

**MODIFICATION OF THE SPECIAL CONDITIONS OF NATIONAL GRID GAS PLC'S GAS TRANSPORTER LICENCE IN RESPECT OF ITS NATIONAL TRANSMISSION SYSTEM UNDER SECTION 23 OF THE GAS ACT 1986**

**NOTICE OF THE REASONS FOR THE DECISION TO MODIFY THE SPECIAL CONDITIONS OF NATIONAL GRID GAS PLC'S GAS TRANSPORTER LICENCE IN RESPECT OF ITS NATIONAL TRANSMISSION SYSTEM UNDER SECTION 38A OF THE GAS ACT 1986**

1. National Grid Gas plc ("NGG") holds a gas transporter licence (the "licence") in respect of its National Transmission System ("NTS") treated as granted pursuant to section 7 of the Gas Act 1986 (the "Act").
2. In accordance with section 23(3) and (4) of the Act, the Gas and Electricity Markets Authority (the "Authority"):
  - (a) gave notice (the "Notice") on 21 March 2007 that it proposed to modify the special conditions of the licence in accordance with the Schedule to the Notice;
  - (b) published the Notice in the manner it considered appropriate; and
  - (c) served a copy of the Notice on NGG.
3. The Authority gave notice of its intention to make the proposed licence modifications to the Secretary of State. The Authority did not receive a direction from the Secretary of State not to make the proposed licence modifications before the relevant time specified in the Notice.
4. The Authority received two representations (in addition to NGG's consent) in relation to the proposed licence modifications before the relevant time specified in the Notice. No representations were withdrawn. The Authority has carefully considered all representations made in relation to the proposed licence modifications and not withdrawn.

All non-confidential representations made in relation to the proposed licence modifications are available free of charge from the Ofgem Research and Information Centre, 9 Millbank, London SW1P 3GE or from the Ofgem website at [www.ofgem.gov.uk](http://www.ofgem.gov.uk).
5. It has come to the Authority's attention that a clarificatory amendment is required. In the definition of "pension costs", which appears in paragraph 5 of the Schedule to the Notice, the reference to "transportation system" should be replaced by a reference to "transportation business" since the definition applies in the context of a pension scheme.
6. NGG has given its written consent to the modifications proposed in the Notice, with the inclusion of the amendment set out in paragraph 5 above.
7. The reasons for making the licence modifications are set out in the following documents published by the Authority:
  - (a) "National Grid Gas System Operator Incentives from 1 April 2007: Final proposals and statutory licence consultation", Ofgem, March 2007;

- (b) "National Grid Electricity Transmission and National Grid Gas System Operator Incentives from 1 April 2007: Initial proposals consultation", Ofgem, December 2006;
- (c) "National Grid Electricity Transmission and National Grid Gas System Operator Incentives from 1 April 2007: October consultation", Ofgem, October 2006;
- (d) "National Grid Electricity Transmission and National Grid Gas System Operator Incentives 2007-08 – Invitation to submit views", Ofgem, July 2006.

These documents are available free of charge from the Ofgem Research and Information Centre, 9 Millbank, London SW1P 3GE or from the Ofgem website at [www.ofgem.gov.uk](http://www.ofgem.gov.uk).

**THEREFORE:**

In accordance with section 23 of the Act, the Authority hereby modifies the special conditions of NGG's licence in accordance with the Schedule to this Modification with effect on and from 06:00 hours on 1 April 2007.

This document constitutes a notice of reasons for the decision to modify the special conditions of NGG's licence under section 38A of the Act.

