Development of the “Enduring NTS Offtake Arrangements”

EOWG, 1st Feb 06

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Outline

- Approach to reform
- Overview of current arrangements
- Issues
- Strawmen proposals – registration process
- Way forward

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Proposed Approach to Exit Reform

- Propose that we consider the areas of current regime that require reform rather than starting from “TANIF model”
- This involves:
  - review of current arrangements
  - identification of issues
  - consideration of potential solutions
  - assessment of relative costs/benefits

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Overview of current arrangements -Up to Oct 2010

Key features include…..

- Single “bundled” product in place at shipper exit points, separate flat/flex products at DNO exit points
- Financial commitment to underpin incremental investments specific to a connection
  - Ofgem responsible for dispute resolution
- UNC application and allocation (“registration”) processes specific to type of offtake…….

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1. NTS Daily Metered (DM) Supply Points

- Shippers allocated firm NTS Exit Capacity per exit zone based on their nominated System Offtake Quantity (SOQ) via SPA process
- Shipper can only hold exit capacity in respect of any supply point while it is the 'Registered User'
- Capacity is allocated on an 'evergreen basis' with no renewal process required
- Changes in SOQ are limited:
  - Decrease - SOQ can only be reduced during "capacity reduction period" (Oct – Jan) and can not be reduced to a level below the previous winters maximum daily consumption
  - Increase – subject to assessment of system capability or whether previously reserved via ARCA

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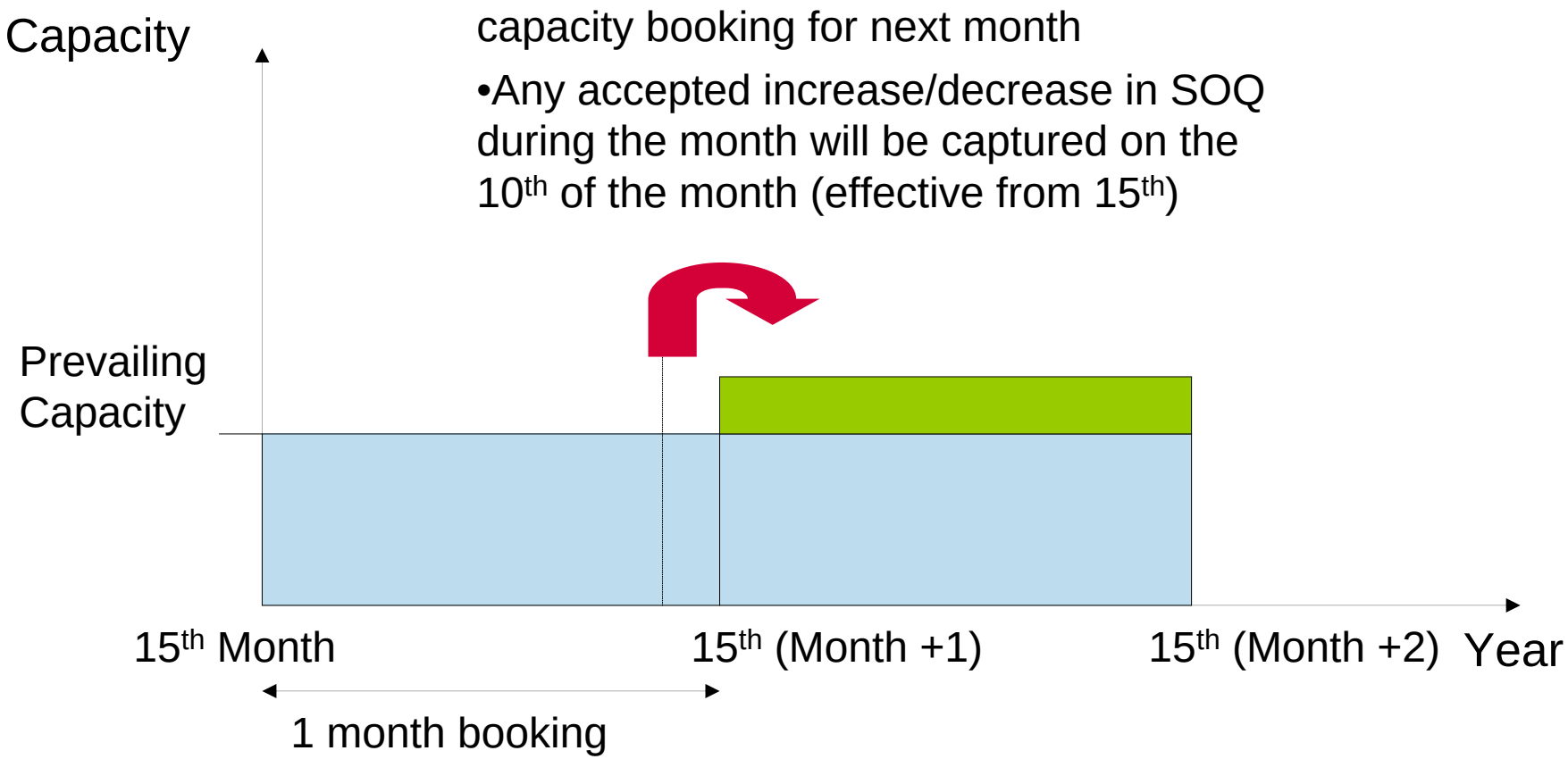
1. NTS Daily Metered (DM) Supply Points

