Making a positive difference
for energy consumers

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Dear Helen,

Network Code on Gas Balancing of Transmission Networks – National Grid Gas Transmission Impact Assessment

I am writing in response to your letter dated 15 January 2014, in which you provided additional information on several points relating to the implementation of the Gas Balancing of Transmission Networks European Network Code ("the Code"). This letter follows our presentation to the UNC European Working Group on 6 March 2014, where we set out our initial thinking. To date we have received no objections to the positions expressed.

This letter summarises the comments we gave at that meeting in response to the points you raised, on which more detail is provided in the appendix to this letter.

1. Potential benefits of using an additional 12 months (up to October 2016) to implement the Code – *we understand that your current intention is to implement by 1 October 2015.*

2. Whether Operating Margins (OM) gas is a balancing service – *it is National Grid's responsibility to act in accordance with applicable EU and national rules when they apply OM as an emergency measure. If National Grid uses OM gas in any circumstances where Article 2(4) of the Code is not applicable, it will likely be considered a balancing service in terms of the Code. Ofgem will monitor compliance with the Code on an ongoing basis.*

3. Status of locational trades for national balancing purposes in the GB System Marginal Prices (SMP) and System Average Price (SAP) – *We agree with you that the cost of implementing a flagging mechanism to remove locational trades from the SMP and SAP calculations would outweigh the benefits that such a mechanism would bring at this time.*

4. Whether National Grid has any Within Day Obligations – *We note that National Grid does not currently believe that they have any WDOs. If we or National Grid consider that WDOs are required in the context of the Code, we expect you to submit a proposal to us for approval.*

5. Whether a separate Neutrality Mechanism methodology is required under the Code, and further approval would be necessary – *Ofgem has already approved the*

provisions in the UNC that implement this aspect of the Code so we do not believe that an additional approval process is required to comply with the Code.

6. Consideration that GB information provision model (base case) and the second Non Daily Metered forecast would not require further NRA approval – *we understand that these questions have been resolved through inclusion of these provisions in the UNC Modification 489 proposal, which will be submitted to Ofgem for approval in due course.*

7. The need for NRA approval of the GB value of the small adjustment if it exceeds 10% of System Average Price (SAP) – *we understand that the small adjustment does not currently exceed 10% of the SAP and therefore no approval is required at present. If National Grid becomes aware that this situation is predicted to change or has changed, we would expect National Grid to justify it to us at that time and seek approval in accordance with the requirements of the Code.*

If you wish to discuss implementation of the Code in greater detail, please do not hesitate to contact me, Ryan McLaughlin (020 3263 9615) or Jessica Housden (020 7901 7254).

In the interests of transparency, we will also publish this letter on the Ofgem website.

Yours sincerely,

Rob Mills
Acting Associate Partner, Gas Wholesale Markets

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Appendix

1. **Potential benefits of using an additional 12 months (up to October 2016) to implement the Code**

   We understand that, since the date of your earlier letter, National Grid has decided that it does not intend to request the extra 12 months to implement the Code.

   If this should change at any point, we would ask you to update us as promptly as possible.

2. **Whether Operating Margins (OM) gas is a balancing service**

   We note that National Grid has stated that it considers that its use of OM gas is exempted from the requirements of the Code in accordance with Article 2(4) of the Code, which reads:

   This Regulation shall not apply in emergency situations where the transmission system operator shall implement specific measures defined under the applicable national rules and on the basis of Regulation (EU) No 994/2010 of the European Parliament and of the Council of 20 October 2010 concerning measures to safeguard security of gas supply, as appropriate.

   We interpret Article 2(4) as disapplying the Regulation in certain circumstances that are set out in the article; where those circumstances do not apply the Regulation's requirements will be binding. It is National Grid's responsibility to ensure that, when it utilises OM gas, it acts in accordance with applicable EU and national rules. If National Grid uses OM gas in any circumstances where Article 2(4) is not applicable, this will likely be considered a balancing service in terms of the Code.

   Ofgem will monitor compliance on an ongoing basis.

3. **Status of locational trades for national balancing purposes in the GB System Marginal Prices (SMP) and System Average Price (SAP)**

   Ofgem notes that the last relevant locational trade took place in July 2006. Ofgem agrees that that locational trades (for balancing purposes only) should continue to feed into the calculation of SMP prices and SAP, as the estimated costs of making system changes to flag these trades would outweigh the benefits that the flagging would achieve.

   We consider that, as locational trades are presently immaterial to the calculation of the SMP and SAP, we do not object to locational trades being included in the calculations of the above prices at present.