**The Official Seal of the Gas and Electricity Markets Authority here affixed  
is authenticated by the signature of:**



**Sonia Brown**  
**Director, European Strategy and Sustainable Markets**  
**Duly authorised on behalf of the Gas and Electricity Markets Authority**

**19 April 2007**

## SCHEDULE

### MODIFICATION OF THE SPECIAL CONDITIONS OF NATIONAL GRID GAS PLC'S GAS TRANSPORTERS LICENCE IN RESPECT OF ITS NATIONAL TRANSMISSION SYSTEM UNDER SECTION 23 OF THE GAS ACT 1986

1. Special condition C8B (Restriction of revenue in respect of the NTS transportation owner activity and NTS system operation activity), Part 2 (The NTS system operation activity revenue restrictions) is amended as follows.
2. In paragraph 14(2) (NTS system operator incentive revenue (SOIR<sub>t</sub>)):
  - (a) for "ICIR<sub>t</sub>", where it appears, substitute "SOIntICR<sub>t</sub>";
  - (b) for "the last 6 months of formula year t=5 (i.e. 1 October 2006 to 1 April 2007)", substitute "formula year t=6".
3. In paragraph 14(3) (NTS system operation costs) (SOIC<sub>t</sub>):
  - (a) in the formula from which SOIC<sub>t</sub> is derived, "+ ICCP<sub>t</sub>" is omitted;
  - (b) the definition of ICCP<sub>t</sub> is omitted.
4. In paragraph 14(8) (System balancing incentive revenue (SBIR<sub>t</sub>)):
  - (a) in sub-paragraph (a), for "formula year t" where it appears, substitute "formula year t=6";
  - (b) in sub-paragraph (c) (The maximum system reserve incentive revenue (SRIR<sub>t</sub>)), for the definition of "SRIT<sub>t</sub>", substitute:

"SRIT<sub>t</sub> means the system reserve incentive target in respect of formula year t (in £m), which shall be derived in the following manner:

$$SRIT_t = ((RPAV_t \times 213) + (RPDY_t \times 116) + (RPGL \times 135) + (RPPA \times 266)) / 100 + 11$$

where:

RPAV<sub>t</sub> means the applicable price for reserved space, in formula year t (in pence per kWh per annum), with respect to the Avonmouth LNG storage facility, as determined by Special Condition C3;

RPDY<sub>t</sub> means the applicable price for reserved space, in formula year t (in pence per kWh per annum), with respect to the Dynevor Arms LNG storage facility, as determined by Special Condition C3;

RPGL<sub>t</sub> means the applicable price for reserved space, in formula year t (in pence per kWh per annum), with respect to the Glenmavis LNG storage facility, as determined by Special Condition C3;

RPPA<sub>t</sub> means the applicable price for reserved space, in formula year t (in pence per kWh per annum), with respect to the Partington LNG storage facility, as determined by Special Condition C3;”;

- (c) in sub-paragraph (d) (The NTS SO gas cost incentive target (GCIT<sub>t</sub>)), for the definition of “GVTP<sub>t</sub>” substitute:

“GVTP<sub>t</sub> means the NTS SO gas target volumes in respect of formula year t, as set out in the table below. The value of GVTP<sub>t</sub> is dependant upon the level of SFAF<sub>t</sub>, where SFAF<sub>t</sub> means the average daily gas flows through the St. Fergus terminal in mcm/day in the formula year commencing on 1 April 2007, calculated as:

$$\frac{(\text{Total annual volumetric flow through St Fergus terminal})}{366}$$

SFAF <sub>t</sub> (mcm/day)	GVTP <sub>t</sub> (GWh)
SFAF <sub>t</sub> > 100	8,312
85 ≤ SFAF <sub>t</sub> ≤ 100	7,129
SFAF <sub>t</sub> < 85	6,393”

5. For paragraph 14(10) (Internal cost incentive)), substitute:

“(10) Internal cost incentive revenue (SOIntICR<sub>t</sub>)

- (a) Principal formula

For the purposes of paragraph 14(2) of Part 2 of this condition, the maximum internal costs incentive revenue allowed to the licensee in respect of formula year t (SOIntICR<sub>t</sub>) shall be derived in the following manner:

$$\text{SOIntICR}_t = \text{IOIRC}_t + \text{ICEIRC}_t + \text{NC}_t$$

Where:

IOIRC<sub>t</sub> means the maximum internal operating cost incentive revenue allowed in respect of formula year t and shall be calculated in accordance with paragraph 14(10)(b) of Part 2 of this condition;

ICEIRC<sub>t</sub> means the maximum internal capital expenditure incentive revenue allowed in respect of formula year t and shall be calculated in accordance with paragraph 14(10)(c) of Part 2 of this condition;

NC<sub>t</sub> means the non incentivised costs allowed in respect of formula year t and shall be determined in accordance with paragraph 14(10)(d) of Part 2 of this condition.

