

CODE MODIFICATION PROPOSAL No 0216A
“Introduction of Additional Pay-as-Bid Auctions for NTS Entry Capacity”
Version 1.0

Date: 22/05/2008

Proposed Implementation Date: 01/08/2008

Urgency: Non Urgent

1 The Modification Proposal

a) Nature and Purpose of this Proposal

Under the current Uniform Network Code (UNC) arrangements, National Grid NTS (NGG NTS) must make Unsold NTS Entry Capacity available to Users subject to a market test. National Grid NTS may also, at its own discretion, make additional Quarterly NTS Entry Capacity and additional Daily NTS Entry Capacity (i.e. in addition to Unsold NTS Entry Capacity) available at an Aggregate System Entry Point. For clarity, E.ON UK does not propose to change the above arrangements.

E.ON UK proposes that the UNC be amended to enable National Grid NTS to introduce one or more additional pay-as-bid auction(s) within the same Capacity Year, to release additional NTS Entry Capacity (including the associated release of Unsold NTS Entry Capacity) outside of, and in addition to, the existing Quarterly and Daily auction mechanisms that are currently in place.

However, E.ON UK proposes that National Grid NTS shall only be entitled to exercise this new discretionary right to effectively break from the current UNC structure of NTS Entry Capacity auctions:

- Until the end of the Capacity Year ending 30th September 2009; at which point the right shall cease to exist under the UNC. The purpose of this is to seek to minimise any unforeseen consequences arising from the new process, whilst allowing time for full industry review of the process, post-winter 2008/9.
- To make available NTS Entry Capacity in strips of no less than one (1) month and no greater than one (1) year.
- By giving a minimum of 28 days notice to Users of a proposed additional pay-as-bid auction to release additional (or associated Unsold) NTS Entry Capacity.
- By running each new pay-as-bid auction with a minimum of two (2) rounds, which should facilitate true price discovery for the new NTS Entry Capacity.

It should be noted that this Proposal does not oblige NGG NTS to release additional NTS Entry Capacity to the market. However, this Proposal does introduce flexibility for NGG NTS to introduce one or more additional pay-as-bid auctions to release more Entry Capacity than would otherwise be the case, but in more transparent and predictable circumstances than proposed under Mod 216. This Proposal places reasonable limits on the complete and sole discretion proposed by NGG NTS (in Mod 216) to potentially release NTS Entry Capacity (both additional and Unsold) at any time and under any circumstance in the same Capacity Year.

If Mod 216 were to be implemented, we do not believe that the current UNC rules provide a satisfactory limit on when and how NG NTS may call a new auction to release additional and associated Unsold NTS Entry Capacity. As a result, if implemented, the Proposer believes that Mod 216 could seriously undermine the existing auction structure and pricing, introducing unacceptable levels of uncertainty for all Users of the NTS; particularly new entrants.

As also specified in Mod 216, it is further proposed that any such release of NTS Entry Capacity shall:

- Be subject to the application of a Reserve Price. For clarification this will be the prevailing AMSEC auction Reserve Price (for each ASEP/s at which the NTS Entry Capacity is released) as specified in the Statement of Gas Transmission Charges.
- Be applied solely within that Capacity Year.
- Be subject to the provisions of UNC Section V3.

For the avoidance of doubt Users will pay Capacity Charges for the Capacity allocated through this process; i.e. quantity of NTS Entry Capacity allocated multiplied by the bid price tendered multiplied by the relevant period for which capacity has been allocated.

For the avoidance of doubt, any NTS Entry Capacity allocated through this process shall be considered in respect of Overruns. Allocated capacity shall be included in the User's aggregate Available NTS Entry Capacity to determine the Overrun Quantity. Bid prices (in respect of satisfied bids) shall be considered for determination of System Entry Overrun Charge rates at the ASEP where the allocation is made.

National Grid NTS will no later than 2 (two) Business Days prior to the first day for which applications for capacity have been made, inform each User of those of its capacity bids that have been accepted, the amount of NTS Entry Capacity which it is registered as holding for the ASEP and the relevant period (for clarification the relevant period will be the period for which the capacity has been allocated).

