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UNC Modification Proposal 0125
'Introduction of new Balancing Neutrality charge for cost of Residual Balancer collateral on the OCM'

Dear Julian,

Thank you for your invitation seeking representation with respect to the above Modification Proposal.

As the proposer, National Grid NTS (NG NTS) supports the implementation of this Modification Proposal.

During discussions at the Workstream Panel meeting held on the 7 December 2006, concern was expressed regarding the appropriate method, type and transparency, of Residual Balancer collateral to be raised for activity on the OCM. The Panel questioned whether more information, detailing the level and associated cost of such collateral, should be provided to the community or/and the EBCC.

We advised the Panel that our license obligations require us to carry out the Residual Balancer role in an efficient and economic manner. In respect of collateralising the OCM activity of the Residual Balancer, we believe that the most cost effective means through which we can achieve such obligations is via the Letter of Credit (LOC) arrangements current used by National Grid NTS to support its own commercial activities, as we consider these offer competitive rates for securing this collateralisation. However the competitive rates achieved through such an arrangement are attained as result of National Grid confidential financial arrangements. We would therefore not wish to release such information into the public domain as such release would undermine these arrangements.

If the community believed that the materiality of the costs potentially incurred warrant greater shipper involvement in the establishment of this collateral and that this requirement is not satisfied by the current audit reporting, licence obligations and Ofgem over-sight then we would seek to secure such collateralisation through separate individual arrangements relating to the Residual Balancer activities only, which would potentially include agreement to publish these terms. However it is our opinion that such terms would not be as competitive as those that could be achieved through existing NG NTS arrangements.

As presented at the Panel meeting on the 7 December 2006, although we would be unable to provide details of the financial terms related to the collateralisation and the costs associated we could provide some comfort through the following obligations; and information provision in the following areas may go some way in assuring an economic and efficient approach to collateralisation of the Residual Role on the OCM:-

- Licence Conditions :-
 - Standard Special Condition A11.1 (a) the efficient and economic operation of the pipeline system.
 - Standard Special Condition A17.2 (b) the Transporter shall not knowingly prejudice the economic and efficient balancing of the pipeline system of any of the relevant Gas Transporters.
 - Standard Special Condition A6.1 – Conduct of the Transportation business. Licensee shall conduct its transportation in a manner which ensures that no User or Transporter obtains an unfair commercial advantage.
- Ofgem over-sight of NG activities
- Undertaking to provide general reporting of costs
- External audit annually that cost have been incurred efficiently and economically (part of SMPS and PG audit)

We believe that regardless of where and how appropriate collateralisation is sourced, the associated cost should be funded by the community through Balancing Neutrality. In order that this may be achieved an amendment to the UNC is required, as proposed, which facilitates such charges being funded and smeared as a neutrality adjustment.

Some Users have sought clarification regarding whether the cost for collateralisation, for Residual Balancing activity on the OCM, will be visible on the Energy Balancing invoice. In response we advise that the cost will not appear as a specific line item, however it will be included as part of the Cash Neutrality Smear (CNU) invoice item and therefore further details will be provided as supporting information within the Neutrality statement.

Please let me know if you require any further information to enable preparation of the Final Modification Report.

Yours sincerely

Ritchard Hewitt

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