**(b) Internal operating cost Incentive revenue (IOIRC<sub>t</sub>)**

For the purposes of paragraph 14(10)(a) of Part 2 of this condition, the maximum internal operating costs incentive revenue allowed to the licensee in respect of formula year t (IOIRC<sub>t</sub>) shall be derived in the following manner:

If  $\left[1 + \left(\frac{IRPI_t}{100}\right)\right] \times IOIT_t \geq IOC_t$ , then:

$$IOIRC_t = \left( \left[1 + \left(\frac{IRPI_t}{100}\right)\right] \times IOIT_t \right) - \left( \left( \left[1 + \left(\frac{IRPI_t}{100}\right)\right] \times IOIT_t \right) - IOC_t \right) \times (1 - ICUSF_t)$$

otherwise:

$$IOIRC_t = \left( \left[1 + \left(\frac{IRPI_t}{100}\right)\right] \times IOIT_t \right) - \left( \left( \left[1 + \left(\frac{IRPI_t}{100}\right)\right] \times IOIT_t \right) - IOC_t \right) \times (1 - ICDSF_t)$$

where:

IOIT<sub>t</sub> means the internal cost incentive target in respect of formula year t as set out in the following table:

Variable	Formula years				
	t=6	t=7	t=8	t=9	t=10
IOIT <sub>t</sub> £ million, 04/05 prices	24.2	23.2	25.4	24.6	24.2

IOC<sub>t</sub> means the operating costs incurred in respect of formula year t attributable to the provision of NTS SO activity in

accordance with Special Condition C9 (Allocation of revenues and costs for calculations under the price control in respect of the NTS transportation owner activity and NTS system operation activity) other than  $ExCP_t$ ,  $IECCC_t$ ,  $CNIC_t$ ,  $SBIC_t$ ,  $RBIC_t$ , Pension Costs and charges levied on the licensee by the agency (as defined in Standard Special Condition A15);

**Pension Costs** means the actual cash contributions made to the scheme in respect of both ongoing contributions and deficit payments attributable to the transportation business as well as scheme administration costs and payments made to the Pension Protection Fund (as defined under the Pensions Act 2004);

$ICUSF_t$  means the internal cost upside sharing factor in respect of formula year  $t$  as set out in the following table:

	Formula years				
Variable	t=6	t=7	t=8	t=9	t=10
$ICUSF_t$	0.4	0.4	0.4	0.4	0.4

$ICDSF_t$  means the internal cost downside sharing factor in respect of formula year  $t$  as set out in the following table:

	Formula years				
Variable	t=6	t=7	t=8	t=9	t=10
$ICDSF_t$	0.4	0.4	0.4	0.4	0.4

$IRPI_t$  in respect of formula year  $t$ , means the percentage change (whether of a positive or a negative value) between (a) the arithmetic average of the retail price index published or determined with respect to each of the six months from July to December (both inclusive) in formula year  $t-1$  and (b) 182.37 (being the value for  $t-1$  in 2004/05).