And no later then 1 (one) Business Day prior to the first day for which

applications for capacity have been made, National Grid NTS will provide information to all Users in accordance with UNC Section B paragraph 2.14.2 other than sub paragraphs (b) and (h).

The Terms and Conditions applicable to the new pay-as-bid auction(s) will:

- Be made available to Users by National Grid NTS a minimum of 28 days prior to release of the NTS Entry Capacity. The Terms and Conditions will form part of the auction invitation process.
- Be accepted by Users. For clarification the Terms and Conditions will contain the business rules applicable to that release of NTS Entry Capacity. Users will be required to accept the Terms and Conditions prior to participating in the capacity release mechanism.

b) Justification for Urgency and recommendation on the procedure and timetable to be followed (if applicable)

Not applicable

c) Recommendation on whether this Proposal should proceed to the review procedures, the Development Phase, the Consultation Phase or be referred to a Workstream for discussion.

E.ON UK requests that this Modification Proposal, as an alternative Proposal proceeds through the governance process in tandem with Modification Proposal 216.

2 Extent to which implementation of this Modification Proposal would better facilitate the achievement (for the purposes of each Transporter's Licence) of the Relevant Objectives

E.ON UK considers this Proposal would, if implemented, better facilitate the following Relevant Objectives as set out in National Grid NTS' Gas Transporter Licence:

- In respect of Standard Special Condition A11 paragraph 1(a), the Proposal would provide additional flexibility in the NTS Entry Capacity release arrangements to allow National Grid NTS to release additional NTS Entry Capacity via a pay-as-bid auction. This should result in the release of more capacity to the market (particularly for Winter 08/09) than would otherwise be the case, reducing the risk of gas being stranded offshore and better facilitating the achievement of this objective.
- In respect of Standard Special Condition A11 paragraph 1(d), the Proposal would promote effective competition between relevant Shippers by ensuring certainty for Shippers that capacity bought in previous capacity auctions in the same Capacity Year would not be undermined by release of additional and perhaps unexpected NTS Entry Capacity through an unspecified release

mechanism, called at National Grid's discretion (as proposed in Mod 216).

- In respect of Standard Special Condition A11 paragraph 1(d), the Proposal would further promote effective competition between relevant Shippers by ensuring that both new and existing Users are aware of the structure of NTS Entry Capacity Auctions and are able to plan and manage risk on this basis. In addition, by time-limiting this Proposal, any unforeseen consequences on the market are minimised.

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

E.ON UK believes that this Proposal, if implemented, may enhance security of supply by allowing Users the opportunity to obtain more NTS Entry Capacity than would otherwise be the case; particularly for the forthcoming winter period.

E.ON UK also believes that this Proposal, by limiting how and when National Grid NTS can run a new pay-as-bid auction outside of the current UNC auction structure, will not have an adverse effect on industry or system fragmentation.

4 The implications for Transporters and each Transporter of implementing this Modification Proposal, including:

a) The implications for operation of the System:

E.ON UK does not believe this Proposal, if implemented, would adversely affect the physical operation of the System. By optimizing the release of NTS Entry Capacity, implementation of this Proposal would provide Users with a greater opportunity to ensure gas supplies can be delivered to market.

b) The development and capital cost and operating cost implications:

E.ON UK understands that this Proposal, if implemented may have some cost implications with regards to system implementation and operating costs.

It should be noted, however, that if implemented, this Proposal is likely to make use of the existing MSEC auction as a template and thus use existing functionality. As a result, we do not envisage that the costs would be substantial. In addition, as the proposal is time limited the additional development costs could be minimised or avoided by a temporary solution using existing systems.

c) Whether it is appropriate to recover all or any of the costs and, if so, a Proposal for the most appropriate way for these costs to be recovered:

Based on NGG NTS's statement in Mod 216, E.ON UK believes that these costs are internal to National Grid NTS and will be recovered through the existing charging regime.

- d) **The consequence (if any) on the level of contractual risk of each Transporter under the Uniform Network Code of the Individual Network Codes proposed to be modified by this Modification Proposal**

E.ON UK believes that the Proposal will have no material impact on the level of contractual risk of each Transporter.