- On 10th of each month, latest SOQ set as capacity booking for next month
- Any accepted increase/decrease in SOQ during the month will be captured on the 10th of the month (effective from 15th)



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2. NTS CSEPs

- NTS Exit Capacity booked by shipper on a 12-monthly rolling basis
- Shipper can apply for either a new amount, an annual renewal or an increase in current amount no earlier than 6 months, nor later than 4 days prior to proposed registration date
- Capacity period is 12 months after date of registration or the date of an approved increase, at which point the capacity will expire unless renewed via a further application
- During the capacity period, the level of NTS Exit Capacity can not be reduced nor the registration terminated
- Trading facilitated between shippers at the CSEP

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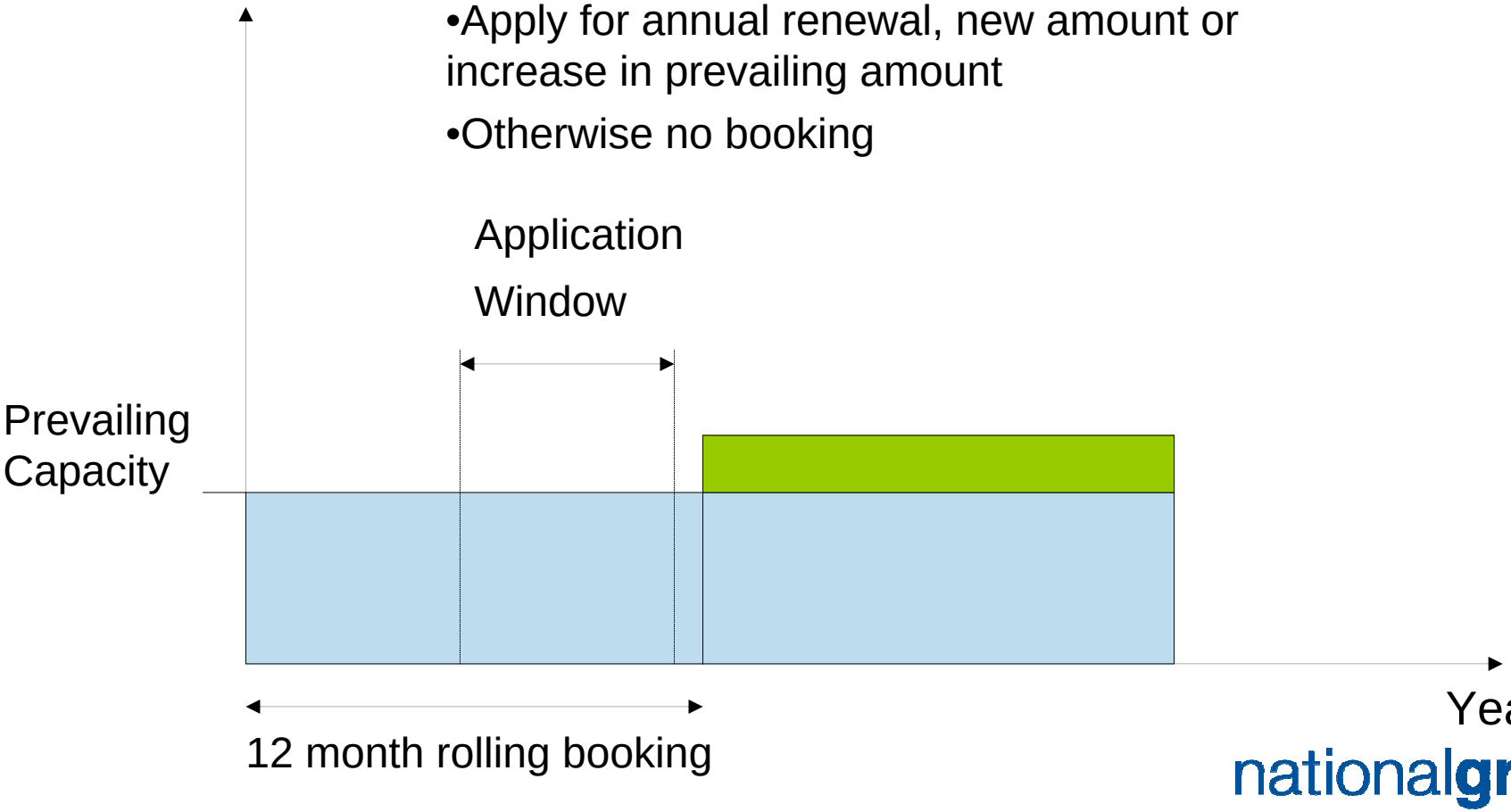
2. NTS CSEPs

