

National Grid House Warwick Technology Park Gallows Hill, Warwick CV34 6DA

Indra Thillainathan Senior Analyst, Gas Distribution Policy Ofgem 9 Millbank London SW1P 3GE

Nigel Sisman nigel.sisman@uk.ngrid.com Direct tel +44 (0)1926 656375 Mobile +44 (0)7778 030716

www.nationalgrid.com

21 July 2006

Our Reference: nks/060721_DN_Embedded_interim_treatment Your Reference: 116/06

Dear Indra

New entry arrangements for connecting to the gas distribution network – Holford interim treatment

Thank-you for the opportunity to respond to this consultation.

The issues in this consultation, particularly with regard to the proposed interim Hoford arrangements, affect both the transmission and distribution businesses of National Grid. This response is made on behalf of the UK Transmission business.

Appendix 1 provides background and articulation of the NGG NTS position. We also include Appendix 2 which describes the proposal for the interim period that has been developed jointly with, and is supported by, the UK Distribution business

National Grid Gas NTS (NGG NTS) does not believe, for the interim period, that it is desirable or necessary to contemplate a modification to NGG NTS's licence to deem Holford an NTS Entry Point to facilitate Holford's interim access to the Total System and specifically "access to the NBP".

NGG NTS considers that an interim arrangement, to enable Holford to both inject and withdraw gas from the storage facility and to access the NBP can be achieved with an approach that avoids much of the complexity associated with requiring NTS Entry Capacity to enable such gas to access the Total System.

The proposal is necessarily pragmatic and expedient. NGG NTS supports the Ofgem view that a temporary but short lived arrangement might be appropriate. The proposal would enable Holford to function as a commercial storage facility this autumn therefore permitting time to consider the potentially fundamental issues raised by the DN embedded entry issue and how an enduring framework to address DN embedded entry and particularly embedded storage might be implemented.

The enduring framework needs careful consideration given the complexities of the interactions and the likelihood of conflicts arising from the many objectives. The enduring proposals should reflect an assessment of the potential scale for future DN embedded entry. The primary objective should be to

ensure that decisions are made to ensure that new connections are made to whichever network might generate the most economic and efficient outcome whilst ensuring that transporters are fairly treated. Specifically the regime should minimise risks to both transporters and consumers of inefficient connection or by-pass.

Furthermore NGG NTS would advocate the complexity of the enduring framework is proportionate to the risks and issues being addressed. This should be influenced by the anticipated scale of impacts on both the physical systems of the relevant transporters (including the consequently knock-on effects to the NTS) and the extent to which these facilities might deliver commercial services to the wider market.

Developing an enduring framework will require substantial effort and commitment and may require substantial changes to UNC, Licences (both NTS and DN) and Charging Methodologies (both NTS and DN).

NGG NTS therefore believes that a simple, pragmatic and expedient approach to enable Holford to offer commercial services to the market from the autumn of this year for one gas year pending the establishment of the enduring framework is appropriate.

NGG NTS would have preferred to have addressed the issue of the other DN embedded entry points within the changes necessary to address Holford's access. However in the context of ensuring the maximum likelihood of Holford access it may be appropriate to resolve the other DN embedded entry points as part of the establishment of the enduring framework.

The first attachment to this response provides some background to the NGG NTS position and describes much of the detail of the recommended approach. The second appendix is a joint note prepared with the relevant DN to describe the recommended approach.

NGG NTS has also had some preliminary discussions with xoserve to establish the viability of the approach from an IT systems and business process perspective.

The NGG NTS view is that implementation of a UNC modification proposal could enable Holford to deliver commercial services by this autumn.

Yours sincerely

Nigel Sisman

cc. Phil Lawton, NGG UKD

Appendix 1

NGG NTS' response

116/06 "New entry arrangements for connecting to the gas distribution network"

Interim framework to enable Holford to offer commercial storage services

Background to NGG NTS position

NGG NTS recognises that the objective of the interim proposal is to provide an ability for Holford to provide commercial services to shippers from autumn 2006. NGG NTS notes that the ¹116/06 consultation document considers that this is achieved by granting Holford "access to the NBP". NGG NTS regards the NBP as a feature of the balancing regime.

