005, to delay the implementation of the “enduring” offtake arrangements by two years to September 2007 for the release of NTS offtake rights applicable from 1 October 2010 onwards.⁵
- 1.2. Given the Authority’s decision to delay the implementation of the long term “enduring” offtake arrangements by two years, it has been necessary to consider the arrangements for the allocation of NTS offtake rights to NTS connectees (that is the Distribution Networks (DNs) and customers directly connected to the NTS), for the period between 1 October 2008 (the time at which the interim arrangements end) and 1 October 2010 (the time at which the enduring arrangements begin).
- 1.3. References to the “transitional” arrangements within this document are references to the arrangements proposed for this two year period. The incentives associated with these “transitional” arrangements are the subject of this consultation. The sequencing of these alternative offtake arrangements is illustrated in Figure 1.1 below.

Figure 1.1: Offtake arrangements going forward



⁵ 151/05, Ofgem open letter on enduring offtake arrangements, June 2005
Initial proposals on transitional incentive schemes supporting the offtake arrangements
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- 1.4. Ofgem considers that the proposed incentive schemes to support the transitional offtake arrangements should primarily be designed to protect the interests of customers (who ultimately pay the costs of system operation) and provide the network businesses with an appropriate balance of risk and reward. For example, the incentive schemes will, among other things, need to ensure that the DNs book a level of NTS exit rights appropriate to their licence and statutory obligations.

Structure of document

- 1.5. This document has four further chapters:
- ◆ Chapter 2 provides background to the proposed NTS and DN incentive schemes, including an outline of the DN sales process and a summary of the current relevant incentives applicable to the NTS and DNs;
 - ◆ Chapter 3 describes the proposed transitional offtake arrangements and provides an overview of a number of aspects of the arrangements directly related to NTS and DN incentive schemes;
 - ◆ Chapter 4 describes Ofgem's initial proposals on the proposed transitional incentive schemes; and
 - ◆ Chapter 5 describes the proposed way forward.

Views invited

- 1.6. Ofgem welcomes views on all aspects of this consultation, to be received by close of business on 19 October 2005. Respondents are asked to provide views in a timely manner. Responses should be addressed to:

Mark Feather

Office of Gas and Electricity Markets

9 Millbank

London SW1P 3GE

(Telephone: 020 7901 7412)

- 1.7. Electronic responses may be sent to matteo.guarnerio@ofgem.gov.uk

- 1.8. Respondents are free to mark their reply as confidential, although we would prefer, as far as possible, open responses that can be placed in the Ofgem library. Ofgem would also prefer that non-confidential responses are sent electronically so that they can be placed on the Ofgem website.
- 1.9. If you wish to discuss any aspect of this paper, Matteo Guarnerio (telephone 020 7901 7493) or Mark Feather (telephone 020 7901 7437) would be pleased to help.

Consultation code of practice

- 1.10. If respondents have comments or complaints about the way this consultation has been conducted these should be sent to:

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London SW1P 3GE

(Telephone: 020 7901 7085)

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Related consultation documents

- 1.11. The following consultations are related to this consultation, and discussed further in Chapter 3:
- ◆ UNC Modification Proposal number 0046: Extension of the Sunset Clauses for Registration of Capacity at NTS Exit Points – this consultation has recently closed; and
 - ◆ Consultation on the Incremental Exit Capacity Release (IExCR) Methodology Statement and SC4B Licence Statements to support the Transitional Gas Exit Capacity Arrangements proposed in UNC Modification Proposal 0046 – this consultation closes on 22 September 2005.

Way forward

- 1.12. Ofgem envisages publishing Final Proposals on transitional incentive arrangements in early November 2005 following consideration of respondents' views to this Initial Proposals consultation. This Final Proposals document will include a formal consultation under section 23 of the Gas Act on proposed licence modifications necessary to implement these proposals, allowing the transitional incentive schemes to be finalised by the end of November 2005.

2. Background

2.1. This chapter sets out the regulatory background relevant to the development of the proposed transitional incentive schemes. It presents an overview of:

- ◆ the regulatory process associated with Transco's sale of four of its DNs⁶;
- ◆ the implementation of interim offtake arrangements; and
- ◆ the implementation of the interim incentives.

DN sales process

2.2. In May 2003, Transco publicly announced that it would consider the sale of one or more DNs, were this to maximise shareholder value (with any such sale requiring the consent of the Authority, the Health and Safety Executive (HSE) and the Secretary of State for Trade and Industry).

2.3. In July 2003, Ofgem commenced a period of consultation on the regulatory, commercial and operational changes required to facilitate the sale of one or more DNs.⁷ This consultation process occurred through a number of regularly held industry workgroups (primarily the Development and Implementation Steering Group), and the publication of a number of Regulatory Impact Assessments (RIAs) and consultation documents, which are discussed in further detail below.

2.4. Following this process of extensive consultation, in January 2005, the Authority granted its conditional consent to the disposal by Transco of four of its DNs. In April 2005, the Authority met to consider whether the conditions precedent to hive-down had been met, and determined that hive-down of the assets to four wholly owned Transco subsidiaries could take place.

⁶ Full details of the regulatory process associated with Transco's DN sales and copies of all documents published by Ofgem can be found in the gas distribution networks sale area of work on Ofgem's website (<http://www.ofgem.gov.uk>).

⁷ *National Grid Transco – Potential sale of network distribution businesses, A Consultation Document*. Ofgem, July 2003.

- 2.5. Following hive-down on 1 May 2005, the Authority met again to establish whether the conditions subsequent had been met to allow share sale to proceed, following which it granted its unconditional consent to share sale, which took place on 1 June 2005. These Authority decisions are discussed in more detail below.
- 2.6. The remainder of this section provides an overview of the key elements of the DN sales process, including:
- ◆ the role of workgroups;
 - ◆ Regulatory Impact Assessments (RIAs); and
 - ◆ key Authority decisions.

Role of workgroups

- 2.7. In January 2004, Ofgem established a number of workgroups as part of the consultation process for DN sales. These included a Development and Implementation Steering Group (DISG), a Commercial Interfaces Workgroup (CIWG), a Regulatory Architecture Workgroup and an Agency Workgroup.
- 2.8. These groups, which were chaired by Ofgem (and which were conducted on a non-binding informal basis without in any way fettering the Authority's discretion), were composed of a diverse representation of interested parties including shippers, customers, potential buyers of the DNs and NGT. The groups commenced work in January 2004 and made considerable progress in clarifying the way in which a divested industry model could operate were the sales of the DNs to proceed (and subject to any necessary licence modifications). In particular, the groups provided a significant contribution to the development of the proposed offtake arrangements.