Capacity



3. NTS Interconnectors

- Broadly same as for NTS CSEPs, other than the administration of a Downstream Capacity Holder (DCH) Voucher scheme
- Any applications for capacity, and requests for transfer of capacity, must be accompanied by a valid DCH certificate

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4. NTS Storage Sites

- Shippers may hold NTS Exit Capacity if they elect for firm transportation
- At present, however, all transportation at storage connection points treated as ‘interruptible’.
- Storage Users are required to register their peak offtake (i.e. injection rate) amounts, equivalent to an interruptible supply point SOQ
- Shippers may book firm exit capacity via the SPA process.

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5. NTS/LDZ offtakes

- DNO Users can apply for new or revised amounts of NTS Exit (Flat) and NTS Exit (Flex) capacity for each year up to Oct 2010 during June/July each year
- Incentives on DNO Users to efficiently book capacity
- DNO Users do not pay (directly) for capacity

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Summary of Current Registration Arrangements

NTS Exit Point	Product	Who books	Process/Duration	Level of Capacity	Notice Period - Increase & Decrease	Other
NTS Supply Points	NTS Exit Capacity	Shipper confirms SOQ via the SPA process	Booked monthly One month duration	Equal to SOQ Aggregate firm Level ≤ physical maximum (24.MHQ)	Min. 10 days Max. 6 months	None
NTS CSEPs	NTS Exit Capacity	Shipper books	Annual tranches but can increase mid-year	Aggregate firm Level ≤ physical maximum (24.MHQ)	Min. 4 days Max. 6 months	Facility for capacity trading.
Interconnectors	NTS Exit Capacity	National Grid books on behalf of shipper (after confirmation of DCH Voucher)	Annual tranches but can increase mid-year	Aggregate firm Level ≤ physical maximum (24.MHQ)	Min. 4 days Max. 6 months	DCH Voucher scheme Capacity trading and transfer.
Storage Sites	NTS Exit Capacity	Shipper can book firm capacity (via SPA process) or can register as interruptible	N/A	N/A	N/A	N/A
NTS/LDZ Offtakes	NTS Flat & Flex Capacity	DN's Book	Annual tranche applied for during June / July. Capacity allocation by 1st Oct	Agreed Flat & Flex Capacity via Offtake Capacity Statement (OCS)	N/A	N/A

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Issues?

- Information to inform efficient and economic NTS investment
  - Limited mechanisms and incentives for shippers to inform of “longer” term requirements - planning process therefore requires assumptions which could, in the extreme, lead to asset stranding
  - Level of user commitment required to underpin incremental investments
- Non-discriminatory release of capacity within constrained period
  - Disparity in UNC capacity registration processes implies “first come first served” allocation between classes of customer
  - In future may see increased competition through Users desire for increased
    - “flexibility” at off-peak demands than available
    - access to capacity close to or on the gas day

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Key questions to inform regime development (1)

- Capacity products – “definition of access rights”
  - common products available to all users?
  - type of capacity products?
  - nodal/zonal products?
- Capacity application processes
  - consistent arrangement across all types of exit point?
  - how far in advance should Users be able to register capacity?
- Capacity allocation processes
  - treatment of competing requests for constrained release?
  - level of user commitment to allocate incremental capacity?
- Charging arrangements
  - should DNs pay directly for capacity?

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Key questions to inform regime development (2)

- Capacity trading
  - Should there be increased opportunity to trade at/between exit points?
- System management
  - What commercial mechanisms should be in place to efficiently and safely manage offtake of gas?

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Development of proposals

- Consider that there are 3 broad options with increased amount of change

  - Option 1. Implement consistent arrangements
  - Option 2. Extend permitted registration timescales
  - Option 3. Implement long term auctions

"TANIF type model"

- Parts of each option could be "interchanged"

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Nomenclature

- “x” years – refers to period of constrained release i.e. investment lead time for release of additional capacity for an exit point
- “y” years – refers to period required to provide notice of capacity reductions (under option 1)
- “z” years – refers to period for which capacity must be booked to underpin system investment (assume sufficient to justify efficient and economic investment)

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Option 1. Implement Consistent Arrangements - Principles

Seek to introduce consistent arrangements across all offtakes with “enhanced” user commitment ….

