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Dear John

Modification Proposal 0261: Annual NTS Exit (Flat) Capacity Credit Arrangements

Thank you for your invitation seeking representations with respect to the above Modification Proposal. As proposer of Modification Proposal 0261 National Grid NTS continues to support implementation of the proposal for the reasons set out within it.

National Grid NTS has consulted with Transmission Workstream attendees in the development of this proposal. In particular National Grid NTS has provided detailed financial analysis on the current level of risk and the potential solutions to address that risk. This analysis noted the key differences between the Exit and Entry Capacity regimes, particularly the higher likelihood of portfolio takeovers on Exit compared to Entry and the application of Demonstration Dates¹ in relation to NTS Exit (Flat) Capacity which would lower the overall Shipper default risk in comparison to Entry Capacity.

Although Demonstration Dates do not apply to projects progressed through the Annual Application Window, the risk to the community was still perceived as low due to Revenue Drivers only being applicable to a small number of projects.

It was however recognised that the same situation applies at NTS Exit Points as that identified in Modification Proposal 0246 "Quarterly NTS Entry Capacity User Commitment" whereby a User is able to defer their Capacity registration and associated liabilities by 12 months at a time by not providing sufficient security. For clarification, although the User's Capacity registration would be deferred, National Grid NTS' obligation to make that Capacity available would remain and any under recovery of associated revenue would be picked up by the shipping community.

Modification Proposal 0261 does not change National Grid NTS' obligation to make the Capacity available. If security was not provided by the User, National Grid NTS would apply the sanctions detailed within Section V3.3.2 preventing bids/applications for both NTS Entry Capacity and NTS Exit

¹ Demonstration Dates apply to Adhoc Applications for Enduring Annual NTS Exit (Flat) Capacity. If Works will be required, the Offer specifies a Demonstration Date and Capacity Delivery Date. Users must provide National Grid NTS with certain information (agreed at time of application) by a pre-agreed date, e.g. S36 consents, project plan, board approval, etc. This date can be set three times before National Grid NTS can choose to cancel the User's capacity holding and invoice for any design works incurred up to that point.

Capacity. If the User then subsequently failed to discharge their liabilities, i.e. pay their invoices, then shipper default proceedings would be instigated.

Transmission Workstream agreed that any Exit Capacity proposal equivalent to Entry Capacity Modification Proposal 0246 would be disproportionate to the level of perceived risk. The most appropriate action would be to address the situation whereby a User can defer their Capacity liabilities by not posting security.

National Grid NTS would like to take this opportunity to clarify that National Grid NTS continuously evaluates whether it is economic and efficient to continue throughout the lifetime of each investment project undertaken. If Modification Proposal 0261 were implemented and a User chose not to post security, National Grid NTS would take the same steps as now to evaluate whether to continue with the investment or not. This situation may even be enhanced in the future due to the further signals received through the application of demonstration dates.

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

In respect of Standard Special Condition A11 1a) the efficient and economic operation of the pipeline system to which the licence relates; National Grid NTS believes that this proposal, if implemented, would better facilitate this relevant objective as the removal of a User's ability to defer their Capacity holdings may avoid Users submitting speculative Capacity applications and therefore triggering unnecessary investment if they know they will not be able to defer their Capacity holdings and will be tied in to their financial liabilities.

In respect of Standard Special Condition A11 1d) the securing of effective competition between Shippers; National Grid NTS believes that this proposal, if implemented, would avoid the situation whereby a User defers their Capacity holdings but National Grid NTS' obligation to deliver the Capacity remains and so the shipping community picks up the cost of the under recovery. This would be resolved by the User no longer being able to defer their Capacity commitment and being held to their financial liabilities.

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

Yours sincerely,

Chris Shanley
Senior Commercial Analyst