Regulatory Impact Assessments

- 2.9. Between April and June 2004, Ofgem consulted upon a series of Regulatory Impact Assessments (RIAs) on the regulatory, commercial and operational arrangements necessary to protect customers within a divested industry structure. These included:

- ◆ Agency and Governance Arrangements RIA, published in April 2004;
- ◆ Allocation of Roles and Responsibilities between Transmission and Distribution Networks RIA, published in April 2004;
- ◆ Offtake Arrangements RIA, published in June 2004; and
- ◆ Interruption Arrangements RIA, published in June 2004.

2.10. Following consideration of responses from industry participants and other interested parties, decision documents detailing the Authority's conclusions with respect to these issues were published. The conclusions regarding the "Agency and Governance" and "Roles and Responsibilities" RIAs were issued in May 2004⁸, and in respect of the Interruption and Offtake Arrangements in August 2004⁹.

2.11. Of primary importance to this consultation document are the conclusions of the Offtake Arrangements RIA. At a high level these were that, for the enduring arrangements:

- ◆ **NTS exit rights should be allocated according to an "NTS connects booking model"**. This means that DNs would have responsibility for determining the amount of NTS exit rights that would be required at each NTS/DN offtake point, consistent with their 1 in 20 obligations. This was in contrast to other models considered, in which, for example, it was the responsibility of shippers representing DN connectees to book NTS exit rights, or in which it was the responsibility of the NTS to allocate rights to NTS connectees; and
- ◆ **NTS offtake flexibility should be allocated on a commercial basis between NTS connectees**. As a consequence of this, in the enduring

⁸ *National Grid Transco – Potential sale of gas distribution network business, Allocation of roles and responsibilities between transmission and distribution networks*, Ofgem, May 2004, 119/04 and *National Grid Transco – Potential sale of gas distribution network business, Agency and governance arrangements*, Ofgem, May 2004 120/04

⁹ *National Grid Transco – Potential sale of gas distribution network business, Offtake arrangements, Conclusions document on framework*, Ofgem, August 2004, 199/04 and *National Grid Transco – Potential sale of gas distribution network business, Interruptions arrangements, Conclusions document on framework*, Ofgem, August 2004 198/04

arrangements, flexibility will be made available as a separate product to all NTS connectees.

2.12. In November 2004, Ofgem published a Final IA¹⁰, which set out:

- ◆ a proposed framework for regulatory, commercial and operational arrangements that would be necessary to protect the interests of consumers were the sale of DNs to proceed. This framework built upon each of the decisions set out in previous RIAs; and
- ◆ Ofgem's analysis of the estimated potential costs and benefits that customers are likely to accrue in the event that the proposed sale of the DNs proceeded.

2.13. This document also concluded that, until implementation of the enduring arrangements, short term arrangements (termed "interim arrangements") would be put in place by NGT such that in this period:

- ◆ all NTS connectees would be able access the amount of NTS exit rights they require, subject to NGT's licence and statutory obligations;
- ◆ interruptions arrangements would continue largely unchanged, other than that all currently interruptible customers would have the ability to apply to become firm should they so wish; and
- ◆ arrangements for the provision of capacity to DN connectees would not be reformed through the DN sales process.

2.14. Ofgem invited views from interested parties on all aspects of the Final IA. Summaries of responses to the Final IA were provided to the Authority in order to inform its decision on DN sales.

Key Authority decisions

2.15. On 20 January 2005, the Authority met to consider Transco's application to dispose of DN assets to four wholly owned subsidiary companies, the shares in which would subsequently be sold to third party purchasers.

- 2.16. At its meeting of 20 January 2005 the Authority:
- ◆ granted its consent to Transco's applications to dispose of DN assets under Amended Standard Condition 29 of its original GT licence and Paragraph 3 Schedule 3 to the Gas Act; and
 - ◆ endorsed the previous decisions that it had reached in 2004 regarding the regulatory, commercial and operational framework that would be necessary to protect the interests of customers in the event that the sale of one or more DNs proceeded.
- 2.17. However, the Authority also concluded that the implementation of the enduring offtake arrangements need not occur prior to the completion of the DN sales transaction. Instead, the Authority decided that customer interests would be protected so long as the enduring offtake arrangements were implemented by September 2005.
- 2.18. In order to achieve the implementation of the enduring offtake arrangements by September 2005, the Authority imposed certain conditions to its consent that had to be met before Transco could be permitted to hive down its DN assets to its wholly owned subsidiary companies, scheduled to occur on 1 May 2005. Furthermore, to progress the development of the enduring regime, in February 2005, Ofgem published an Initial Thoughts document on the form, scope and duration of the enduring incentive schemes for the NTS and DNs¹¹.
- 2.19. All conditions were met and Transco hived down its DN assets to its wholly owned subsidiary companies on 1 May 2005.
- 2.20. On 25 May 2005, the Authority determined that the conditions to its consent had been sufficiently satisfied to allow share sale to proceed on 1 June 2005 and issued a direction consenting to the sale of the entire issued share capital of each of the relevant wholly owned Transco subsidiaries as follows:

¹⁰ *National Grid Transco, Potential sale of gas distribution network businesses, Final Impact Assessment.* Ofgem, November 2004, 255/04a

¹¹ 79/05 - National Grid Transco – Potential sale of gas distribution network businesses: Initial proposals on interim incentive schemes supporting the offtake arrangements, Ofgem Initial proposals on transitional incentive schemes supporting the offtake arrangements
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Distribution Network	Blackwater Company	Purchaser
North of England DN	Blackwater F Limited (now Northern Gas Networks Limited)	Northern Gas Networks Limited
Scotland DN	Blackwater SC A Limited (now Scotland Gas Networks Limited)	Scotia Gas Networks plc
South of England DN	Blackwater G Limited (now Southern Gas Networks Limited)	Scotia Gas Networks plc
Wales & West DN	Blackwater 2 Limited (now Wales and West Utilities Limited)	MGN Gas Networks (Senior Finance) Limited

- 2.21. On 24 June the Authority reviewed its previous decision to require the implementation of the enduring offtake arrangements by 1 September 2005 and decided that implementation should be delayed until September 2007¹², thus enabling further consultation against the detail of these arrangements.
- 2.22. The Authority concluded that a revision to the timetable would be consistent with the principles of better regulation and would also provide additional time for it to consider a number of important interactions between the NTS offtake arrangements and the NTS entry capacity regime as part of the forthcoming NTS price control review.