- Implement common
  - capacity products available to all users
  - request and allocation process at all exit points
  - trading arrangements at all exit points
  - charging arrangements for capacity holder (i.e. move to DN pays model)
- User’s existing capacity rights maintained, but common notice period of “y” years for capacity reductions
- System investments underpinned by commitment to book capacity for “z” years through “reservation” agreement

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Option 1. Implement Consistent Arrangements - Overview of model

- Capacity application
  - Users able to request capacity rights for following gas year during “application window”
  - Users able to request daily capacity day ahead and on the day
- Capacity allocation
  - Existing capacity rights maintained in absence of request to increase or decrease holdings
  - Decreases: subject to “y” years prior notice
  - Increases: accepted if
    - previously “reserved” (see next slides); or
    - physically available and no competition, otherwise prorate user requests

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Option 1. Implement Consistent Arrangements - Overview of model

- Charging
  - Capacity holder pays prevailing use of system charges
- Trading
  - Users able to trade at exit points

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Option 1. Implement Consistent Arrangements - Capacity reservation

- To obtain increase in existing capacity levels greater than one year ahead…
  - Party able to reserve firm capacity through a bilateral “reservation agreement”
    - if investment required, “x” years notice required
  - If investment not required, party makes commitment to ensure “y” years of use of system charges paid from when incremental capacity first available
  - If investment required, party makes commitment to ensure “z” years of use of system charges paid from when incremental capacity first available
    - z>=y, with simplifications if z=y
- Party could be shipper/DNO Users or developer

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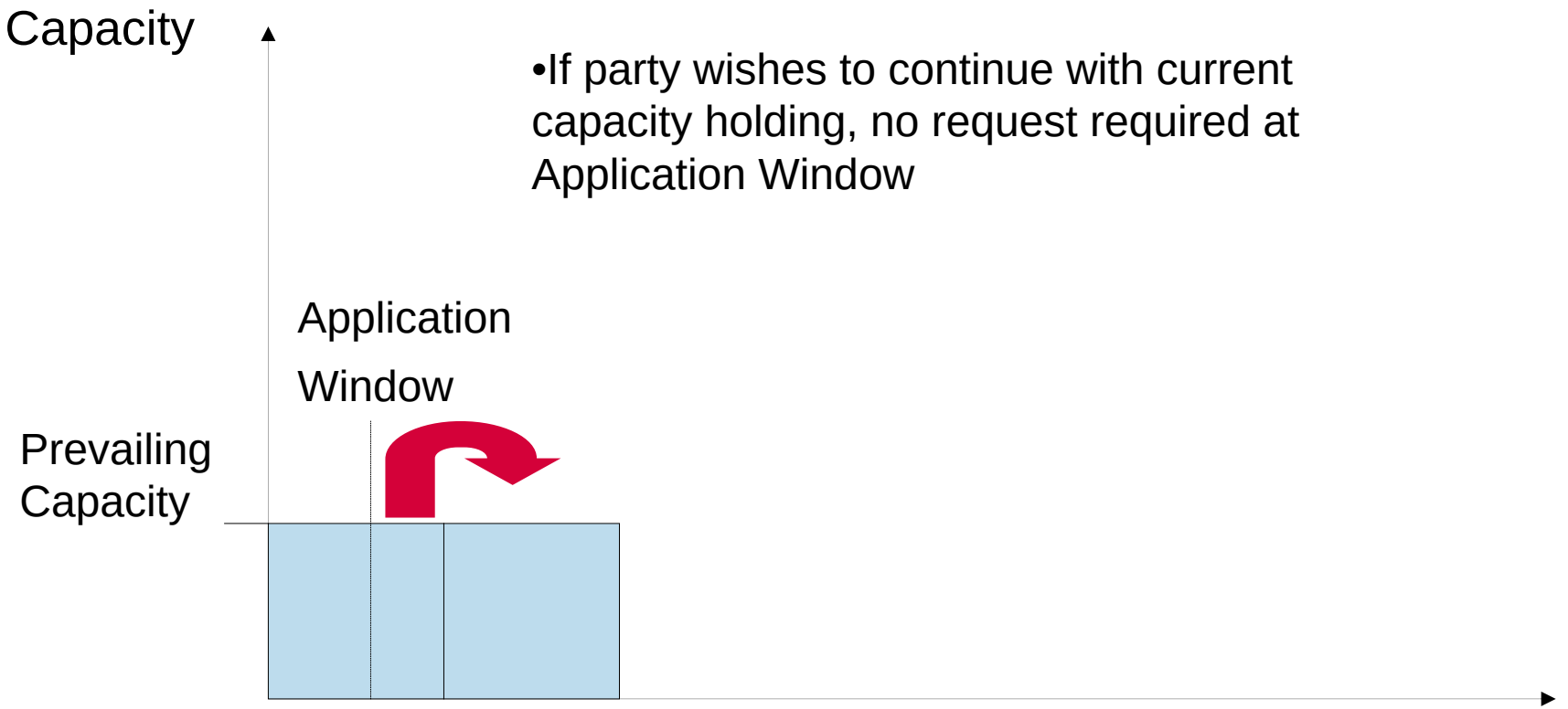
Option 1. Implement Consistent Arrangements – No change