**(c) Internal capital expenditure incentive revenue (ICEIRC<sub>t</sub>)**

For the purposes of paragraph 14(10)(a) of Part 2 of this condition, the maximum internal capital expenditure incentive revenue allowed to the licensee in respect of formula year  $t$  ( $ICEIRC_t$ ) shall be derived in the following manner:

$$ICEIRC_t = ICED_t + ICER_t$$

where:

$ICED_t$  means the depreciation on the NTS SO regulatory asset base in respect of formula year t and is calculated on a straight-line basis using a life of seven years for assets;

$ICER_t$  means the return on the average NTS SO regulatory asset value in respect of formula year t at a rate of 5.05%;

“NTS SO regulatory asset value” means the allocation of assets to the NTS SO activity in accordance with Special Condition C9 (Allocation of revenues and costs for calculations under the price control in respect of the NTS transportation owner activity and NTS system operation activity); and has the value £40.3m (in 2004/05 prices) on 1 April 2007. Allowed internal capital expenditure ( $AICE_t$ ) shall be added to the NTS SO regulatory asset value in respect of any relevant year t;

$AICE_t$  means the allowed internal capital expenditure that shall be added to the NTS SO regulatory asset base in respect of any formula year t and is derived in the following manner:

$$AICE_t = \left( \left[ 1 + \left( \frac{IRPI_t}{100} \right) \right] \times ICET_t \right) - \left( \left( \left( \left[ 1 + \left( \frac{IRPI_t}{100} \right) \right] \times ICET_t \right) - ICE_t \right) \times 0.75 \right)$$

where:

$ICET_t$  means the internal capital expenditure target in respect of formula year t as set out in the following table:

Variable	Formula years				
	t=6	t=7	t=8	t=9	t=10
$ICET_t$ £ million, 04/05 prices	12.8	8.3	6.5	10.8	10.3

$ICE_t$  means the internal capital expenditure allocated to the NTS SO activity in accordance with Special Condition C9 (Allocation of revenues and costs for calculations under the price control in respect of the NTS transportation owner activity and NTS system operation activity) in respect of formula year t.

**(d) Non-incentivised costs ( $NC_t$ )**

For the purposes of paragraph 14(10)(a) of Part 2 of this condition, the non-incentivised costs allowed to the licensee in respect of formula year t ( $NC_t$ ) shall be derived in the following manner:

$$NC_t = (IT_t + IP_t + IX_t) \times \left[ 1 + \left( \frac{IRPI_t}{100} \right) \right]$$

where:

$IT_t$  means the licensee's tax allowance in respect its NTS system operation activity in respect of formula year t as set out in the following table:

Variable	Formula years				
	t=6	t=7	t=8	t=9	t=10
$IT_t$ (£ million, 04/05 prices)	3.1	2.1	1.3	0.0	-0.4

$IP_t$  means the licensee's pension cost allowance in respect of its NTS system operation activity in respect of formula year t as set out in the following table:

Variable	Formula years				
	t=6	t=7	t=8	t=9	t=10
$IP_t$ (£ million, 04/05 prices)	6.7	6.9	6.8	7.1	7.1

$IX_t$  means the relevant proportion (in respect of its NTS system operation activity) of the charge levied on the licensee by the agency (as defined in Standard Special Condition A15) in respect of formula year t as set out in the following table:

Variable	Formula years				
	t=6	t=7	t=8	t=9	t=10
$IX_t$ (£ million, 04/05 prices)	6.6				

$IRPI_t$  has the same meaning ascribed to it in paragraph 14(10)(b) of Part 2 of this condition."

6. In paragraph 14(11) (Determination of any adjustment factor to be applied to  $SOMR_t$  ( $SORA_t$ )):

(a) in sub-paragraph (a)(iv) for the paragraph beginning with the words "where the event has" substitute:

"where the event has, for relevant formula year t:



(aa) increased or decreased the value of  $SOIC_t$  (having the meaning given to that term in paragraph 14(3) of Part 2 of this condition) by more than £2,000,000 (the "threshold amount"). This threshold amount does not apply in respect of sub-paragraphs 14(11)(a)(ii) or 14(11)(a)(iii); or