Interim offtake arrangements

- 2.23. The interim offtake arrangements (as currently described in the UNC) were originally defined in such a way as to be consistent with the underlying principles for the allocation of offtake capacity outlined in the Final IA¹³.
- 2.24. As such, the interim offtake arrangements outlined in this section relate to:
- ◆ NTS exit capacity and NTS offtake (flat) capacity;
 - ◆ NTS offtake (flexibility) capacity;¹⁴ and

¹² 151/05, Ofgem open letter on enduring offtake arrangements, June 2005

¹³ National Grid Transco – Potential sale of gas distribution network businesses, Final Impact Assessment, November 2004, 255/04a, page 65

- ◆ interruptible access to the NTS.

NTS exit capacity and NTS offtake (flat) capacity

- 2.25. Under the interim offtake arrangements (and consistent with the “Option 2” model for offtake arrangements as described in the Offtake Arrangements RIA¹⁵), each DN is required to ensure that it has a sufficient level of NTS offtake rights to meet its 1 in 20 planning obligation. This 1 in 20 obligation applies to each DN and means that sufficient capacity must be made available such that the peak aggregate daily demand for gas to be conveyed to premises is only likely to be exceeded on one or more days in one year in every 20 years¹⁶.
- 2.26. For each of the years in the interim period (1 May 2005 – 30 September 2008), the DNs have been allocated an amount of NTS offtake (flat) capacity for each offtake point consistent with each DN’s 1 in 20 obligation.
- 2.27. DNs are able to secure additional NTS exit rights through an annual release of additional offtake rights, facilitated by Transco NTS. To the extent that the request for additional NTS exit rights cannot be delivered through the existing network, the NTS establishes whether this can be facilitated economically and efficiently through the use of (or contracting for) additional demand management tools including with other NTS connectees (e.g. tendering for the buy back of exit capacity, according to agreed procurement guidelines). The process followed for the release of additional offtake rights is described in Transco NTS’s Incremental Exit Capacity Release (IExCR) Statement.
- 2.28. Under the terms of Transco NTS’s IExCR statement, the NTS is required to make as much exit capacity as is requested available to DNs and customers directly connected to the NTS on an annual basis during the interim period, subject to its statutory and licence obligations.

¹⁴ For the purposes of this paper, the “bundled” product offered to NTS direct connects in the interim is referred to as “NTS exit capacity”. The separate capacity and flexibility products offered to the DNs are named “NTS offtake (flat) capacity” and “NTS offtake (flexibility) capacity”. This is consistent with the terminology adopted in the Uniform Network Code (UNC). In addition, for the purposes of this document, all the products described above will be generally termed “NTS exit rights”.

¹⁵ National Grid Transco – Potential sale of gas distribution network businesses, Offtake arrangements, Regulatory Impact Assessment, June 2004

¹⁶ Standard Special Condition A6. Pipe-Line System Security Standards, paragraph 2. Initial proposals on transitional incentive schemes supporting the offtake arrangements

Flow flexibility

- 2.29. For the duration of the interim period, DNs have also been provided with an allocation of NTS offtake (flexibility) capacity (for each NTS offtake point on the DN), consistent with each DN's 1 in 20 obligation. This holding of NTS offtake (flexibility) capacity allows each DN to profile their offtake of gas from the NTS over the day, rather than requiring DNs to offtake gas from the NTS at the flat offtake rate consistent with their holding of NTS offtake (flat) capacity.
- 2.30. As with NTS offtake (flat) capacity, DNs are able to request increases (or decreases) in their allocation of NTS offtake (flexibility) capacity on an annual basis. This enables DNs to trade off the use of NTS offtake (flexibility) with the use of demand management tools and, to an extent limited by lead times, with additional DN investment. For shippers serving directly connected customers, access to flow flexibility is bundled with firm offtake rights.

Interruptible access to the NTS

- 2.31. In the interim, current arrangements for shippers securing interruptible NTS exit capacity remain largely the same as those that applied prior to May 2005. The key difference is that all NTS directly connected interruptible sites have the right to apply for the sites to become firm should they so wish. This is consistent with the requirement for the NTS to release capacity consistent with the terms of Transco's IExCR statement in the interim, subject to statutory and licence obligations.
- 2.32. The NTS therefore retains the right to interrupt those NTS interruptible sites that choose to retain interruptible status, consistent with the terms of their current contracts. The NTS is also able to request DNs to "turn down" offtake at NTS/DN offtake points, up to the level of volume of interruptible offtake DNs make available at each NTS/DN offtake point.

Interim incentives

- 2.33. On 8 March 2005, Ofgem issued an Initial Proposals consultation for interim incentives schemes¹⁷. These were designed to apply to both the DNs and the NTS for the duration of the interim period (i.e. 1 June 2005 to 30 September 2008).
- 2.34. Following consideration of responses to this consultation, on 26 April 2005, Ofgem issued a further consultation (the April consultation) which outlined Ofgem's Final Proposals for interim incentives and represented a formal consultation (under section 23 of the Gas Act) in relation to proposed modifications to the six relevant GT licences¹⁸ which included, amongst other changes, changes to reflect Ofgem's final proposals for interim incentives¹⁹.
- 2.35. Following consideration of responses to this consultation, on 25 May 2005, the Authority, with the written consent of the six relevant licensees, directed that each of the six relevant licences be modified in the form set out in the April consultation such that they took effect on completion of the sale of the shares which occurred on 1 June 2005. As a result, Ofgem's interim incentive proposals were implemented on 1 June 2005.

NTS interim incentives

- 2.36. The interim incentives were designed to ensure that Transco operates its NTS business in a manner consistent with its statutory duties and licence obligations. These obligations include the requirement to develop and maintain an efficient and economical pipeline system and the obligation to operate the NTS in an economic, efficient and coordinated manner.
- 2.37. Under the current exit arrangements, Transco's NTS business is incentivised in three key areas:
- ◆ a buy-back and interruptions incentive;

¹⁷ *National Grid Transco – Potential sale of gas distribution network businesses, Initial proposals on interim incentive schemes supporting the offtake arrangements*, March 2005 79/05

¹⁸ i.e. the Transco's NTS licence, Transco's RDN licence, and the four licences for each of the four DNs proposed for sale by Transco.

