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Dear Steve,

Proposed amendments to National Grid Gas National Transmission System's (NG NTS) System Management Principles Statement (SMPS)¹

The Gas and Electricity Markets Authority (the Authority²) has carefully considered the issues raised in the consultation on NG NTS's SMPS issued in January 2007 and the subsequent Report to the Authority submitted by NG NTS to the Authority in March 2007 (the 'Authority Report').

NG NTS recommended that no changes be made to the current version of the SMPS (2.3). The Authority agrees that, at the time of the January consultation, no modification was required to the SMPS as set out in the Authority Report. However, the Authority acknowledges that the approval of Uniform Network Code (UNC) 125³ on 1 February 2007 raised a number of issues relevant to the SMPS and welcomes NG NTS's commitment to undertake a further consultation on these issues going forward.

This letter explains the background to the no change recommendation and sets out the Authority's views on the issues raised during consultation.

The proposed revisions

NGG NTS did not propose any changes to the SMPS in its January 2007 consultation.

Respondent's views

There was one response received in relation to the January 2007 SMPS consultation⁴. This respondent was of the view that due to recent changes to the market and to the

1 The SMPS defines the broad principles and criteria by which NG NTS, in its role as System Operator, will use balancing tools and other measures to assist in the operation of the transmission system. NG NTS prepares a SMPS in accordance with special condition C5(5) of its gas transporters licence.

2 The terms "Ofgem" and "the Authority" are used interchangeably in this letter. Ofgem is the Office of the Gas and Electricity Markets, which supports the Gas and Electricity Markets Authority (the "Authority"), the regulator of the gas and electricity industries in Great Britain. Ofgem's primary aim is to bring choice and value to all gas and electricity customers by promoting competition and regulating monopolies. The Authority was established by the Utilities Act 2000 and its powers are provided for under the Gas Act 1986, the Electricity Act 1989, the Competition Act 1998, the Utilities Act 2000, the Enterprise Act 2002 and the Energy Act 2004.

3 Uniform Network Code (UNC) 125: Introduction of new balancing neutrality charge for cost of residual balancer collateral on the OCM. A copy of the decision letter can be found on the Gas Transporters Information Service Site

4 The consultation response received can be found in Appendix B of the Report to the Authority

utilisation of the NTS, NG NTS's operation of the system and responses to incentives has changed. The respondent suggested a number of amendments to the SMPS where they believed improvements could be made and also considered that a full review of the SMPS is required in order to ensure that NG NTS is given better guidance, which in turn will allow the market to operate with minimum interference⁵.

NG NTS's view

While NG NTS, in its Report to the Authority, acknowledges the issues raised by the respondent, it is NG NTS's overall view that it would not be appropriate to consider these proposed SMPS (and where necessary, UNC) amendments without industry wide consultation held via the appropriate UNC governance channels. NG NTS has also stated that if the respondent believes there is benefit from discussing these issues at the UNC Transmission/Distribution Workstreams, it would welcome and contribute fully to such an approach.

NGG NTS's recommendation

NGG NTS considers that the version of the SMPS (2.3)⁶ which has been consulted upon should remain unchanged, and therefore recommends that this version be approved by the Authority with an effective date of 1 April 2007.

Ofgem's view

Ofgem's principal objective is to protect the interest of consumers, wherever appropriate by promoting effective competition⁷. Having regard to its principal objective and to its wider statutory duties, Ofgem agrees that the current version of the SMPS (2.3) should remain unchanged, effective as of 1 April 2007.

With regard to the approval of Uniform Network Code (UNC) 125⁸ on 1 February 2007, Ofgem in its decision letter recognised the concerns raised by some respondents regarding the transparency of NGG NTS's proposed arrangements. Ofgem recognises that NGG NTS's actions will be subject to external oversight as part of its annual System Management Principles Statement and Procurement Guidelines audit, however Ofgem would encourage parties to respond to the further consultation on these issues as committed to by NG NTS.

Other issues

Ofgem notes that the one respondent to the consultation flagged several areas where additional clarity or detail could be provided. Ofgem encourages market participants to highlight potential enhancements to the SMPS to NG NTS for its consideration, as part of its upcoming review under special condition C5(8) of its gas transporter licence.

The Authority's decision

Having regard to the above, the Authority agrees that, as at the time of NG NTS's January consultation, no change was required to be made to the current version of the

⁵ A summary of the response received can be found in National Grid NTS's Report to the Authority

⁶ The version of the SMPS (2.3) consulted upon can be found on National Grid's website: www.nationalgrid.com

⁷ Section 4AA of the Gas Act 1986

⁸ Uniform Network Code (UNC) 125: Introduction of new balancing neutrality charge for cost of residual balancer collateral on the OCM. A copy of the decision letter can be found on the Gas Transporters Information Service Site

SMPS (2.3). However, the Authority acknowledges that the approval of Uniform Network Code (UNC) 125 on 1 February 2007 raised a number of issues relevant to the SMPS and welcomes NG NTS's commitment to undertake a further consultation on these issues going forward.

If you have any queries in relation to the issues raised in this letter, please feel free to contact Claire Rozyn on 020 7901 7216.

A handwritten signature in black ink, appearing to read "Sonia Brown".

| Yours sincerely

Sonia Brown

Director, Wholesale Markets