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for energy consumers

National Grid Gas plc, gas shippers, gas suppliers and other interested parties

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2014/15 Permits Arrangements (varying lead-times for incremental obligated capacity) – Modification of the special licence conditions of the gas transporter licence held by National Grid Gas plc under section 23(1) of the Gas Act 1986

We are making changes to National Grid Gas plc's (NGG) licence to extend its Permits Arrangements to Year 2 of RIIO-T1, and to implement a £13.39m allowance within that year.

On 17 March 2014 we issued a statutory consultation on implementing the Permits Arrangements for 2014-15.¹ Our letter announcing this consultation also provided responses to a previous consultation, issued on 5 February 2014,² and our views on points raised. The March consultation differs from the February consultation only in that we have decided not to include a power in the licence to implement permits by a separate direction.

Background

Users of the NTS provide signals to NGG through the capacity release windows when they require additional capacity. This capacity is known as "incremental capacity".³ NGG is required to deliver this capacity within specified default delivery lead-times. The scale and complexity of the investment in infrastructure required by NGG to deliver the capacity to meet some signals may mean that longer lead-times are required.

To allow NGG sufficient time to provide this infrastructure, we put into effect the Permits Arrangements.⁴ Under these, we grant NGG an allowance of Permits which enables it to extend lead-times where it needs more time to deliver incremental capacity. NGG can also "earn" additional permits by reducing the lead-times for simpler projects. The overall effect is that this allows NGG to trade off the risk of more complex projects with those of simpler projects.

Each permit also has an associated financial value. At the end of each scheme,⁵ NGG receives a sum of money for any permits that it has not used or that it has earned. This incentivises NGG to reduce lead-times where possible.

¹ Ofgem, Statutory consultation on the 2014/15 Permits Arrangements (varying lead-times for incremental obligated capacity) – Notice under section 23(2) of the Gas Act 1986, 17 March 2014

² Ofgem, Statutory consultation on the 2014/15 Permits Arrangements (varying lead-times for incremental obligated capacity) – Notice under section 23(2) of the Gas Act 1986, 5 February 2014

³ Incremental capacity is capacity above NGG's baselines – the amount of capacity NGG is obligated to provide under its licence.

⁴ The Permits Arrangements were first introduced in TPCR4 (Transmission Price Control Review 4) which ran from 1 April 2007 to 31 March 2012.

⁵ The permits schemes are time-defined. Separate schemes were put in place for each of TPCR4, TPCR4 Roll-over and for RIIO-T1.

In our RIIO-T1 Final Proposals,⁶ we said that if the new commercial arrangements were not in place for Years 2-4 of RIIO-T1, we would consider continuing the RIIO-T1 Year 1 Permit Arrangements. The policy and structure of possible Permits Arrangements in Years 2-4 were determined as part of the RIIO-T1 Final Proposals, which we had previously consulted on as part of RIIO-T1. The proposals in this consultation and in our February consultation are therefore in line with the policy in RIIO-T1.

Consultation and responses

We received one non-confidential response to the consultation (from NGG). This supported the licence change. The response commented on the licence text and the policy behind the Permits Arrangements, and is available on our website.

Start date of the Permits Arrangements

NGG stated that the Permits Arrangements should be implemented from 1 April 2014 as otherwise the months of April, May and June would not have permit arrangements in place. NGG expressed concern that consumers might face buyback costs in the event that a signal was received before 1 July 2014.

Status of the Permits Arrangements when the new commercial arrangements are introduced

NGG expressed concerns about the potential treatment of Permits by Ofgem should the new commercial arrangements be introduced partway through the year. NGG indicated that it would not support any retrospective adjustment to the permits volume and argued against any proportionate curtailments of the permits allowance if permits were not required for the full year.

NGG obligation to inform Ofgem about proposed use of permits

NGG said it would not be able to meet its obligation to indicate where it is proposing to extend lead times through the use of permits in its invitation letter 90 days before the July Application Window for Enduring Annual Exit Capacity.

New commercial arrangements

NGG expressed disappointment in our process, progress and timings for approving the new commercial arrangements and about the fact that it was no longer possible to implement these before the July 2014 window.

Our views

Start date of the Permits Arrangements

We do not accept that it is appropriate to have a retrospective implementation date. If an incremental capacity signal were to materialise before the proposed implementation date of 1 July 2014, we would be able to take steps to ensure consumers do not face excessive buyback costs.

Status of the Permits Arrangements when the new commercial arrangements are introduced

We are currently considering what the appropriate and fair treatment of NGG's permit allowance will be, if and when new commercial arrangements are introduced.

⁶ Ofgem, RIIO-T1 Final Proposals for National Grid Electricity Transmission and National Grid Gas, Outputs, incentives and innovation supporting document, Section 3, 17 December 2012

NGG obligation to inform Ofgem about proposed use of permits

We expect NGG to inform us of their intention to use permits in the July application window, in line with the provisions specified within the licence condition.

New commercial arrangements

As noted in our RIIO-T1 Final Proposals, we are keen to see new commercial arrangements in place to deal with incremental capacity requirements. However, we only received the Uniform Network Code modifications on 20 December 2013 and were concerned that the proposals still contained some unresolved issues. Before we make a decision on new commercial arrangements, we must be satisfied that this decision endorses an arrangement which is not contrary to the interests of consumers.

Proposed Licence Modifications

Please find attached a copy of the modifications to Special Condition 2D (Permit Arrangements for the Provision of Incremental Capacity) and Special Condition 3A (Restriction of NTS System Operation Revenue) of the gas transporter licence held by National Grid Gas plc (NGG).

The reasons for these modifications are to:

- a. enable the licensee to continue to manage incremental capacity requests efficiently while new incremental capacity arrangements are developed;
- b. allow existing capacity arrangements to continue, consistent with our RIIO-T1 final proposals;
- c. maintain existing lead times; and
- d. ensure consumers are not potentially exposed to significant incremental buy-back costs under the constraint management incentive.

The effect of the proposed modification is to enable us to issue a direction to:

- a. implement permits arrangements from 1 July 2014 to 31 March 2015;
- b. allow permits earned or not used between 1 April 2013 and 31 March 2014 to be used between 1 July 2014 and 31 March 2015;
- c. increase the permits allowance in the RIIO-T1 formula year commencing 1 April 2014 by £13.39m; and
- d. delay by a year when revenue is earned from the RIIO-T1 permit arrangements.

This modification will take effect on and from 1 July 2014.

This document constitutes notice of the reasons for the decision to modify the gas transporter licence, as required by section 38A of the Gas Act 1986.

If you have any questions regarding the proposed modification please contact Fabien Laroche, (0207 901 3123; fabien.laroche@ofgem.gov.uk) in the first instance.

Yours faithfully,

Andy Burgess
Associate Partner, Transmission and Distribution Policy