¹⁹ *National Grid Transco – Potential sale of gas distribution network businesses, Final Proposals for Interim Incentives and Formal consultation under section 23 of the Gas Act 1986*, April 2005, 129/05
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- ◆ a constrained LNG incentive; and
- ◆ a charges foregone and exit investment incentive;

Buy-back and interruptions incentive

- 2.38. Transco NTS contracts with shippers for interruption under either Transco Nominated Interruptible (TNI) or Shipper Nominated Interruptible (SNI) contracts. Transco NTS may call an interruption in the event of network capacity constraints, supply demand balancing on high demand days, in an emergency or for testing purposes. Where Transco NTS nominates a supply point to be interrupted for more than 15 days in a particular year (up to the maximum permitted which is usually 45 days), there is a transportation charge credit.
- 2.39. In the interim period, NTS exit capacity is released on an unconstrained basis and this unconstrained release may mean under certain circumstances that it will be necessary for Transco's NTS business to "buy-back" NTS offtake rights.
- 2.40. An interim incentive scheme has been introduced to give the NTS an incentive to interrupt NTS connected supply points²⁰ and buy-back NTS offtake rights as efficiently as possible. These incentives are provided through a single (combined) mechanism which is specified in a standard "sliding scale" form. Under this approach, a target is defined, equal to the expected level of Transco NTS's expenditure on the buy-back of NTS offtake rights and the cost of interrupting customers for more than 15 days. Deviations from this target level of incurred cost are shared between Transco's NTS business and customers, subject to defined sharing factors (75% upside and 50% downside), a cap (£1.68m) and a collar (-£7m).

Constrained LNG incentive

- 2.41. Under the constrained LNG incentive, Transco NTS is set a target for the cost of using constrained LNG storage, and is exposed to the difference between actual costs and this target, thereby incentivising the efficient use of LNG.

²⁰ For the purposes of clarification, NTS connectees, in this context, mean all parties directly connected to the NTS, including, without limitation, directly connected customers such as power stations and the DNs. Initial proposals on transitional incentive schemes supporting the offtake arrangements

- 2.42. When originally developing the exit incentive schemes, Ofgem considered that Transco NTS's incentives could be distorted by its ownership of LNG storage facilities that can function as an alternative to interruption²¹. In particular, increases in the price and/or volume of its use of LNG over forecast levels, as an alternative to using interruption, could result in increased revenues to Transco LNG.
- 2.43. If sharing factors and caps and collars were applied to LNG costs, then Transco SO would only bear a proportion of such higher costs and the remainder would then be recovered in whole (or in part) by higher transportation charges levied on shippers and eventually borne by customers. In order to avoid such a perverse outcome, no cap or collar is specified with regard to the costs of Transco NTS procuring transmission support from the LNG facilities (with Transco NTS therefore facing a 100% exposure to the LNG costs incurred).
- 2.44. As part of the introduction of interim incentives in June 2005, new targets were specified for 2007/8 and 2008/9.

Charges foregone and exit investment incentive

- 2.45. This element of the current exit incentive scheme is based upon the revenues foregone by Transco NTS as a result of its existing interruption discounts. In exchange for agreeing to be interrupted by Transco NTS up to 45 days per year, shippers at interruptible supply points do not pay exit capacity charges. Ofgem refers to these foregone charges as the "interruptible discount".
- 2.46. A foregone charges and exit investment incentive applies to the NTS to:
- ◆ give Transco's NTS business an incentive to reduce the charges foregone as a result of the interruptible "discount" applied to shippers agreeing to have interruptible sites interrupted by the NTS for up to 45 days per year; and
 - ◆ allow Transco's NTS business additional revenues associated with exceeding the baseline output measures set out within its GT licence.

²¹ *Transco's National Transmission System - System operator incentives 2002-7, Final Proposals*, December 2001.

2.47. As part of the introduction of interim incentives in June 2005, new targets were specified for 2007/8 and 2008/9 – these are capped and collared at +/- £1m.

DN interim incentives

2.48. The exit incentive schemes as described in the five relevant DN licences are designed to ensure that the DNs operate their businesses in a manner consistent with their statutory duties and licence obligations. These obligations include the requirement to develop and maintain an efficient and economical pipeline system and the obligation to operate their networks in an economic, efficient and coordinated manner.

2.49. As described earlier, on 1 June 2005, Ofgem implemented its final proposals for interim incentives within each of the six relevant GT licences. Under these schemes, DNs face a single incentive relating to:

- ◆ requests for NTS offtake (flat) capacity;
- ◆ requests for NTS offtake (flexibility) capacity; and
- ◆ the cost of interrupting DN connectees for greater than 15 days.

2.50. This incentive is structured to follow a standard “sliding scale” form with a defined incentive cost target, a symmetrical cap and collar, and deviations from the target shared between DNs and their customers and subject to defined sharing factors (of 100%). The caps and collars applied are derived as fixed percentages (7.5%) of each DN’s cost performance target to reflect the locational nature of both exit charges and demand and to ensure that incentive schemes are targeted accurately across the networks.

3. Proposed transitional offtake arrangements

- 3.1. As outlined in Chapter 2, Ofgem published an open letter in June 2005 stating that further consideration would need to be given to determining the mechanism by which capacity is allocated to DNs and shippers acting on behalf of NTS direct connects from the period 1 October 2008 to 30 September 2010²². In this chapter, we describe the offtake arrangements currently proposed for this period.
- 3.2. On 10 August 2005, Transco NTS raised Uniform Network Code (UNC) Modification Proposal 0046 (Extension of the Sunset Clauses for Registration of Capacity at NTS Exit Points), outlining details of a proposed process through which firm capacity (held by NTS direct connects) and NTS offtake capacity (held by DNs) could be allocated for the period 1 October 2008 to 30 September 2010²³. The consultation relating to this Modification Proposal recently closed and will be considered by the Authority in due course.
- 3.3. Related to Modification Proposal 0046, changes are proposed to a number of supporting documents as part of the transitional arrangements. Accordingly, Transco NTS has released consultations on proposed changes relating to:
- ◆ the Incremental Exit Capacity Release (IExCR) Methodology Statement which currently only applies to the interim period;
 - ◆ Standard Condition 4B statement of “Principles and Methods to be used to Determine Charges for National Transmission System Connection Services” to introduce the concept of an Advanced Reservation of Capacity Agreement (ARCA) for DNs; and
 - ◆ a proposed generic form of ARCAs applicable to DNs, based upon that which is currently applicable in respect of NTS direct connects.
- 3.4. The consultation on these supporting documents is due to close on 22 September 2005.

