

National Grid NTS Response to UNC Modification Proposal 0061
“Facilitating further demand-side response in the event that a Gas Balancing Alert is triggered”

National Grid NTS’s Position.

National Grid NTS supports the implementation of this proposal. Below is National Grid NTS’s detailed response to the Modification Proposal:

1. The Modification Proposal

National Grid NTS supports the implementation of this proposal.

Background to this Proposal:

Commencing in 2004 (Quarter 4) and throughout 2005, we have participated in the Ofgem chaired the Demand Side Working Group (DSWG). This group considered how further demand side response could be facilitated. The consensus of these DSWG discussions was that, in limited circumstances, National Grid NTS, in its role as the residual system balancer, should be able to supplement its current use of the On-the-Day Commodity Market (OCM) with other non-OCM Eligible Balancing Actions and be allowed to take balancing actions with a duration of more than one Gas Day (i.e. multi-day trades). Such multi-day trades should be facilitated both through the OCM and OTC contracts with non Trading Participants.

We have also undertaken, as part of the DSWG discussions, to provide further information to Users in the form of a Gas Balancing Alert (GBA). The GBA aims to provide an early indication of a greater likelihood that demand side response might be required to help resolve a gas deficit balancing position.

We believe that the consensus of the DSWG discussions is that the use of non-OCM trades and initiation of multi-day trades should only be facilitated for a Gas Day for which a Gas Balancing Alert (GBA) has been triggered. And that further, the consensus of the DSWG discussions is that these changes should be enabled prior to the Winter 2005/06 peak demand periods.

2. Extent to which implementation of the proposed modification would better facilitate the relevant objectives

We believe that implementation would further the relevant objectives as set out in the Gas Transporter Licence, Standard Special Condition as: -

a. In respect of paragraph 1.a):

The Proposal may improve “*the efficient and economic operation of the pipe-line system*” by facilitating co-operation between consumers and Users that might provide further demand-side response, through the provision of multi-day trades, to the market at the time when the Total System most requires it. The Proposal also provides National Grid NTS with the ability to access demand side response, or supplies, held by non-OCM Trading Participants thus extending the

National Grid NTS Response to UNC Modification Proposal 0061
“Facilitating further demand-side response in the event that a Gas Balancing Alert is triggered”

boundaries of the competitive area in which the residual balancer operates. Therefore, the Proposal would ensure that National Grid NTS is able to utilise all available trading actions to minimise the risk of entering an NGSE.

b. In respect of paragraph 1.e):

The introduction of the Proposal might improve *“the provision of reasonable economic incentives for relevant suppliers to secure that the domestic customer supply security standards are satisfied as respects the availability of gas to their domestic customers”*.

The Proposal would increase the information available to industry parties thereby enabling a timely response to secure sufficient demand-side response in order to match supplies. The use and inclusion of OTC contracts in the derivation of SAP, and where relevant SMBP and SMSP, would further facilitate competition by reflecting the value of all the gas that has been traded to meet residual balancing requirements during times of system stress thereby ensuring that cashout incentives reflect a wider market value.

In addition the proposed methodology for setting the effective price for a multi-day Eligible Balancing Action by assessing the probability of the Total System requiring the gas on subsequent Days ensures that the total cost of the trade is correctly targeted to the days when it is required.

3. The implications for Transporters and each Transporter of implementing the Modification Proposal.

i. Implications for operation of the System

By affording the opportunity to participate in OTC trading, and accepting multi-day trades it is anticipated that National Grid NTS, in its role as the residual system balancer, will be able to maximise its commercial tools in an attempt to mitigate the risk of an NGSE being declared.

National Grid NTS expects to make changes to its System Management Principle Statement (SMPS) and Procurement Guidelines in order to facilitate certain elements of this Proposal, for example, the introduction of the GBA and multi-day trades. These changes will be completed should this Proposal be implemented.