• The balancing regime

To facilitate the operation of the market and to avoid the complexity of individual users having to balance physical inputs and offtakes from the Total System the UNC features the NBP concept.

The NBP is the notional point at which UNC users are able to trade gas. An NBP trade is effectively a transfer of gas from one user to another. The trade debits the seller's daily imbalance account and credits the purchaser's account.

Essentially user daily balances are derived taking account of their physical inputs to the Total System (User Daily Quantity Input - UDQI), net traded quantities and physical offtakes from the Total System (User Daily Quantity Output – UDQO).

Therefore for players with physical inputs and outputs from the Total System access to the NBP for such "physical gas flows" involves an ability to be able to record input and offtake flows from the Total System.

This is achieved by having meters on the commercial IT system (Gemini) that enables the recording of the relevant contributions to a User's UDQI and/or UDQO for each day.

UNC Users face exposure to balancing regime charges including imbalance cashout, and (for those with physical inputs or offtakes) scheduling and daily neutrality net cost or benefit redistribution.

• Transportation service

Access to the NBP does not require NTS Entry Capacity. Users have access to, and pay for, the transportation services that they use in respect of physical gas flows onto and out of the Total System.

DN embedded entry points will be receiving physical access services from the network to which they are connected. It is the NGG NTS view that therefore there should be some consideration

¹ New entry arrangements for connecting to the gas distribution network 116/06 7 July 2006 Ofgem consultation document

within the contractual access arrangements between the DN and either the connectee or Users who are using, or providing the service. The issue of NTS charges in respect of commercial access to the system is an entirely separate manner.

As an interim, and particularly given that we do not anticipate that within the interim timescale there is any scope for receiving investment signals to the NTS and given that the indirect impacts on physical flows in the NTs are anticipated to be small, NGG NTS would not see merit, in its role as a transportation service provider, in charging for NTS entry services in respect of the Holford DN embedded entry.

Indeed the provision of NTS entry service to Holford in the interim (as currently defined in both NGG NTS' Licence and the UNC) would imply significant complications including

- o the difficulty of setting an NTS baseline and UCA
- \circ $\,$ enabling longer term capacity access beyond the suggested interim period $\,$
- \circ $\;$ addressing the issues associated with NGG NTS' exposures to buy-back risks
- o complicating management reporting of NTS capacity sales.

Therefore, and in the context of the interim period, NGG NTS does not believe Holford (or users at the facility) should be contracting and potentially paying for what can only be regarded as a virtual service from the NTS.

It is therefore the NGG NTS view that a proportionate and expedient approach to addressing the Holford system entry requirement would be to contemplate the entry as a DN Entry Point rather than an NTS Entry Point.

However when the enduring arrangements are considered the potential scale of impacts associated with DN embedded entry will need to be carefully considered. Whilst DN embedded entry flows are anticipated to be small and to have relatively minor impacts on NTS/DN offtake flow patterns then it might be sufficient to regard the current OCS booking and DN operational interface approaches to provide adequate information to the NTS for planning, development and operational purposes. This is unlikely to be the case if flows are larger. In extremis, should there be any scope for reverse flow at any offtake at the NTS/DN interface, we would need to address the fundamentals of both physical operation of the network and the commercial framework. Additionally, and even in the context of relatively modest DN embedded entry flows, the enduring regime might need to contemplate whether any explicit service charge for commercial access to the NBP would be appropriate.

The next section considers the service and charging elements that would need to be considered in the context of the interim approach.

Holford's interim access to both the NBP and transportation service

Essentially the preferred approach involves setting up :

- LDZ offtake meter
- LDZ entry meter

to respectively address injection, and withdrawal, of gas to, and from Holford.

The approach assumes that the relevant DN will have secured connection terms with the Holford operator that would define the necessary operator-to-operator arrangements. This would have to be completed regardless of the commercial framework definition.