²² 151/05, open letter on enduring offtake arrangements, Ofgem, June 2005

²³ UNC Modification Proposal 0046, Extension of the sunset clauses for registration of capacity at NTS exit points, August 2005.

- 3.5. It is important to note that although the contents of this modification proposal and the associated changes to relevant supporting documents are outlined in this chapter, nothing in this consultation document should be viewed as fettering the discretion of the Authority in relation to these consultations.
- 3.6. The focus of this consultation is to outline initial proposals for the most appropriate scope, form and duration of the incentive schemes necessary to support the offtake arrangements proposed for NTS offtake capacity in the period from October 2008 to September 2010. As such, it is necessary to make some high-level assumptions as to the nature of the offtake arrangements that may be in place for this period without fettering Authority discretion.
- 3.7. Modification proposal 0046 describes a process through which NTS exit rights may be allocated to NTS connectees (i.e. both DNs and directly connected customers). This process relates to the allocation of rights for the duration of the transitional period (i.e. for NTS exit rights relating to the period October 2008 to end September 2010).
- 3.8. The offtake arrangements proposed by Transco NTS for the transitional period differ from those currently defined in the UNC in that they are designed to relate to periods for which investment by Transco NTS may be undertaken to satisfy requests for NTS capacity that might otherwise not be capable of being satisfied. Consequently, the proposal is designed to provide Transco NTS with sufficient confidence that requests for NTS exit rights relating to future periods will be backed by firm bookings in the future, and hence that it would be in the interests of customers to invest to meet this demand. In contrast, the interim offtake arrangements are designed for the period May 2005 to October 2008 (i.e. a period in which Transco NTS will have insufficient time to invest to meet requests for additional NTS exit rights).
- 3.9. Fundamentally, the proposed transitional offtake arrangements are similar to those already implemented for the duration of the interim period. In particular, under the proposed transitional offtake arrangements, DNs continue to determine the level of NTS offtake (flat) capacity and NTS offtake (flexibility) capacity required at each NTS/DN offtake point. Therefore, consistent with the existing offtake arrangements, each DN is responsible for requesting a sufficient level of NTS offtake rights at each NTS/DN offtake point to meet its 1 in 20 licence obligation (rather than, for example, shippers representing DN

connectees determining their own NTS offtake requirements). In addition, aside from payments made through any incentive arrangements, DNs do not bear any of the cost of NTS exit rights requested. Instead, any such costs would be borne, under the current charging arrangements, entirely by customers connected to the DNs. It is also proposed that there are no changes to the way in which shippers representing customers directly connected to the NTS request increases in NTS exit capacity.

- 3.10. The key difference between the transitional offtake arrangements and the existing (interim) offtake arrangements relates to the period over which NTS exit rights may be requested, and the process through which these requests are made. Under the current UNC provisions, DNs are able to request changes to their “initial allocations” of NTS exit rights up to the end of the interim period (i.e. gas year ending 30 September 2008).
- 3.11. In contrast, under the new proposals, DNs will not be assigned an initial allocation of NTS exit rights for the transitional period. Instead, DNs will be required to request their *total* requirements for NTS exit rights for the gas year 2008/09 (i.e. for the first year of the transitional period) in October 2005²⁴ and for gas year 2009/10 (i.e. the second year of the transitional period) in June / July 2006.
- 3.12. In the event that these requests require Transco NTS to undertake any specific reinforcement to deliver the level of NTS exit rights requested by a DN at any NTS offtake point (or group of NTS offtake points), then, DNs will be required to enter into a contractual agreement with the NTS. This “DN ARCA” (which will be required given the proposed changes to Transco NTS’s Incremental Exit Capacity Release Methodology Statement and Standard Condition 4B statement) will outline the volume of NTS exit rights the DN requests from Transco NTS, the date at which these rights are required, and also outline the financial implications of either party defaulting on the terms of the agreement.
- 3.13. DNs will then have the ability to request amendments to their capacity allocations within the three year investment lead time. For example, in June /

²⁴ or two weeks after implementation of the Modification proposal if this is different.
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July 2008, DNs will be able to request amendments to their allocated capacity for gas years 2008/9 and 2009/10.

- 3.14. Transco NTS considers these arrangements are comparable to those that are already in place for customers directly connected to the NTS, hence are desirable to ensure there is no undue discrimination between the two classes of NTS connectees.

4. Proposed transitional incentive schemes

- 4.1. This chapter sets out Ofgem's initial proposals for the scope, form and duration of incentive schemes supporting the transitional offtake arrangements, for the DNs and the NTS in turn.

DN transitional incentives

- 4.2. This section outlines Ofgem's proposals for the incentives that will relate to the DNs for the transitional period. It describes the proposals in terms of:

- ◆ scope;
- ◆ form; and
- ◆ duration.

Scope

- 4.3. As discussed in Chapter 3, under the proposed transitional offtake arrangements any DN requests for NTS exit capacity at the three year ahead stage that trigger NTS investment will require the DN in question to enter into a contractual agreement with the NTS. It is anticipated that such contractual agreements will financially commit the DN to remunerating Transco NTS for the NTS exit capacity requested with some form of penalty payment being payable should the DN amend its capacity request at a later date to a lower volume of capacity.
- 4.4. If the costs incurred as a result of such penalty payments could be passed through, by the DN, to its shippers, and ultimately customers, then the DNs might be incentivised to over-request capacity at the three year ahead stage leading, in turn, to an inefficiently high level of NTS investment and the potential for stranded assets. As such, Ofgem does not propose that any penalty payments made by the DNs to the NTS should be able to be passed through to customers. Instead, the DNs should be exposed to 100% of such costs.
- 4.5. Under current Transco NTS proposals, DNs will be able to amend their initial capacity requests (which were made at the three year ahead stage) within investment lead times, and as late as three months before the commencement of

the relevant gas year. Therefore, as under the interim arrangements, DNs will retain responsibility for determining the appropriate level of NTS exit rights to book to ensure that the users of its network can offtake in a manner that is consistent with the DN's licence obligations. Given that the DN will decide the level of NTS capacity that it is appropriate, but that the customers connected to its network that pay for that level of NTS capacity through network charges, there exists, absent any incentive scheme, a potentially rational tendency for the DN to overbook NTS exit capacity.