   Ofgem will monitor compliance on an ongoing basis and will review this position should there be a material increase in the volume and impact of locational trades on the imbalance prices.

4. **Whether National Grid has any Within Day Obligations (WDOs)**

   We note that National Grid does not believe it currently has any WDOs and does not intend to propose any in the near future. We are also aware that some stakeholders indicated that they believed that local operating terms within National Grid's connection contracts (Network Entry Agreements and Network Exit Agreements) might be considered WDOs as network flexibility is an important issue for industry.

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We recognise concerns from market participants on this matter, and we believe that National Grid's RIIO Talking Networks project may be a more appropriate forum for detailed discussions about network flexibility. This would further allow scope for a holistic view to be taken in the context of the GB regime. We understand that the stakeholders who raised the initial concerns are also supportive of this approach.

If we or National Grid consider that WDOs are required in the context of the Code, we expect National Grid to submit a proposal to us for approval in accordance with the requirements of the Code.

This view does not restrict Ofgem's right to take a decision on our own initiative in accordance with Article 26(1) of the Code.

5. Whether a separate Neutrality Mechanism methodology approval is required under the Code

We note that National Grid believes that GB's existing UNC neutrality processes contained within UNC Section F are compliant with the Code and provided evidence to justify their position. We have subsequently conducted our own analysis of the Code and UNC, and our conclusions are set out in the table below:

Code - Article 30	**UNC**
1. The neutrality charge for balancing shall be paid by or to the network user concerned.	The following details are from Section F4.2.2: *"For each relevant User the Balancing Neutrality Charge shall be calculated as the sum of:* *(a) the Unit Daily Neutrality Amount multiplied by the sum of the relevant User's relevant UDQIs and relevant UDQOs for the relevant Day;* *(b) the Adjustment Neutrality Amount for the relevant Day."* The following details are from Section F4.2.3: *"The Balancing Neutrality Charge is payable by National Grid NTS to the User where it is negative and by the User to National Grid NTS where it is positive."*
2. The NRA shall set or approve and publish the methodology for the calculation of the neutrality charges for Balancing, including the apportionment and credit risk rules	The Neutrality Methodology is set out in UNC Section F.4, and Credit rules set out in UNC Section X.
3. The neutrality charge for balancing shall be proportionate to the extent the network user makes use of the relevant entry or exit points	We understand this is achieved by using the User's relevant UDQIs and relevant UDQOs for the relevant Day.
4. The neutrality charge for balancing shall be identified separately when invoiced to network users and the invoice shall be accompanied by sufficient supporting information defined in the methodology referred to in 2	TPD Section F 4.2.4 states: *"Balancing Neutrality Charges shall be invoiced and are payable in accordance with Section S."*
5. Where variant 2 is applied the	N/A as refers to variant 2 and this is not

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neutrality charge may be based on forecasts, etc.	applicable to GB.
6. Where relevant, the transmission system operator's methodology for the calculation of the neutrality charge for balancing may provide rules for the division of the neutrality charge for balancing components and the subsequent apportionment of the corresponding sums amongst the network users in order to reduce cross subsidies.	N/A as this is not currently the case in GB.

We are satisfied that the applicable requirements of Article 30 of the Code are met within the UNC. As Ofgem approved these provisions when they were implemented into the UNC, we do not believe an additional approval process is required to comply with the Code.

6. Consideration that GB information provision model (base case) and the second Non Daily Metered forecast would not require further NRA approval

We understand that the second within day Non Daily Metered Forecast is already provided for under the UNC. All the information provision Code requirements will be implemented as part of *UNC Modification 489: EU Gas Balancing Code - Information Provision changes required to align the UNC with the EU Code*[1], which will be considered at the August 2014 UNC Panel. As the modification is not proceeding as self-governance, it will be submitted to Ofgem for its approval in due course.

As the GB balancing regime already operates under the base case information provision model, we do not believe an additional NRA approval is necessary to facilitate compliance with the Code.

7. The need for approval of the GB value of the small adjustment if it exceeds 10% of SAP

We note that the current methodology for calculating the small adjustment (aka the Default System Marginal Price (DSMP)) in GB creates the possibility of it exceeding 10% of SAP. Given that the current methodology would require a SAP of approximately 10p/therm in order for the DSMP to be greater than 10% we do not believe that there is any requirement to amend the current methodology at present.

We consider that, under Article 22(7) of the Code, if National Grid becomes aware of any circumstance where the small adjustment may be greater than 10% of SAP, we would expect you to justify this to us and seek approval pursuant to Article 20 of the Code.

[1] http://www.gasgovernance.co.uk/0489

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