In this section NGG NTS will focus on the balancing regime and NTS transportation issues. A key feature of the proposal is that it is designed to fit with current processes, procedures and current Gemini system functionality. This is essential to ensure that timely access to service can be achieved without requiring substantial IT systems and business process changes given the very short timescales available for defining, effecting the necessary framework changes (which NGG NTS can be delivered via a UNC modification proposal) and implementing the necessary changes.

Initial discussions with xoserve have supported the view that the proposal can be implemented in a timely way having regard to IT systems and business processes although, if the proposal is considered acceptable, it would be prudent to run an end-to-end test to confirm its viability particularly in the light of confirmation of the preferred LDZ transportation service and billing arrangements.

Similarly an initial discussion with National Grid lawyers has provided an initial view of the acceptability and deliverability of the proposal from a UNC drafting perspective.

• Balancing regime

Holford would be treated in an analogous manner to any other system offtakes and inputs within the LDZ eg:

- o Exit nominations would feed demand attribution processes
- Exit nominations would feed shipper and national projected imbalance calculations
- o End of day exit allocations would be determined (possibly involving an agent)
- o Exit allocations would contribute to shipper's UDQO
- Exit nominations and allocations would be used to determine scheduling charges
- o Exit allocations would attract relevant daily gas balancing neutrality credits/charges
- o Entry nominations would influence projected LDZ stock change
- Entry nominations would feed shipper and national projected imbalance calculations
- o End of day entry allocations would be determined (possibly involving an agent)
- o Entry allocations would contribute to shipper's UDQI
- o Entry nominations and allocations would be used to determine scheduling charges
- Entry allocations would attract relevant daily gas balancing neutrality credits/charges
- NTS "transportation" charging

NGG NTS view is that whilst NTS charges are designed to recover the costs of both transportation services (in so far as they relate to the physical transportation of gas) and the market facilitation activity these roles are not clearly delineated within the current NTS charging structure which is based upon TO/SO, and capacity/commodity charge splits.

The issue of access to the NBP in the context of entry access downstream of the NTS raises significant issues. This is a fundamental policy question that should be confirmed before work starts in earnest to define an enduring DN entry regime. This policy question should be considered in the context of the scale and scope for DN entry and the potential risks for such entry flows to have consequential impacts on the NTS arising from potential bypass and/or indirect impacts on NTS capacity utilisation particularly in the context of offtake flow rate variations. Should DN embedded entry access to the NBP become an enduring feature of the regime then it might be appropriate to consider whether some market facilitation/access charge (beyond current balancing charges, transportation charges and their associated redistributions) might be appropriate.

Without prejudice to any enduring regime NTS charging structure NGG NTS believes that a pragmatic way forward to support Holford for the interim period would be that:

o NTS Entry capacity would not need to be procured

The designation of Holford withdrawal as DN entry would avoid all the complexity that would not be warranted in respect of treating Holford as NTS entry. NGG NTS understands that this is deliverable from an IT system perspective.

NTS Exit capacity charges could be avoided

If Holford injection were to be treated as an interruptible supply point then the current systems would not attribute NTS exit capacity to the Holford (DN exit) capacity holdings. Current IT systems would automatically attribute NTS Exit capacity to the DN exit point should it be designated firm within the DN.

NGG NTS understands that the relevant DN is proposing interruptible exit service definition. Current IT systems and processes will therefore support the desired outcome with respect to these charges.

NTS TO Entry commodity charge

This charge item is designed to address under-recovery of TO allowed revenue and hence it does not seem appropriate for Holford to pay this charge. We have confirmed that it is possible to set up the Holford withdrawal (system entry meter) so that allocated gas flows do not attract the NTS TO Entry Commodity charge.

NTS SO Commodity charge

This charge is generally regarded as providing for NTS SO activities apportioned over NTS entry and offtake flows.

This would imply that the charge should not apply in respect of DN embedded entry flows. This treatment can be accommodated via existing systems and processes.