•If party wishes to continue with current capacity holding, no request required at Application Window

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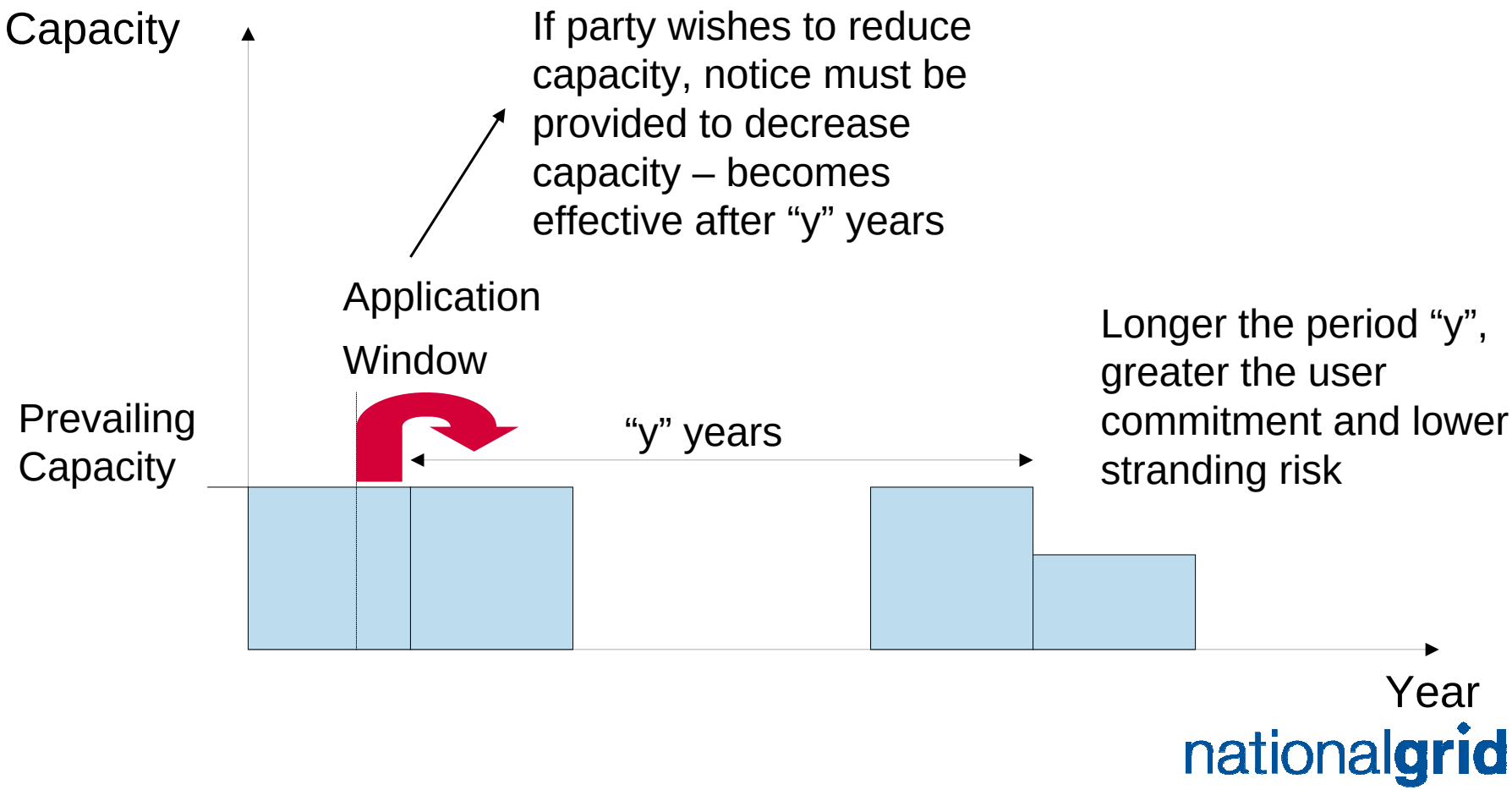
Option 1. Implement Consistent Arrangements - Reduction