- 4.6. In addition, where DNs enter into an ARCA with Transco NTS, there will be an additional incentive upon DNs not to reduce their (3 year ahead) initial capacity requests if the resulting shortfall between amended capacity requests and the initial capacity requests triggers penalty payments by the DN, under the terms of the ARCA, which cannot be passed through to customers.
- 4.7. For these reasons, Ofgem considers it necessary to specify incentives for the DNs for the duration of the transitional period primarily to mitigate this potential tendency to overbook NTS exit rights when making amended capacity requests (within investment lead times). In order to deliver a relatively simple incentive scheme, Ofgem proposes a single incentive mechanism for each DN for the duration of the transitional offtake arrangements. This requires the specification of a single cost performance measure and target (for each DN) covering both NTS offtake (flat) capacity and NTS offtake (flexibility) capacity.
- 4.8. Note that Ofgem does not consider it appropriate to extend the current greater than 15 day interruptions DN incentive for the duration of the transitional period. Instead, Ofgem proposes to review this element of DN incentives at the time of the next gas distribution price control review at which time a broader review of DN incentives (in the context of DN interruption reform) will be undertaken.

Form

- 4.9. Ofgem proposes that the DN incentive schemes continue to be structured following a standard "sliding scale" form, with a defined incentive cost target and a cap and collar. Deviations from this target level of incurred cost would

then be shared between DNs and customers, and therefore be subject to a defined sharing factor.

4.10. Ofgem proposes that cost performance targets are specified for NTS offtake (flat) capacity and NTS offtake (flexibility) capacity for each DN (for formula years 2009/10 and 2010/11²⁵) as follows:

- ◆ expected volume of NTS offtake (flat) capacity and NTS offtake (flexibility) capacity required by each DN (by offtake point) in each year; multiplied by
- ◆ a reference price for both NTS offtake (flat) capacity and NTS offtake (flexibility).

4.11. These components of the incentive scheme are discussed in turn below. We then set out Ofgem's initial proposals on the caps, collars and sharing factors for the scheme.

Expected volume of NTS exit rights

4.12. A key element of the proposed DN incentive scheme is the inclusion of an estimate of the level of NTS offtake (flat) capacity and NTS offtake (flexibility) capacity that DNs would be expected to require, all other things being equal. Ofgem considers that the most appropriate level for these volumes should be consistent with the 1 in 20 obligation of each DN.

4.13. The proposed levels of NTS offtake (flat) capacity and NTS offtake (flexibility) capacity proposed for inclusion in the cost performance targets are included in Appendix 1.

4.14. In order to inform its decision on the value of the cost performance targets, Ofgem invited each individual DN to provide their view of appropriate capacity targets for the transitional period. However, it was recognised that the DNs may have a rational tendency to overstate the required targets. Therefore Ofgem performed an independent analysis of the data provided and determined a methodology for the derivation of the DN targets as outlined below. In addition,

²⁵ Targets for 2008/9 are already specified within the licence.
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Ofgem commissioned technical consultancy advice to review the submission of volume requests from the DNs for the transitional period.

- 4.15. The actual NTS capacity requests recently submitted from the DNs to Transco NTS for the year 2007/08 were adopted as a baseline for the calculation of the expected capacity volumes for each LDZ exit zone. These capacity requests for 2007/08 reflect a change in DN behaviour in response to the prices and incentive targets faced during the interim period. Amongst other things, these data have indicated that DNs are able to respond to incentives and price signals by substituting NTS offtake (flat) and NTS offtake (flexibility) capacity between different exit zones.
- 4.16. LDZ specific, annual growth rates were applied to this 2007/8 baseline in order to calculate the volume targets for 2009/10 and for 2010/11.²⁶ The growth rates applied were provided by Transco NTS and are consistent with the growth rates assumed by Transco NTS in its forthcoming Ten Year Statement for 2005 and provided to DNs in accordance with the Uniform Network Code (section H of the Offtake Arrangements Document).²⁷ These assumed growth rates are provided in Appendix 1. Ofgem considers that the application of growth rates at the LDZ level is appropriate given the potential substitutability of NTS offtake (flat) and NTS offtake (flexibility) capacity between different exit zones within an LDZ.
- 4.17. When the volume target derived, following application of the methodology outlined above, was found to be higher than the capacity targets requested by the DN from Ofgem at an LDZ level, the proposed targets, as presented in Appendix 1, reflect the exit zone targets requested by the DN for each exit zone within the relevant LDZ.
- 4.18. The proposed targets are intended to provide DNs with an appropriate trade-off between DN-specific investment and NTS offtake capacity. However, the methodology applied to calculate proposed incentive targets for capacity will not necessarily be applied in the calculation of incentive targets in the future. In

²⁶ Note that the years for which the transitional incentive would apply are financial years (1 April to 31 March), while the capacity requests from DNs were submitted for gas years (1 October to 30 September). However, it was assumed that the two requests would be comparable, given that the same peak winter period is included in both.

particular, it should not be assumed that, in the future, past behaviour will be used for the derivation of DN incentive targets, as this may, in the long term, cause distortions in the capacity booking mechanism. However, it should be noted that the numbers utilised as a baseline for the calculation of the volume targets for 2008/09 reflect the actual DN capacity requirements for 2007/08, which were submitted when the DNs had no indication of the methodology that would be adopted for the setting of DN cost performance targets in the transitional period.

