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Promoting choice and value for all customers

11th July 2006

Dear Colleague

National Grid's Winter 2006/07 Consultation Document July 2006

Ofgem has published today National Grid's (NG) second Winter 2006/07 Consultation Document[1]. This signals the second phase of the consultation process to develop gas and electricity supply-demand outlooks for winter 2006/07.

This report reflects feedback on NG's May document[2]. We very much welcome all of the views received from respondents and the time taken by everyone to feed into this process. This feedback has helped NG develop its analysis of the outlook for the coming winter, and provide a more robust outlook for the industry and customers to plan for the challenges ahead. I strongly encourage everyone to respond to this second phase of the consultation to assist NG in developing a robust final outlook for winter 2006/07 that will be published in September of this year.

Overall, NG's assessment of the gas supply balance remains broadly the same as that outlined in the May report. NG's forecast gas supplies from the UK Continental Shelf have been confirmed by offshore producers through NG's Transporting Britain's Energy (TBE) process. The outlook for new gas imports and storage positions have broadly been maintained on the back of feedback received through the consultation. At the time the May document was published, we identified a number of key issues and uncertainties affecting the winter supply position. We provide a brief update on each of these issues in this letter.

On the demand side, NG has made a significant reduction in its gas demand forecasts because of the impact of much higher gas prices on demand for all customers including domestic and small business customers. This has reduced NG's estimate of the levels of demand side response that could be required this winter.

NG has not made any significant adjustments to its electricity market assessment since the May consultation document and continues to indicate that forecast margins remain healthy even under severe weather conditions. With the gas supply/demand balance remaining tight, gas fired electricity generation is likely to continue to provide a valuable source of flexibility to the gas market as it did last year. But significant problems in the gas market could spill over into the electricity market as some gas fired generation will be required during periods of peak electricity demand.

[1] 'Winter 2006/07 Consultation Document', NG, July 2006 available on Ofgem's website: www.ofgem.gov.uk.
[2] 'Winter 2006/07 Consultation Document', NG, 16 May 2006 available on Ofgem's website: www.ofgem.gov.uk.

Key issues revisited

Below we provide an update on the key issues that could affect gas supplies this winter:

Gas supplies

- **the timely completion and utilisation of new import infrastructure:** construction delays and/or low utilisation of the four new potential sources of gas supply (the BBL interconnector from the Netherlands, the Langeled pipeline from the Norwegian Continental Shelf, the second enhancement to the Belgian interconnector and the proposed new LNG deliveries at Teesside) could result in much tighter supplies than last winter. There have been no delays announced to any of the projects since May but clearly the risks still remain at this stage;

- **availability of Rough storage facility**: Gas is now being injected into Rough following the outage in February this year. The Rough storage facility is approximately 68 percent full and on track to be full for the start of winter, with full production rates expected to be available no later than October 01. Despite the positive news, there remains the risk that there could be delays to the injection programme over the course of the summer and Rough may not be full going into the winter;

- **availability of UK North Sea gas supplies**: in May NG noted that the incident at Rough highlighted potential safety issues with equipment that may be used on other UK gas fields. South Morecambe has since been identified as the only other field using the same type of units as the Rough platform. The South Morecambe field is expected to return to full production by September.

Given these ongoing risks and uncertainties, it remains vital that companies in the UK, Norway and Continental Europe continue to participate in NG's consultation process ahead of the publication of the final report in September.

Gas demand

NG has made a significant reduction in its estimate of the level of demand side response required under all scenarios. We would encourage the major energy suppliers to respond to NG's questions on whether its forecasts and assumptions are reasonable particularly in a very cold winter. Suppliers should have the best information on how their customers' demand will be affected by rising prices under different weather conditions.

As part of the May consultation, NG asked the Distribution Network Operators (DNOs) for information on the demand levels at which they would trigger their rights to interrupt customers. A number of DNOs have been unable to provide this data to NG in time for publication of this report. We expect all DNOs to provide NG with the information they require and welcome NG's commitment to include a full set of this data (in mcm/day) as part of the final outlook report to be published in September.

