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Dear Colin

Transmission Price Control Review: Third Consultation on draft licence modifications (Gas transmission)

I am writing in response to the above consultation and I hope that you will find the following comments on the draft text of a number of the special licence conditions useful.

Comments on licence drafting covered under chapter one of Ofgem's consultation

Special Condition C8A: Revenue restriction definitions etc.

We believe that further work is required in respect of the definitions contained within this special condition. In particular, we note that no drafting has been provided for the additional and amended definitions in respect of the NTS exit capacity arrangements that were identified in paragraphs 3.65 – 3.71 of Ofgem's January 2007 licence drafting consultation document. Given the importance of these amendments/additions to Special Condition C8E, it is difficult to comment meaningfully on this condition at this time.

However, in addition to those definitions already identified by Ofgem we believe that "transition period" and "enduring period" need to be defined in the context of the NTS exit arrangements.

We also believe that there are a number of other definitions that need to be reconsidered, for example, the definition of "formula year" which defines $t=1$ as 1st April 2002. If this date remains within the definition, it will be necessary to ensure

that all references to t=1 in the other special conditions are intended to mean 1st April 2002 and not 1st April 2007 (e.g. the use of t=1 in paragraph 4(b)(i)(A) of C8E).

Special Condition C8E: NTS gas exit incentives, costs and revenues

As we discussed on the telephone, in the main, the drafting of Special Condition C8E has not altered since the previous consultation we have therefore repeated the key points of our previous response below.

(i) Baselines.

We are unsure where the initial baselines for both NTS exit flat capacity and NTS exit flex capacity will be specifically set out. Given the importance of these baselines for NGG NTS in terms of its allowed revenue and to both shippers and DNOs for capacity release obligations etc, we believe that it is essential that the initial baselines are set out either in the licence or in a specific statement that the NTS is required to produce under this special condition.

We also believe that there should be a specific requirement on NTS to define, in a statement, the exit zones and regions along with the associated capacity maxima proposed by NGG NTS in respect of the allocation of NTS exit flex capacity under UNC Modification 116. These parameters are central to the allocation of flex and the flex market and therefore transparency is essential. We therefore believe that these parameters should either be set out in the licence or, alternatively, the licence should stipulate that these parameters should be included in one of the number of statements NGG NTS has to prepare under this licence condition. Certainly, these aspects of the enduring regime should be defined as soon as possible given that the DN operators are already having to model their requirements for the enduring period as part of the long term planning process. At the very latest these parameters should be defined by the start of this winter. We also believe that any proposal by NGG NTS to change them would be subject to consultation with relevant parties and subject to Ofgem approval.

(ii) NTS gas exit revenues

For the period 1 April 2007 to 30 September 2011 only shippers will pay for NTS exit capacity and the product that the shipper is paying for is NTS baseline shipper capacity. Therefore, references to NTS baseline exit flat capacity and NTS baseline exit flow flexibility should be removed from the definition of TOExRF in paragraph 2.(a) (since these terms relate to the products being sold from 1st October 2011 under the enduring regime).

Similarly, the terms TREVExCt and TREVBFFt set out in paragraph 2.(a)(i) are not required. Therefore the definition of TOExRFt in this paragraph could be significantly simplified or, alternatively, removed altogether and appropriate amendments made to the definition of TOExRF in paragraph 2.(a) to reflect that from and including 1 October 2011 the value of this term is zero.

(iii) Capacity release obligations

The first line of paragraph 3.(a)(ii) should refer to “NTS exit point” rather than “supply point, connected system exit point or storage connection point” to be consistent with paragraph 3.(a)(i) and Ofgem’s policy to ensure that capacity release obligations apply to all categories of NTS exit point. As currently drafted the obligation would not apply to DN offtakes which is clearly incorrect.

We are unsure where in the licence the investment lead time for delivering incremental NTS exit capacity is set out.

(iv) Statements required from the licensee

As mentioned above, we firmly believe that it should be quite clear where the initial exit capacity baselines are set out. If they are not to be set out specifically in a Schedule as part of the special conditions, we believe they should be provided for in a specific statement required to be produced by the NTS under this section of Special Condition C8E. Likewise, we believe the exit zones and regions and the associated capacity maxima proposed by NGG NTS in respect of the allocation of NTS exit flex capacity under UNC Modification 116 should be specifically set out as a licence requirement. Accordingly, we believe that the statements required from the licensee under this section of Special Condition C8E should include these provisions.

Special Condition C18: Licensee’s methodology for determining the release of NTS exit capacity volumes.

This condition has been changed from the January drafting so that it now relates to the release of *all* NTS exit capacity and not just *incremental* exit capacity volumes as in the existing licence condition. However, no explanation or discussion on this change has been provided. We do not understand why these changes have been made and we would welcome an explanation in this respect.

