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Date: 6 April 2010

Dear colleague

Date of submission of the Incremental Entry Capacity Release (IECR) methodology statement: initial consultation

This letter seeks views on changing the final submission date of the IECR methodology statement so it is aligned better with the March QSEC auction.

Special Condition C15 of National Grid Gas's (NGG) Gas Transporter Licence (the "Licence") requires that an IECR methodology statement is submitted to the Authority for approval before the 1 July in each formula year. The IECR methodology statement sets out how NGG will determine the release of incremental entry capacity if signals for such capacity are made by system users at the Quarterly System Entry Capacity (QSEC) auction.

The submission of the IECR methodology statement was timed to coincide with the holding of the QSEC auction in September each year. This allowed NGG to set the level of charges users pay to secure incremental entry capacity two months before the QSEC auction took place. As the QSEC auction will now be held in March of each year¹ there is no longer alignment between the QSEC auction and approval of the IECR methodology statement. As a result, NGG has requested to change the submission date of the IECR methodology statement contained in Special Condition C15 of the Licence.

The current submission date also created a very short timetable for the Authority to consider if the statement should be approved – in effect the Authority had a two week period to consider the changes to the IECR methodology statement, not the two month period permitted by paragraph 4 of Special Condition C15. The revised submission date being proposed would also address this issue.

Background

Each year, NGG are required to auction long term entry capacity at the QSEC auction. At this auction Shippers can choose to purchase firm entry capacity or incremental entry capacity at each Aggregated System Entry Point (ASEP). This incremental capacity is usually offered for sale in twenty price steps which correspond to increasing amounts of incremental capacity that can be made available. If Shippers signal for the release of incremental entry capacity at an ASEP NGG will undertake a Net Present Value (NPV) calculation to determine if revenue gained from releasing the incremental entry capacity will cover 50% of the project costs they estimate would be incurred.

¹ UNC modification 230AV revised the QSEC auction timetable. A copy of the decision letter can be found here: <http://www.gasgovernance.co.uk/0230>

The IECR methodology statement describes in detail how the NPV calculation is carried out and when NGG can make incremental capacity available if a signal for incremental capacity passes the test. The statement also describes the methodology for calculating project costs to provide incremental entry capacity at each ASEP and how the incremental price steps, which NGG must publish two months before the QSEC auction takes place, are set.

Paragraph 2 of Special Condition C15 of the Licence states that NGG must submit an IECR methodology statement to the Authority for approval before 1 July every year. The IECR methodology statement must be accompanied by an audit report which confirms that the licensee has developed a methodology that is consistent with the licensee's duties².

Paragraph 4 of Special Condition C15 allows the Authority a 2 month period from the date of submission to veto the proposed changes to the statement.

Issue

Prior to 2010, the QSEC auction was held annually in September. Submission of the IECR methodology statement (and accompanying audit report) on 1 July was necessary so that the notice of incremental charges could be provided two months before the QSEC auction took place.

UNC modification 0230AV changed the QSEC auction timetable so that the auction is held during March each year and not September. This has created a disconnection between the submission of the IECR methodology statement and the holding of the QSEC auction.

NGG's proposed solution

NGG propose that paragraph 2 of Special Condition C15 be amended so that the IECR methodology statement (and accompanying audit report) must be submitted to the Authority no later than 7 November each year. The schedule below shows the effect of this change in the licence condition.

Submission of the IECR methodology statement on this date will give the Authority until 7 January to veto the proposed revisions. The final version of the IECR methodology statement will be published in January with the notice of incremental charges published no later than mid-January.

NGG consider this change will better align the submission of the IECR methodology statement to the March QSEC auction and allow the publication of incremental charges two months before the auction takes place. They also state that the revised submission date will increase the amount of decision making time the Authority has to consider changes to the IECR methodology statement.

Ofgem's view

Our initial view is that this is a common sense proposal to better align the submission of the IECR methodology statement with the QSEC timetable. The revised date will allow NGG to better match their internal work processes for the preparation of the IECR methodology statement and QSEC auction. This should allow NGG to provide appropriate information to system users in line with the new timing of the QSEC auction.

The revised date will also increase the amount of time the Authority has to consider proposed changes to the IECR methodology statement. The current timetable constrains the Authority to a two week period to consider revisions to the IECR methodology statement. While it has been possible to date to review the statement in such a short timescale it does create resourcing and work planning issues for the Authority at a time of year when staff availability can be naturally restricted.

² See paragraph 3 Special Condition C15 of the Licence.

The revised submission date should lead to a more considered analysis of the statement especially if significant changes are proposed. Allowing the Authority a greater amount of time to assess proposed changes should help ensure that they have been given due consideration.

Next steps

We are seeking views on this proposed change. Specifically,


- Are system users content with the new submission date for the IECR methodology statement?
- Are system users content that they will be consulted on the IECR methodology statement annual review during September or October each year?
- Are there any problems with the publication of the IECR methodology statement in January each year?

Ofgem would be interested in receiving comments from interested parties on the above questions and any other points of relevance. We are asking for responses by **4 May 2010**. Unless marked confidential, all responses will be published by placing them in Ofgem's library and on its website www.ofgem.gov.uk. Respondents may request that their response is kept confidential. Ofgem shall respect such requests subject to any obligations to disclose information, for example, under the Freedom of Information Act 2000 or the Environmental Information Regulations 2004. Any respondent who wishes their response to remain confidential should clearly mark the response to that effect and give their reasons for confidentiality.

It would be helpful if responses could be submitted both electronically and in writing. Electronic responses should be sent to gastransmission@ofgem.gov.uk. Respondents are asked to put any confidential material in appendices to their response. Subject to responses, we would expect to follow up this consultation with a Notice under section 23 Gas Act 1986 in at the start of May 2010, such that the Licence could be changed by July 2010.

If you have any comments or questions on this letter, please contact James Thomson on +44 (0)141 331 6012 or james.thomson@ofgem.gov.uk in the first instance.

Yours sincerely,



Stuart Cook
Senior Partner, Transmission and Governance
Signed on behalf of the Authority and authorised for that purpose.

Schedule A - Special Condition C15. Licensee's methodology for determining incremental entry capacity volumes

2. The licensee shall before ~~1 July~~ [7 November](#) in each formula year (or such later date in each formula year as the Authority may approve) prepare and submit for approval by the Authority an incremental entry capacity release methodology statement setting out (consistently with the licensee's duties under the Act, and the standard, Standard Special and Special Conditions) the methodology by which it will determine whether to make incremental entry capacity available for sale to gas shippers. For the avoidance of doubt this methodology will take into account where appropriate the licensee's obligations with respect to entry capacity substitution.