(bb) increased or decreased the value of  $IOC_t$  (having the meaning given to that term in paragraph 14(10)(b) of Part 2 of this condition) or  $ICE_t$  (having the meaning given to that term in paragraph 14(10)(c) of Part 2 of this condition) by more than £1,000,000 (the "internal threshold amount") and is demonstrably not included in  $IOIT_t$  or  $ICET_t$  respectively for formula year  $t$ . This internal threshold amount does not apply in respect of sub-paragraphs 14(11)(a)(ii) or 14(11)(a)(iii) above.";

(b) in subparagraph (i)(ii):

- (i) after "threshold amount," where it first appears, insert, " or  $IOC_t$  or  $ICE_t$  by more than the internal threshold amount,";
- (ii) after "threshold amount" where it next appears, insert "and internal threshold amount".

7. In paragraph 14(13) (Quality of information incentive):

(a) In sub-paragraph (a) (principal formula), for Table (B) substitute:

$QWIP_t$	$QWIIR_t$
$QWIP_t \leq 0$	0
$0 < QWIP_t < 0.27$	$(QWIP_t \times 100) \times \text{£}0.037\text{m}$
$QWIP_t = 0.27$	£1m
$0.27 < QWIP_t < 0.67$	$[(QWIP_t - 0.27) \times 100] \times \text{£}0.01261\text{m} + \text{£}1\text{m}$
$QWIP_t \geq 0.67$	£1.5m

(b) in sub-paragraph (b) (Quality of demand information performance measure):

- (i) for the first formula (from which  $QDIP_t$  is derived), substitute:

$$QDIP_t = \frac{\left( 0.040 - \frac{\sum_d^D |DADF_d - AD_d|}{\sum_d^D AD_d} \right)}{0.040}$$

"Where d is the first day of the scheme, commencing at 06:00 on the 1<sup>st</sup> October 2006, and D is the final day of the scheme, finishing at 06:00 on 1<sup>st</sup> April 2007",

substitute:

"Where d is the first day of formula year t, and D is the final day of formula year t";

- (iii) for the definition of "DADF<sub>d</sub>" substitute:

"DADF<sub>d</sub> means the day-ahead forecast NTS throughput value (in mcm) published by the licensee (in accordance with the Network Code) on its website not later than 14:00 hours at day ahead (d-1) in respect of each day of formula year t. Where the day ahead 14:00 forecast NTS throughput value is not published by 14:00 hours at day ahead (d-1), the next forecast published on the licensee's website for the gas day concerned shall be used";

- (iv) for the definition of "AD<sub>d</sub>", substitute:

"AD<sub>d</sub> means Actual NTS Throughput (in mcm) on a given day (d), calculated five days following the day (d+5), on each day of formula year t";

- (v) for the definition of "Actual NTS Throughput" substitute;

"Actual NTS Throughput means the total offtake of gas from the NTS on each day (measured in mcm), including gas offtakes by DN Operators, Storage Facilities, interconnectors and Very Large Daily Metered Consumers (VLDMC) connected to the NTS, plus the physical elements of NTS Shrinkage;

and:

DN Operators, Shrinkage, Storage Facilities and VLDMC have the meaning given to those terms in the Network Code.";

- (c) for sub-paragraph (c) (Quality of website information performance measure) substitute:

**"(c) Quality of website information performance measure**

For the purposes of paragraph 14(13)(a) of Part 2 of this condition the quality of website information performance measure (QWIPT) shall be derived from the following formula:

$$QWIP_t = \frac{\left\{ \underbrace{\left\{ \frac{\text{MAX} \left[ \left( \frac{180 - WPM_q}{180} \right), 0 \right]}{4} \right\}}_{\text{each quarter q int}} + \text{MAX} \left[ \left( \frac{WTP_t - 0.75}{0.75} \right), 0 \right] \right\}}{2}$$

where,

$WPM_q$  means website availability performance measure, calculated as follows:

$$WPM_q = \frac{(WAPL_q + WAPNN_q + WAPNA_q + WAPDF_q)}{4}$$

"q" means each quarter year;