Unless explicit action is taken in the context of routinely generated NTS SO commodity charges then, in respect of both the NTS – Holford and Holford – end-user physical gas journeys, the allocated DN exit flows would attract NTS exit commodity charges. From a transportation charging perspective it might be considered preferable to charge only one journey (which could be achieved via amending processes not to bill NTS exit commodity against injections into Holford). However given that an implicit market access fee is embedded within the NTS SO allowed revenue stream it might be considered to be more appropriate to charge NTS SO exit commodity charges on Holford injection quantities.

Given that the current processes would effectively charge NTS SO commodity on both injections into Holford and subsequently when the gas is consumed by users then NGG NTS would advocate this as the preferred position.

Implementation of the proposal

Given the urgency attached to this issue NGG NTS would advocate implementation of this proposal via a UNC modification proposal avoiding the need for Licence and Charging Methodology changes.

Appendix 2

Interim approach to afford Holford DN entry for Gas Year 2006/7

National Grid plc

Joint proposal developed by NTS and UKD

Background

The issues raised in Ofgem's consultation document "New entry arrangements for connecting to the gas distribution network" (116/06) affect both National Grid's UK transmission and UK distribution businesses.

This is an alternative to Ofgem's proposals for the interim period, which has been jointly developed by these organisations.

Objectives

To provide Holford access to the system for a 1 year temporary period To minimise framework changes

- avoiding Licence changes (NTS & DN)
- avoiding charging methodology changes (NTS & DN)
- o minimise requirements for regulatory effort/oversight (eg UCA setting)
- to deliver a solution via implementation of a single, simple UNC modification proposal
- o to deliver a solution using existing IT systems, processes and procedures
- to minimise the risk of unanticipated impacts particularly with regard to information and regulatory reporting issues

Proposal

The proposal would define a requirement for a UNC modification proposal. It's principle aim would be to do define that in respect of DN entry points not referenced in the NTS that NTS will not be responsible for allocating system entry rights but rather this is a matter for the relevant transporter.

The proposal is based on Holford requiring only interruptible entry and exit capacity in the interim period.

The proposal would regard the Holford facility as both a DN CSEP exit point (corresponding to the offtake of gas into the Holford facility (injection into Holford)) and a DN entry point (corresponding to the input of gas into the DN (withdrawal from Holford)).

The proposal is capable of implementation via existing IT system functionality, and current processes and procedures.

The NTS and DN transportation charging arrangements are consistent with the existing charging methodologies and so no consultation on changes to the existing methodologies for the interim period would be envisaged.

Furthermore the proposal is not envisaged to require either NTS or DN Licence amendment.

The following illustrate the financial consequences of the arrangements:

Holford exit treatment (injection into Holford) - DN CSEP approach for "system exit" purposes

		Charges	Comment
Capacity	LDZ System CSEP capacity	None	Service delivery via interruptible service anticipated so no DN capacity charges applicable
	LDZ Customer charge	None	No charge to be levied, as for other CSEPs
	NTS exit capacity	None	DN interruptible service and existing processes ensure no NTS exit capacity charges applicable
Commodity	LDZ System CSEP commodity	Yes	Charges levied on the basis of User Daily Quantity Output at CSEP
	NTS SO exit commodity charge	Yes	Charge levied on the basis of User Daily Quantity Output at CSEP

Holford entry treatment (withdrawal from Holford)

		Charges	Comment
Capacity	DN entry capacity	None	interruptible entry service defined in connection arrangements – no transportation charges to be levied in interim period
	NTS entry capacity	None	Combination of DN entry arrangements and IT system meter configuration to ensure no NTS entry related charges apply in interim
Commodity	DN entry commodity	None	No charges to be levied in interim period
	NTS SO entry commodity charge	None	No charge to be levied in interim period

Daily Balancing Regime Treatment

Nominations, physical flows and allocations treated in a similar way to any other contributions to (User Daily Quantity Input) UDQIs and (User Daily Quantity Output) UDQOs for the purposes of all balancing processes including demand attribution, User balancing and invoicing thereby ensuring "access to the NBP" and exposure to gas balancing payments/charges

DN Connection Agreement

A DN Connection Agreement will also be required covering the one-off connection charge, operational and other requirements.