Expected price of NTS exit rights

- 4.19. In the interim period, for NTS offtake (flat) capacity, annual NTS exit charges (defined on an LDZ charging zone basis in the interim period) are used as the most appropriate price element for calculating the cost performance target (and actual cost performance measure). Furthermore, the price for NTS offtake (flexibility) capacity is assumed to be the same as for NTS offtake (flat) capacity.
- 4.20. Ofgem considers that the most appropriate reference price for NTS offtake (flat) capacity remains the prevailing (outturn) price of NTS exit capacity as set out in NGT's charging statement. This is because this price will be defined on an ongoing basis throughout the transitional period (for the purposes of charging shippers who convey gas across the DNs).
- 4.21. As regards the most appropriate reference price for NTS offtake (flexibility) capacity in the transitional period, Ofgem considers it to be important that additional flexibility purchased by DNs is priced on the same basis as additional flexibility purchased by customers directly connected to the NTS. As NTS directly connected customers access increased levels of flexibility by purchasing additional units of NTS exit capacity (hence increasing their maximum hourly offtake quantity), Ofgem considers that the prevailing (outturn) price of NTS exit capacity continues to be the most appropriate reference price for NTS offtake (flexibility) capacity. This ensures that both DNs and customers directly connected to the NTS are able to access NTS offtake flexibility on a not unduly discriminatory basis.

- 4.22. It is important to note that by using the prevailing (outturn) price of NTS exit capacity for NTS exit rights, DNs will be exposed to an amount of price risk to the extent that the volumes of NTS exit rights they request differ from those volumes included in the calculation of the incentive target.
- 4.23. Ofgem would also note that the methodology used to calculate the price of NTS exit capacity is likely to be reviewed in the context of the forthcoming transmission price control review. Ofgem considers it would be appropriate to include the resulting revised NTS offtake (flat) capacity and NTS offtake (flexibility) capacity charges in the calculation of the cost performance targets for the transitional incentive schemes rather than the current prices. Accordingly, any changes to capacity charges will have implications for the DN exposure under the incentive schemes proposed above.

Definition of caps, collars and sharing factors

- 4.24. Ofgem's initial proposal is that caps and collars for DN cost performance measures should continue to be calculated as a fixed percentage of each DN's cost performance target. This will mean that the absolute level of DN caps and collars will vary significantly across each network. Ofgem considers that this approach will reflect the locational nature of both exit charges and demand and ensure that incentive schemes are accurately targeted across the network. Ofgem's initial view is that these caps and collars should continue to be symmetric around defined targets.
- 4.25. Sharing factors also need to be defined when setting the incentive parameters for the transitional DN incentive schemes. For consistency with the interim incentive scheme, Ofgem's initial proposal is that the incentive parameters that currently apply to the DNs are extended to cover the two years of the transitional period. These parameters are presented in Table 4.1.
- 4.26. As Table 4.1 shows, the proposal is therefore to maintain upside and downside sharing factors at a level of 100%. In Ofgem's view, such sharing factors are appropriate to ensure that DNs bear, within the limits of the cap and collar, the opportunity cost of over-requesting capacity and can therefore make rational and efficient trade-offs between additional NTS exit capacity and alternative means of balancing supply and demand such as interruption and demand management.

Furthermore, were the sharing factors to be less than 100%, whilst DNs bear 100% of the penalty payments incurred as a result of a shortfall in amended capacity requests relative to initial capacity requests, this would incentivise DNs to minimise such a shortfall by over-requesting as part of its amended capacity requests, even if this would mean that the DN exceeds its incentive target.

Table 4.1 Parameters for DN incentive schemes

	Cap and Collar (% of each DN target)		Sharing factors	
	Cap	Collar	Upside	Downside
Proposed incentive parameters	7.5%	-7.5%	100%	100%

Duration

- 4.27. Ofgem considers that the transitional incentive schemes should be defined for the entire transitional period (i.e. from 1 October 2008 to 30 September 2010). Ofgem would welcome views on the proposed duration of the DN transitional incentive scheme.
- 4.28. It should be noted that Ofgem will consider the interaction between the transitional incentive scheme and the DN price controls as part of GDPCR. In particular Ofgem will want to understand better the existing capacity of the DN and the relationship between capex allowances under the price control settlement and the future capacity of the DN. This understanding will be important in allowing Ofgem to reach a view on the appropriate treatment at future price controls of any capital expenditure incurred as a result of the transitional incentive scheme.

NTS transitional incentives

- 4.29. As more fully described in Chapter 3, Transco NTS has proposed that the transitional offtake arrangements should, to a large extent, be based upon the (existing) interim offtake arrangements. The key issue concerns the extent to which the form of the NTS incentive arrangements is required to be reviewed at

the time of the implementation of the transitional offtake arrangements (as opposed to being consulted upon and implemented as part of the gas Transmission Price Control Review (TPCR)).

- 4.30. Ofgem considers that, in general, it would be advantageous for NTS exit incentives for the transitional period not to be reviewed now, but instead be defined at the time of the next TPCR (i.e. in 2007). This would enable incentives to be set following the operation of the interim incentives (therefore offering a greater set of performance data and hence promoting greater accuracy and certainty with respect to incentive target setting). In addition, specifying incentives targets in 2007 will also give the opportunity for incentives to be set in the context of wider price control agreement (and hence may be more relevant to the regulatory environment in which the NTS will be operating).
- 4.31. This approach would also enable Ofgem to consider more fully all interactions between entry and exit before making a number of policy decisions regarding the setting of NTS incentives. These include determining the most appropriate methodology to select for the definition of output measures, and the setting of Unit Cost Allowances (UCAs) at NTS exit points. As a consequence, by following this approach, NTS incentives determined at the time of the TPCR would be designed to address short term efficiency trade-offs regarding day-to-day operational decisions with respect to the management of NTS exit capacity.
- 4.32. The key risk that arises from opting not to set NTS incentives for the transitional period at this time is that the NTS will face a degree of uncertainty regarding cost-recovery and the treatment of investment for the transitional period. As a consequence, benefits to customers may be reduced to the extent that the NTS makes inefficient decisions (compared to those it would have made under a correctly specified set of incentives). For example, without an effective set of incentives, Transco NTS may simply choose to invest in pipelines rather than choosing to deliver capacity through more efficient network management (i.e. interruption contracts and the use of constrained LNG). Furthermore, benefits to customers may be reduced to the extent that there are no incentives on Transco NTS to reduce investment lead times and deliver timely investment.

4.33. On balance, Ofgem does not propose to specify NTS incentives for the transitional period at this time. Ofgem considers that the potential benefits of considering the most appropriate scope and form of NTS incentives at the time of the TPCR outweigh the potential costs resulting from a lack of certainty regarding the cost-recovery and treatment of investment for the transitional period.