National Grid NTS currently believes that this Proposal, as outlined, would not require a material change to its Safety Case.

ii. Development and capital cost and operating cost implications:

a) National Grid NTS will be required to establish additional contracts, credit and off-line processes in order to manage OTC contracts and multi-day trades.

b) This Proposal will require xoserve to put additional processes in place to ensure timely and accurate billing/payment, credit/interest calculations and

National Grid NTS Response to UNC Modification Proposal 0061

“Facilitating further demand-side response in the event that a Gas Balancing Alert is triggered”

additional operational requirements. The full impact of these processes are still being evaluated.

c) With regard to the introduction of the Gas Balancing Alert, National Grid NTS has already implemented improvements to its information provision web pages. Publication of the GBA is included within this programme.

d) During Periods of high demand National Grid NTS may be required to redeploy staff from other activities in order to manage the OTC trades and carry out the processes resulting from OTC and multi-day Eligible Balancing Actions.

4. The implications of implementing the Modification Proposal on security of supply, operation of the Total System and industry fragmentation

We believe that the consensus of the attendees of the DSWG considered that the subject matter of the Proposal was worthy of assessment against the relevant objectives as they considered that security of supply would be enhanced by the implementation of this Proposal by:

- Encouraging demand-side response and providing signals to the market in advance (D-1) would allow consumers to prepare for, and plan, a reduction in their gas consumption on the Total System.
- In addition to undertaking Eligible Balancing Actions on the OCM, it would afford National Grid NTS with the ability to utilise OTC contracts.
- Multi-day bids/offers would provide Users and National Grid NTS with the ability to post and accept multi-day trades that might be considered economic and efficient at the time that the action is taken.
- The combination of accepting multi-day trades and OTC trades should afford all Users that want to participate in Eligible Balancing Actions with the residual balancer are able to do so.

5. The high level affect on the UK Link System and other related Systems for Transporters and Users

Full implications of the Proposal are still being assessed, however National Grid NTS and xoserve will introduce manual process to support the implementation of this Proposal.

For a transitional period National Grid NTS has been advised by APX that it will not have the system functionality to correctly include OTC and multi-day trades in the published SAP and SMP prices on their system. It is intended that in the event of any Eligible Balancing Actions being taken which include OTC trades or multi-day trades, APX will flag that the SMP and SAP published on its systems may be misleading. As soon as practicable following any such Eligible Balancing Action National Grid NTS will publish sufficient detail on its systems to enable Users to calculate the prevailing SAP and SMP. Except in exceptional circumstances the prevailing SAP and SMP prices will be updated on National Grid NTS systems hourly as per current practice. APX have indicated to National Grid NTS that they intend to investigate the feasibility of an automated SAP and SMP price in the event that the Proposal is implemented.

National Grid NTS Response to UNC Modification Proposal 0061

“Facilitating further demand-side response in the event that a Gas Balancing Alert is triggered”

The proposed methodology for the apportionment of costs associated with multi-day trades, creates an increased risk that the prevailing cashout prices may exceed 99.9999 pence/kWh. This would exceed the maximum value that the Gemini system is currently able to process. The feasibility of a systemised solution to this issue or a manual work around is currently being assessed. However, whilst the risk is increased it remains low, for example the current SMP buy price is below 2.5p/kWh – some forty times below the current Gemini maximum value.

6. The implications of implementing the Proposal for Users

The Proposal, if implemented, should assist the Users’ processes, for accessing demand-side response and communicating with their customers in a more timely and efficient manner.

Potentially increased credit risk; although this is unlikely to be a material change. For example, if a GBA is triggered for a Gas Day, it is likely that any Eligible Balancing Actions undertaken by National Grid NTS will be executed as acquiring trades actions rather than disposing trades.

It is intended that any interest payments incurred because of any difference between OCM and OTC clearing/invoicing settlement periods will be funded through the Balancing Neutrality account.

Lack of anonymity with OTC contracts means that the third party trading with the residual balancer will be aware of the potential affect on system clearing prices before other Users. This might lead to some Users in those markets effectively having an information advantage over other Users in that they might effectively have asymmetrical access to price data until the revised SAP and SMP prices are published to the market. As detailed above National Grid NTS intend to publish the effect of such trades on SAP and SMP prices within an hour of such trades being completed.

7. The implications of implementing the Modification Proposal for Terminal Operators, Consumers, Connected System Operators, Suppliers, producers and any Non Code Party

Through our discussions at the DSWG and elsewhere, we believe that there are a number of major gas consumers that would be willing to offer demand response to the residual balancer (via their shipper) when the Total System is “under stress”. Some of these major gas consumers are unable to significantly reduce their gas demand for a single day and therefore require the residual balancer to commit to taking gas for a number of days. The Multiple Day element of the Proposal will enable these consumers to offer this potential demand response.