"quarter year" means the first, second, third and fourth three calendar months of formula year t;

"calendar month" has the meaning given to that term in the Network Code;

and,

$WTP_t$  means the website timeliness performance measure calculated as follows:

$$WTP_t = \frac{(WTPL_t + WTPNN_t + WTPNA_t + WTPDF_t)}{4}$$

where,

$WAPL_q$  means the website availability performance measure for the licensee's Predicted Closing Linepack Data Item or Report expressed as the number of minutes of downtime of the Predicted Closing Linepack Report published on the licensee's website in each quarter year;

$WAPNN_q$  means the website availability performance measure for the licensee's National Forecast Flow Data Item or Report expressed as the number of minutes of downtime of the National Forecast Flow Report published on the licensee's website in each quarter year;

$WAPNA_q$  means the website availability performance measure for the licensee's National Physical Flow Data Item or Report expressed as the number of minutes of downtime of the National Physical Flow Report published on the licensee's website in each quarter year;

WAPDF<sub>q</sub> means the website availability performance measure for the licensee's NTS Throughput Data Item or Report expressed as the number of minutes of downtime of the NTS Throughput Report published on the licensee's website in each quarter year;

WTPL<sub>t</sub> means the website timeliness performance measure for the licensee's Predicted Closing Linepack Data Item or Report, and has a value between 0 and 1, representing the proportion of occasions during formula year *t* that hourly data updates were posted within 10 minutes of the start of the hour (i.e. the 12:00 update published by 12:10 at the latest), expressed as a proportion of all publication occasions;

WTPNN<sub>t</sub> means the website timeliness performance measure for the licensee's National Forecast Flow Data Item or Report, and has a value between 0 and 1, representing the proportion of occasions during formula year *t* that hourly data updates were posted within 10 minutes of the start of the hour (i.e. the 12:00 update published by 12:10 at the latest), expressed as a proportion of all publication occasions;

WTPNA<sub>t</sub> means the website timeliness performance measure for the licensee's National Physical Flow Data Item or Report, and has a value between 0 and 1, representing the proportion of occasions during formula year *t* that hourly data updates were posted within 10 minutes of the start of the hour (i.e. the 12:00 update published by 12:10 at the latest), expressed as a proportion of all publication occasions;

WTPDF<sub>t</sub> means the website timeliness performance measure for the licensee's NTS Throughput Data Item or Report, and has a value between 0 and 1, representing the proportion of occasions during formula year *t* that the 14:00 hours (day ahead), 02:00 hours (day ahead), 12:00 hours (within day), 15:00 hours (within day), 18:00 hours (within day) and 21:30 (within day) publication deadlines are met;

NTS Throughput Data Item or Report means a data item or report published by the licensee showing, amongst other data, the forecast level of Actual NTS Throughput;

Predicted Closing Linepack Data Item or Report means an hourly data item or report published by the licensee showing, for each day, the opening NTS Linepack, two projected closing NTS Linepack figures, and Forecast Total System Demand (measured in mcm). NTS Linepack and Forecast Total System Demand have the meaning given to those terms in the Network Code;

National Forecast Flow Data Item or Report means an hourly data item or report published by the licensee showing, for each day, aggregate forecast flows of gas into the NTS based on delivery flow nominations (measured in mcm);

National Physical Flow Data Item or Report means an hourly data item or report published by the licensee showing, for each day, aggregate forecast flows of gas into the NTS based on actual (aggregate) physical flows into the NTS (measured in mcm).";

- (d) in sub-paragraph (d)(i) (Exceptional events), for "the last 6 months of formula year  $t=5$  (i.e. 1<sup>st</sup> October 2006 to 1 April 2007)", substitute "formula year  $t$ ".

8. In paragraph 16(5) (Disapplication of the NTS SO activity revenue restriction):

- (a) sub-paragraph (ii)(ee) is omitted;
- (b) in sub-paragraph (iii), for "31 March 2007" substitute "1 April 2008".