Views invited

4.34. Views are invited on all aspects of the transitional incentive schemes outlined in this chapter for the DNs and the NTS, and in particular regarding Ofgem's initial proposals on:

- ◆ the proposed targets for NTS offtake (flat) capacity and NTS offtake (flexibility) capacity;
- ◆ the most appropriate reference price for NTS exit rights;
- ◆ the proposed definition of caps, collars and sharing factors in the DN transitional incentive schemes;
- ◆ the proposal not to define an incentive for cost of greater than 15 day interruptions by DNs at this time; and
- ◆ the proposal not to define NTS incentives for the transitional period at this time but to defer setting of these incentives to the forthcoming TPCR process.

5. Way forward

- 5.1. This document sets out Ofgem's initial proposals on a wide range of issues relating to the development of enduring incentive schemes for the NTS and the DNs. Views are invited on all aspects of this consultation and in particular on the transitional incentive schemes outlined in Chapter 4. Paragraph 4.35 above outlines issues on which Ofgem would particularly welcome views.
- 5.2. Following consideration of respondents' views to this Initial Proposals consultation, Ofgem envisages publishing Final Proposals on enduring incentive schemes in early November 2005. This document will include a final consultation on proposed licence amendments necessary to implement these proposals, allowing the enduring incentive schemes to be finalised by the end of November 2005.

Appendix 1

Table A1.1: LDZ growth rates assumed

LDZ	2007/8 to 2008/9	2008/9 to 2009/10	2009/10 to 2010/11
Scotland	1.45%	1.23%	1.06%
Northern	1.61%	1.15%	1.04%
North West	1.57%	2.32%	0.93%
North East	1.77%	1.48%	1.32%
East Midlands	1.71%	1.45%	1.29%
West Midlands	1.63%	1.96%	1.23%
Wales North	1.97%	1.67%	1.42%
Wales South	1.28%	1.01%	0.91%
Eastern	2.26%	1.72%	1.56%
North Thames	1.66%	1.44%	1.25%
South East	1.44%	1.27%	1.18%
Southern	1.92%	2.47%	1.57%
South West	2.34%	1.92%	1.66%

Table A1.2: Comparison of incentive targets and DN requests from NTS for 2007/8²⁸
(GWh / day)

DN	LDZ Exit Zone	Flat capacity		Flexible capacity	
		incentive target	DN requests from NTS	incentive target	DN requests from NTS
Scotland	SC1	59.73	59.73	6.00	6.00
	SC2	72.71	72.71	8.09	8.09
	SC4	245.32	245.32	13.57	13.57
North of England	NO1	250.04	234.84	-0.03	-2.34
	NO2	26.97	26.40	2.64	2.45
	NE1	226.29	227.06	9.86	19.00
	NE2	61.94	62.45	0.31	1.01
North West	NW1	347.80	228.91	8.71	25.04
	NW2	216.63	330.96	8.74	14.96
East of England	EA1	39.70	39.39	5.36	5.33
	EA2	43.32	43.29	5.86	5.85
	EA3	65.16	71.36	-0.14	0.72
	EA4	233.68	226.02	0.02	0.29
	EM1	92.09	110.37	1.33	0.12
	EM2	97.03	104.00	0.78	6.49
	EM3	294.18	268.51	5.74	2.09
	EM4	19.50	20.35	1.26	1.25
London	NT1	12.86	20.59	0.00	0.00
	NT2	197.34	182.59	0.00	-3.93
	NT3	284.71	312.84	0.00	-7.35
West Midlands	WM1	77.52	109.86	1.81	-0.50
	WM2	254.96	232.21	5.92	2.66
	WM3	134.14	119.14	-4.56	-2.75
Wales & West	SW1	38.26	37.50	2.09	1.89
	SW2	164.62	161.98	4.73	4.80
	SW3	95.24	93.66	4.96	4.68
	WA1	53.94	51.88	0.00	0.00
	WA2	193.68	193.78	0.00	0.00
South of England	SE1	419.01	442.67	0.00	0.00
	SE2	109.67	99.74	0.00	0.00
	SO1	116.54	116.46	5.66	5.00
	SO2	297.99	296.13	6.45	7.22
Total		4842.57	4842.67	105.16	121.65

²⁸ Note that the incentive targets relate to the formula year 2007/8, and the DN requests from the NTS relate to the gas year 2007/8. However, these capacities are compared within this table on the basis that both are driven by the 2007/8 winter and are therefore comparable.

Table A1.3: Proposed incentive targets for the transitional period²⁹ (GWh / day)

DN	LDZ Exit Zone	Flat capacity		Flexible capacity	
		2009/10	2010/11	2009/10	2010/11
Scotland	SC1	55.53	56.08	6.17	6.23
	SC2	75.97	77.04	8.31	8.39
	SC4	245.95	248.90	13.94	14.08
North of England	NO1	241.37	243.89	-2.28	-2.25
	NO2	27.13	27.42	2.52	2.55
	NE1	234.50	237.60	19.62	19.88
	NE2	64.49	65.35	1.05	1.06
North West	NW1	233.83	235.58	22.82	23.61
	NW2	344.73	347.16	15.08	15.11
East of England	EA1	40.78	41.58	5.54	5.63
	EA2	46.29	47.08	6.09	6.18
	EA3	76.66	71.16	0.75	0.77
	EA4	230.17	241.50	0.30	0.30
	EM1	113.88	115.35	0.12	0.13
	EM2	107.31	108.69	6.70	6.78
	EM3	277.06	280.63	2.15	2.18
	EM4	21.00	21.27	1.29	1.31
London	NT1	21.23	21.50	0.00	0.00
	NT2	188.29	190.65	-5.57	-4.48
	NT3	322.60	326.65	-9.48	-9.03
West Midlands	WM1	114.18	115.63	-0.49	-0.48
	WM2	240.55	243.62	2.75	2.79
	WM3	122.53	123.56	-2.65	-2.62
Wales & West	SW1	39.12	39.76	2.13	2.23
	SW2	168.96	171.76	5.38	5.62
	SW3	97.69	99.31	3.69	4.00
	WA1	53.79	54.55	0.00	0.00
	WA2	198.25	200.05	0.00	0.00
South of England	SE1	454.73	460.09	0.00	0.00
	SE2	102.46	103.67	0.00	0.00
	SO1	120.72	121.88	5.22	5.30
	SO2	308.34	313.89	7.54	7.66
Total		4990.10	5052.83	118.70	122.93

²⁹ Figures expressed are with respect to formula years.
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