- 5 **The extent to which the implementation is required to enable each Transporter to facilitate compliance with a safety notice from the Health and Safety Executive pursuant to Standard Condition A11 (14) (Transporters Only)**

Not applicable

- 6 **The development implications and other implications for the UK Link System of the Transporter, related computer systems of each Transporter and related computer systems of Users**

E.ON UK envisages that this Proposal, if implemented, could have an impact on both the Gemini and UK Link systems.

- 7 **The implications for Users of implementing the Modification Proposal, including:**

- a) **The administrative and operational implications (including impact upon manual processes and procedures)**

E.ON UK believes that implementation of this Proposal would retain much-needed certainty for Users about when and how to bid for NTS Entry Capacity.

- b) **The development and capital cost and operating cost implications**

E.ON UK is not aware of any such implications.

- c) **The consequence (if any) on the level of contractual risk of Users under the Uniform Network Code of the Individual Network Codes proposed to be modified by this Modification Proposal**

E.ON UK is not aware of any such implications.

- 8 **The implications of the implementation for other relevant persons (including, but without limitation, Users, Connected System Operators, Consumers, Terminal Operators, Storage Operators, Suppliers and producers and, to the extent not so otherwise addressed, any Non-Code Party)**

This Proposal places reasonable limits on the discretion of National Grid NTS and by doing so, introduces certainty for all Users of the NTS about how and when additional NTS Entry Capacity may be released, outside of the established auction structure.

A 28 day notice period for a new pay-as-bid auction limits the gap between the spot

market and the sale of capacity, thereby allowing Users to efficiently and economically manage their own risks.

9 Consequences on the legislative and regulatory obligations and contractual relationships of the Transporters

E.ON UK is not aware of any such consequences

10 Analysis of any advantages or disadvantages of implementation of the Modification Proposal not otherwise identified in paragraphs 2 to 9 above

Advantages

E.ON UK considers that this Proposal:

- Avoids undermining both the existing auction structure and NTS Entry Capacity Baselines. If National Grid NTS were to have unrestricted discretion as to when and how to run a new pay-as-bid auction, this could introduce previously unexpected amounts of NTS Entry Capacity to the market, which could undermine the value of capacity bought or sold in other auctions and would also undermine the importance of existing (or future) Baselines.
- Ensures clarity and non-discrimination by ensuring that Users are aware that under this Proposal, additional or associated unsold capacity can only be released via a pay-as-bid auction and not by any other 'release mechanism'.
- By placing reasonable limits on National Grid NTS' discretion, this Proposal creates certainty and transparency for the market about the structure of NTS Entry Capacity auctions. This is particularly important for new entrants.
- Limits the potential for adverse impact on exchange rates in the 'enduring' Trade and Transfer process by restricting the sale of capacity to strips of NTS Entry Capacity greater than one month.
- Limits any unforeseen impacts on the market by placing time restrictions on National Grid's ability to exercise its new discretionary right to call a new auction. This should allow sufficient industry time before September 2009 to evaluate the success (or otherwise) of this new auction process and to plan for the future.
- A minimum two-round auction facilitates better price discovery in the market than a single round auction.

Disadvantages

If NGG NTS exercises its discretionary rights conferred under this Modification Proposal, it has been indicated by NGG NTS that releasing more capacity in this

way would have an adverse impact on some Trade and Transfer exchange rates.

11 Summary of representations received as a result of consultation by the Proposer (to the extent that the import of those representations are not reflected elsewhere in this Proposal)

The Proposer has met with National Grid NTS to discuss the viability of this alternative Proposal before raising it formally.

12 Detail of all other representations received and considered by the Proposer

None received.

13 Any other matter the Proposer considers needs to be addressed

None

14 Recommendations on the time scale for the implementation of the whole or any part of this Modification Proposal

As with Mod 216, it is our understanding that this Proposal could be implemented immediately following a direction from the Authority.

15 Comments on Suggested Text

To be advised

16 Suggested Text

To be advised

Code Concerned, sections and paragraphs

Uniform Network Code

Transportation Principal Document

Section(s) Section B

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Proposer

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