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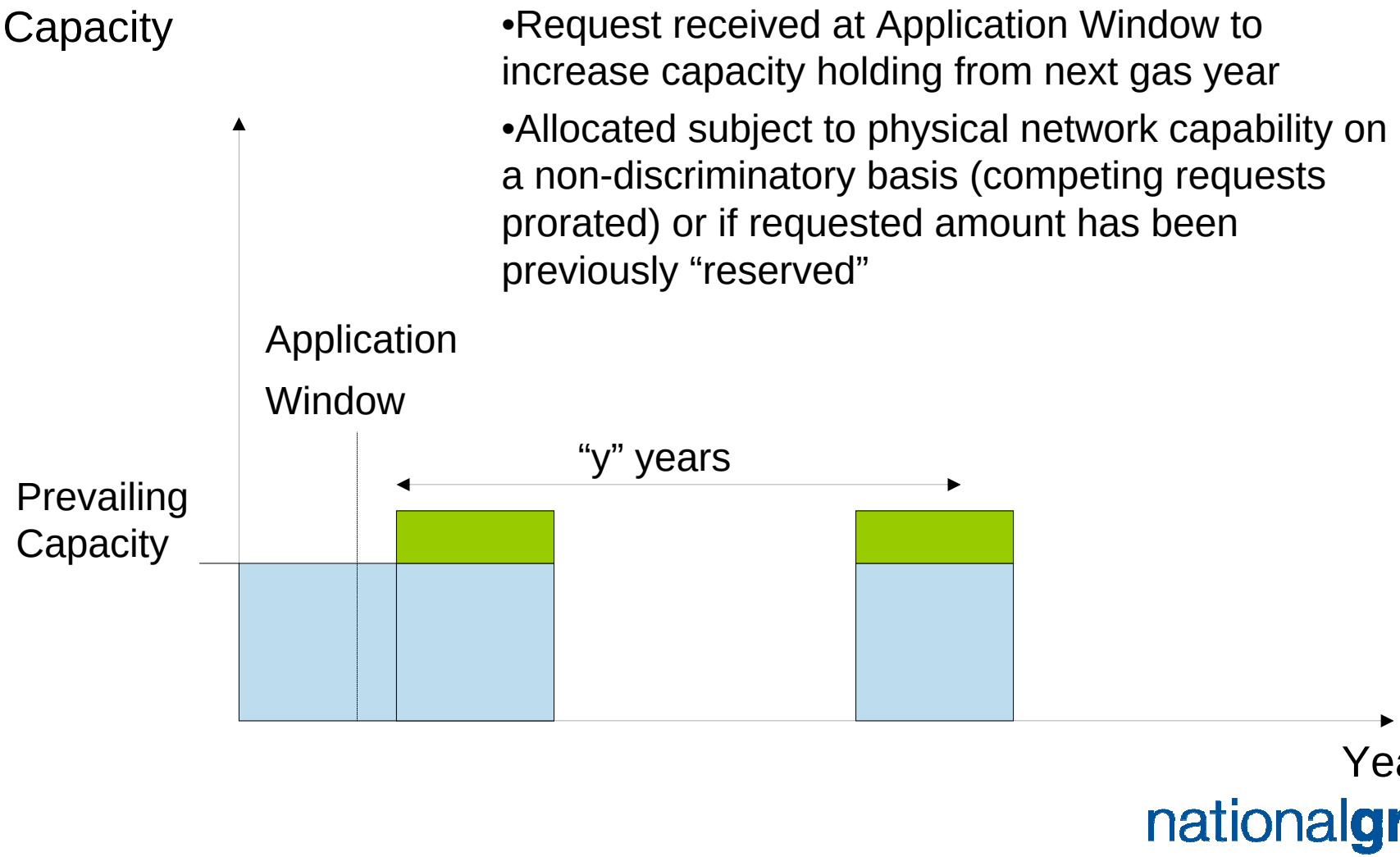
Option 1. Implement Consistent Arrangements - Increase



- Request received at Application Window to increase capacity holding from next gas year
- Allocated subject to physical network capability on a non-discriminatory basis (competing requests prorated) or if requested amount has been previously “reserved”

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Option 2. Extend permitted registration timescales - Principles

Build on option 1 to allow Users greater choice in respect of capacity registration…..