Further we believe that there is a subset of major gas consumers that are unable to trade with the residual balancer via a shipper that is also an OCM member (Trading Participant). The OTC element of the Proposal will enable such non Trading Participants to trade with National Grid NTS in its role as the residual balancer.

National Grid NTS Response to UNC Modification Proposal 0061
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8. Analysis of any advantages or disadvantages of implementation of the Modification Proposal

a. Advantages:

National Grid NTS believe that the consensus of the attendees of the DSWG considered the primary advantages of this Proposal as:

- The GBA would provide a timely and important signal to the market that demand-side response is more likely to be required in order to maintain the balance of the Total System. If implemented the GBA would also provide an additional trigger for Users and major gas consumers to initiate appropriate demand-side reductions.
- It provides National Grid NTS with the ability to consider other trading actions, which, it deems to be economic and efficient at the time of such actions in order to mitigate the risk of an NGSE being declared.
- It could create additional price signals that might encourage Users to resolve their own supply-demand deficit prior to an NGSE being declared.
- It provides a facility for non Trading Participants to offer demand-side response to the residual system balancer during the period of a GBA.
- It would further facilitate competition in those gas markets associated to the pipeline system and appropriately reflect the value of gas that the residual system balancer had traded in other markets during times of system stress.
- The Proposal is restricted to the duration of a GBA and might therefore, be considered to have a negligible affect on the majority of Gas Days.

b. Disadvantages:

- Lack of anonymity with OTC contracts; taking an Eligible Balancing Action in uncleared Markets might have an adverse impact on SAP and SMP as the Users making OTC offers will be aware that they are trading with the residual balancer.
- Information asymmetry : Lack of anonymity with OTC contracts means that the third party trading with the residual balancer will be aware of the potential affect on system clearing prices before other Users. This might lead to some Users in those markets effectively having an information advantage over other Users in that they might effectively have asymmetrical access to price data until the revised SAP and SMP prices are published to the market.
- Additional complexity: Daily operation of the Network, associated commercial actions, processes and procedures to manage the OTC process. Invoicing and Settlement; additional processes and procedures to manage the billing payment of OTC trades and the credit management of the OTC trades. In particular where a multi-day trade straddles a month end there will potentially be a

National Grid NTS Response to UNC Modification Proposal 0061
“Facilitating further demand-side response in the event that a Gas Balancing Alert is triggered”

disparity in the Energy Balancing Invoice. This disparity will be rectified in the following month’s EBI with interest accruing as applicable.

- In the event that a GBA is triggered and National Grid NTS takes non-OCM Eligible Balancing Actions or multi-day actions either on the OCM or OTC, there will be a delay in the provision of cashout price information to the market. Currently, cashout prices (SAP & SMP) are published by APX (the market operator) on a close to real-time basis as they are derived from those trades undertaken exclusively on the OCM. In the event that the residual balancer actions OTC or multi-day trades, there will be times when the published OCM SAP (and SMP) will not reflect those actions undertaken by National Grid NTS. However, National Grid NTS will endeavour to minimise any timing delay to the publication of price information to the market. It is our intention to ensure that any such time delay is contained to within an hour in all but exceptional circumstances.
- For a transitional period National Grid NTS has been advised by APX that it will not have the system functionality to correctly include OTC and multi-day trades in the published SAP and SMP prices on their system. It is intended that in the event of any Eligible Balancing Actions being taken which include OTC trades or multi-day trades, APX will flag that the SMP and SAP published on its systems may be misleading. As soon as practicable following any such Eligible Balancing Action National Grid NTS will publish sufficient detail on its systems to enable Users to calculate the prevailing SAP and SMP. The prevailing SAP and SMP prices will be updated on National Grid NTS systems hourly as per current practice. APX have indicated to National Grid NTS that they intend to investigate the feasibility of an automated SAP and SMP price in the event that the Proposal is implemented.
- The proposed methodology for the apportionment of costs associated with multi-day trades, creates an increased risk that the prevailing cashout prices may exceed 99.9999 pence/kWh. This would exceed the maximum value that the Gemini system is currently able to process. The feasibility of a systemised solution to this issue or a manual work around is currently being assessed. However, whilst the risk is increased it remains low, for example the current SMP buy price is below 2.5p/kWh – some forty times below the maximum.