We are particularly concerned that this proposed drafting could compromise the provisions of the UNC, either the TPD or the OAD, that set out the arrangements that apply in respect of the release of NTS exit capacity by the NTS to gas shippers and/or DN operators. This is particularly relevant to a) the release of existing NTS exit capacity in the transition period which is provided for in the UNC; and b) to the release of both existing and incremental capacity in the enduring NTS exit capacity arrangements which are both provided for by UNC modification 116. We are therefore unsure why this condition allows NGG NTS to establish a methodology when one is already provided for within the UNC. We therefore believe that further consideration needs to be given to the proposed drafting of this condition to clarify exactly what the statement should cover and to ensure that it does not compromise the scope and content of the UNC in this respect.

Special Condition 23: Amendments to Standard Special Conditions

We do not believe that it is appropriate to refer to “NTS standard special conditions” in paragraph 1 of this condition. NTS standard special conditions are those contained in Part B of the licence. We therefore believe that either “NTS” should be removed from this paragraph.

We believe that “gas systems” in paragraphs 4(iii) and 4 (iv) should read “gas”.

Comments on licence drafting covered under chapter two of Ofgem’s consultation

Special Condition C8D: NTS gas entry incentives, costs and revenues

Turning now to the specific questions Ofgem has asked in respect of the proposed licence drafting for Special Condition C8D.

Q2.1: Do you support the proposed structure of the legal text?

The structure of the legal text would appear to be consistent with the final proposals as set out in the TPCR. However, we do have a couple of small comments relating to the drafting. Reference is made in paragraph 5 of the draft licence to EnCBBICt, but this term would not appear to be defined in the licence. Secondly, in paragraph 6 the categories outlined and referenced in section (a) are not consistent with the nomenclature used in the subsequent section (b). In order to avoid any possible challenge, we would recommend that the two are made consistent.

Q2.2. Do you have any comments on the proposed buy-back incentive mechanisms?

Whilst we understand the rationale and sense in establishing two separate buy-back incentive mechanisms, we believe that this will lead to additional complexity and a risk that buy-back actions are double-counted. We therefore welcome the clause that *“the licensee shall ensure that while applying these cost allocation rules, it does not double count costs by attributing the same costs to more than one scheme”*.

In terms of the incremental buy-back incentive mechanism and, more specifically, the cap that has been set, we do not consider 0.52 p/kWh/day to be cost-reflective of the value at stake. We do not believe that 0.52 p/kWh/day is sufficient to compensate shippers for subsequent loss of value incurred by not being able to enter gas into the NTS. Furthermore, we are not aware of any proper and due process to derive this cap. We would therefore welcome further discussion before any cap is set.

Q2.3. Do you have any comments on the detail of the drafting for the release of additional entry capacity and the proposed arrangements for capacity substitution, transfer and trade?

Separate to this response, we have already raised our concerns regarding the scope of the proposed trading arrangements. Ofgem's comment in clause (b) of paragraph 9 reinforces our concern: "[Need to be clear which capacity rights will be subject to the methodology]".

From discussions with Ofgem, we do not believe that it was Ofgem's intention to differentiate between sold obligated baseline entry capacity and sold obligated incremental entry capacity. However, the UNC modifications necessary to implement the transfer and trade proposals fail to define sold entry capacity and have therefore introduced uncertainty. We believe Ofgem needs to be absolutely clear in its licence drafting of paragraph 9 that capacity trade means the transfer of all sold entry capacity, be it obligated baseline or obligated incremental. Both forms of entry capacity are paid for in the same way and therefore should not be treated any differently.

Additional Point

Finally, although not specifically consulted upon, we do have concerns relating to the introduction of a 'trading mechanism' to enable NGG NTS to defer lead times within a notional trading allowance of "7,200 GW months". Whilst we recognise that this is intended to formalise a process that is already in place, we do not understand how it can be considered acceptable for NGG NTS to accumulate 'slack' on future project delivery timescales in return for delivering other infrastructure, especially new infrastructure to connect, early. As we see it, there is no benefit in delivering a project ahead of schedule if the user of that infrastructure is not in a position to utilise the new capacity and there is certainly a real concern that this can be used to offset delays elsewhere. In terms of the actual licence drafting, we believe that this does nothing to alleviate concerns relating to the proposal. Indeed, the lack of clarity increases our concerns: "*the licensee shall notify the Authority in writing and in a timely manner of each instance where it varies the contractual lead time for the deliver of obligated incremental entry capacity from the default of 42 months*". Without defining "*timely*" it is impossible to comment on the reasonableness of this clause.

Again, I hope these comments are helpful. If you would like to discuss any of the points we have made, do give me a call.

Yours sincerely

Victoria Hunter
Regulation Manager