Consultation process

We would like to thank once again all those market participants, customers and other interested parties who have taken the time to attend either of our first two Winter 2006/07 seminars. The seminars have been designed to give parties additional opportunities to participate in the Winter 2006/07 consultation process further than feedback received in the consultation. We are continuing these seminars over the lead up to winter - timetable as follows:

Date	Event	Location
16-May	Winter 2006/07 first consultation	Available on Ofgem's website
24-May	Winter 2006/07 seminar	London - Presentation materials available on Ofgem's website
2-Jun	Winter 2006/07 seminar	Edinburgh - Presentation materials available on Ofgem's website
07-Jul	Winter 2006/07 second consultation	Available on the Ofgem website
20-Jul	Winter 2006/07 seminar	Ferrybridge power station
Late September	Winter 2006/07 final report	Available on the Ofgem website
27-Sep	Winter 2006/07 seminar	Birmingham

As above, the next Winter 2006/07 Seminar will be held on **20 July** at **Ferrybridge Power Station**. Could requests to attend this or any other of Ofgem's Winter 2006/07 seminars please be sent to wholesale.markets@ofgem.gov.uk.

Initiatives ahead of winter 2006/07

To date, there has been two new modification proposals raised with a view to implementation ahead of winter 2006/07[3]. Once these proposals have completed their respective consultation processes and have been submitted to Ofgem for a decision, we will aim to take our decisions quickly to give the market as much notice as possible ahead of the winter.

Below, we set out an update on our own initiatives ahead of winter 2006/07. These are set out below:

- **Working with government, customers and market participants:** We continue to work to ensure that the government, customers and market participants are kept fully briefed on developments of the work undertaken ahead of winter 2006/07 and progress during next winter for example via steering groups and our seminar series.

- **Demand Side Working Group:** We continue to chair the work of the DSWG, working alongside customers and shippers to identify and develop further ways in which potential barriers to providing demand side response can be removed.

- **Customer and Supplier seminars:** We have held a number of 'Options for Energy Buyers' seminars that are designed to help customers gain a better understanding of the commercial options which are available to them through a series of supplier presentations. We are continuing this seminar series over the lead up to winter, including seminars covering the outlook for winter 2006/07.

- **Information issues**: There will also be greater information available to the wider market on gas flows onto the network this winter because of Ofgem's decision to approve UNC Modification Proposal 006. We have also completed a number of meetings with major European suppliers and transporters and have shared what we have learned through our seminar series. We are also continuing to push for more transparency in European gas markets (e.g. European gas flows and storage stock

[3] These proposals are UNC modification proposal 0086 'Introduction of Gas Demand Management Reserve Arrangements', raised by Gaz de France, and UNC modification proposal 0088 'Extension of DM service to enable Consumer Demand Side Management', raised by Total Gas & Power.

information) and in the UK where appropriate (e.g. distillate stocks at gas fired power stations, stocks at Grain LNG/Medium Range Storage).

- **New incentives on NG:** We will soon publish our final proposals for new incentives for NG for this winter covering;

    - Improved website performance in respect of key market information; and
    - Improved gas demand forecasting.

  These incentives were developed through discussions with the Ofgem led DSWG and Gas Safety Reserve work groups.

- **Gas safety reserve**: We are continuing our work to consider whether any improvements can be made to the existing safety monitor arrangements over the medium term.

Gas quality: technical study into blending opportunities

NG has published a summary of the study feasibility of blending at Bacton as Annex C in the July outlook report. NG will publish the full report in the next three weeks. The study concludes that it is technically feasible to offer a gas blending service at Bacton. But NG does not think it will be technically possible to make the necessary investment in new systems and measuring equipment in time for this winter. We would welcome views on the report, NG's assessment and on whether parties consider NG should continue to look at developing this service for next winter.

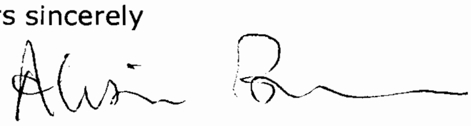
Demand forecasting: review of methodology

NG has also published a review of NG's gas demand forecasting methodology, commissioned by Ofgem. The report indicates that as a whole NG's forecast methodology is sound but makes a number of recommendations about how NG could improve their forecasting in the light of experience last winter. We would again welcome views on this report and its recommendations. NG has claimed that it has intellectual property rights over some of this material and has removed certain sections of the report. We would welcome views on whether the publication of a full version of this report would help market participants and customers understand NG's forecasts and prepare for the winter.

Way forward

Finally, I would like to once again thank all those companies, customers and other key stakeholders who found the time to participate in the first stage of NG's Winter 2006/07 consultation process - by either responding to the May document or attending our Winter 2006/07 seminars in London and Edinburgh. It remains important that all market participants respond to the consultation and provide as much information as possible. I hope that despite the busy time facing us all that you will all be able to continue to find the time to contribute to this process.

Yours sincerely



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