- Users able to request required level of capacity for any gas year up to “n” years ahead – existing rights not maintained
  - Within constrained period - introduce price rationing to ensure non-discriminatory release of capacity
  - Within unconstrained period - charges “locked-in” or set at prevailing rates

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Option 2. Extend permitted registration timescales - Overview of model

- Capacity application
  - Ability to request capacity up to “n” years ahead
- Capacity allocation
  - Constrained period
    - Allocate through “pay-as-bid” allocation process up to a “baseline”
  - Unconstrained period
    - Allocate if aggregate requests within baseline or meet incremental release threshold
      - minimum of “z” years of capacity requested
    - Pay prevailing use of system charges or “lock-in”

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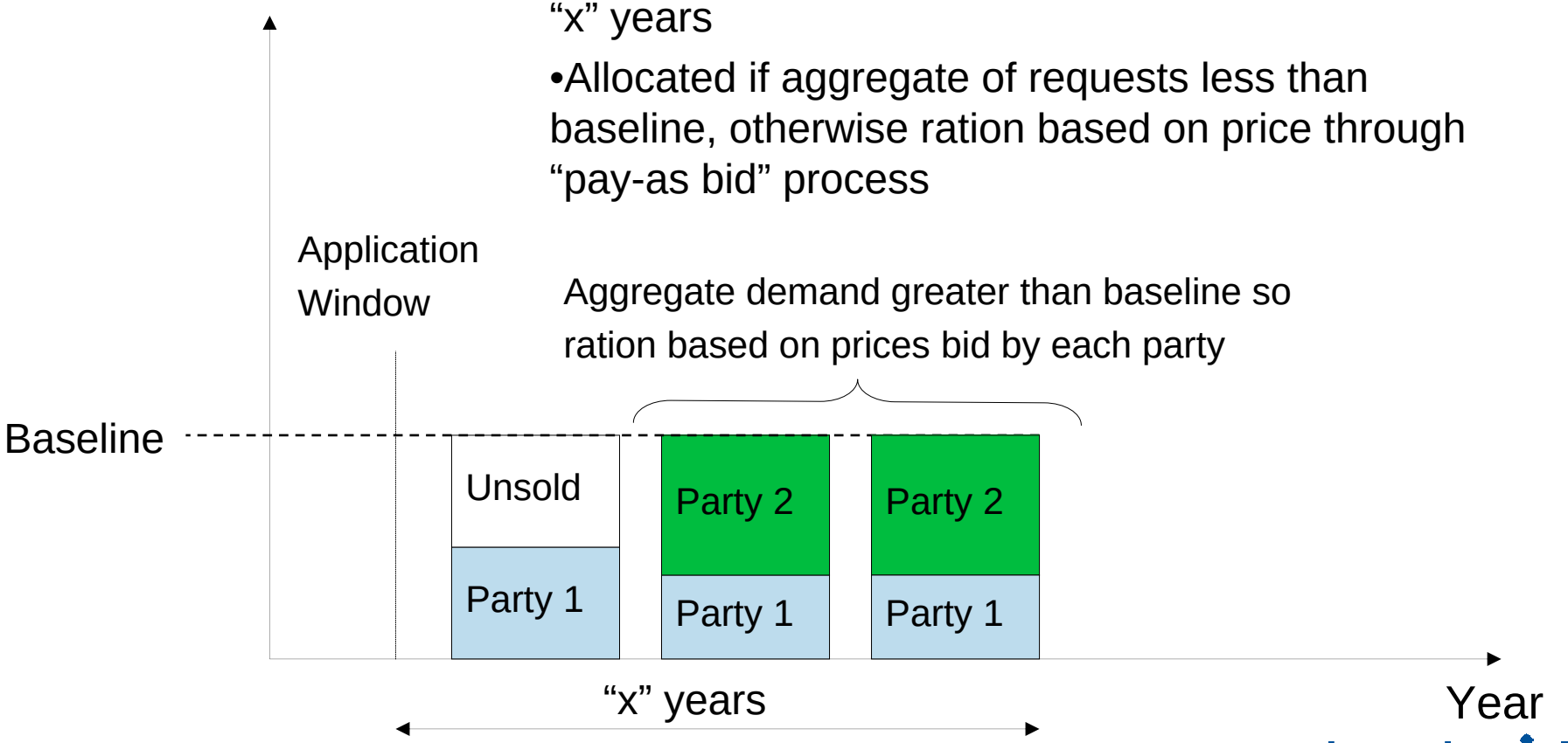
Option 2. Extend permitted registration timescales – Constrained Release

- Requests received at Application Window for capacity rights for any year in constrained period of "x" years
- Allocated if aggregate of requests less than baseline, otherwise ration based on price through "pay-as bid" process



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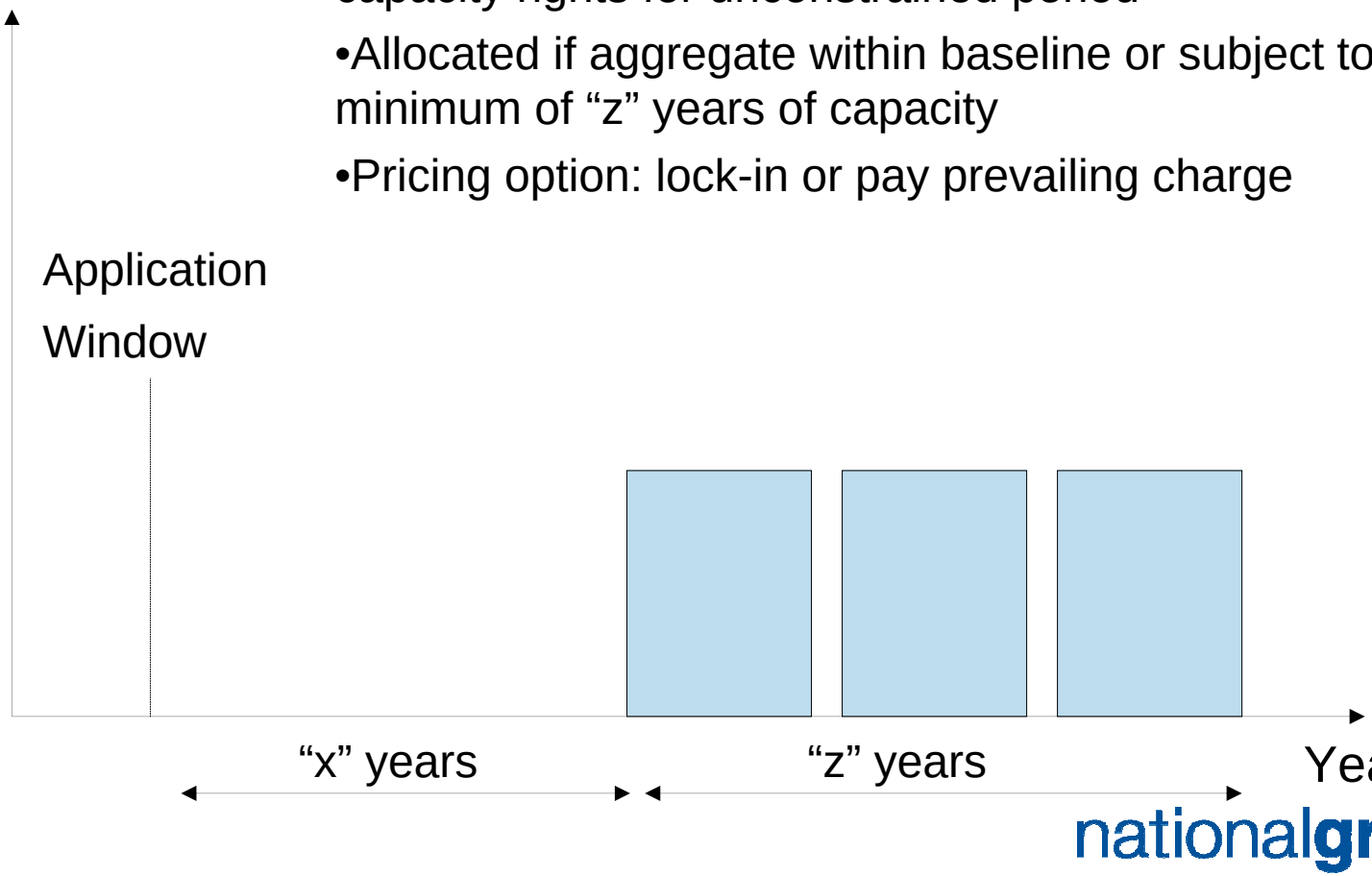
Option 2. Extend permitted registration timescales - Unconstrained Release

- Requests received at Application Window for capacity rights for unconstrained period
- Allocated if aggregate within baseline or subject to minimum of “z” years of capacity
- Pricing option: lock-in or pay prevailing charge



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Option 3. Implement long term auctions - Principles

Build on option 2 to introduce fully financially firm access arrangements…..

- Long term auctions introduced
  - Users required to bid against incremental step prices to secure release of required quantity of incremental capacity

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Way Forward

- Does the EOWG see merit in further development of any of these options?
  - Option 1. Implement consistent arrangements
  - Option 2. Extend permitted registration timescales
  - Option 3. Implement long term auctions
- If so, what needs to happen between now and next EOWG?
- Alternatively, are there other approaches that should be considered?

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