



Debra Hawkin
Regulatory Frameworks
National Grid
National Grid House
Gallows Hill
Warwick
CV34 6DA

11 December 2009

Dear Debra

**EDF Energy Response to Charging Methodology Discussion Document NTS GCD07:
“Optional NTS Commodity Tariff”.**

EDF Energy welcomes the opportunity to respond to this consultation, we support the work and progress that NGG has undertaken in looking to update the Optional NTS Commodity Tariff – the Short Haul charge. Currently we support the development of a cost reflective charge that is consistent with NGG’s Licence; we therefore support Option 2.

The current short haul methodology was developed to reflect the costs of laying an independent pipeline and bypassing the NTS on the grounds that this was inefficient. However this is not an objective contained with NGG’s Licence regarding charging methodologies under SLC A5. In particular the requirements of NGG’s Licence condition requires that where prices are not established by an auction then charges should:

- Reflect the costs incurred
- Take account of developments in the Transportation business
- Facilitate effective competition between gas Shippers and Suppliers.

However the current methodology appears to be based around costs avoided by the exit point and providing an incentive to connect to the NTS. Further the costs avoided appear to relate to expenditure that if undertaken by NGG would be classified as TO costs and revenue in the long term and not SO costs. As identified within the consultation SO costs relate to the operation of the system, including costs such as shrinkage and operating margins. However the current methodology is based around construction and connection costs both of which are normally classified as TO costs. It therefore appears that the current methodology also confuses TO costs to develop an SO charge.

In the past the current methodology appears to have been accepted on the grounds that avoiding system bypass benefits consumers in general as sites that opt to take short haul rather than bypassing the system will end up paying charges and so reducing the burden placed on the industry in general. However we would note that it becomes important to differentiate between TO and SO costs and charges. In particular all firm sites have to pay TO capacity charges and there is no availability to reduce these charges through a short haul TO capacity charge. Implementation of the Transportation model through GCM01 helped to ensure that exit points close to entry points received a more cost reflective charge, normally

set to the minimum of 0.0001p/kWh/day. We would note that any revenues from these sites will provide a benefit to consumers in general by reducing the burden of NTS TO revenue they are required to cover, whilst also providing an attractive alternative to bypassing the system as rather than having a large upfront capex expenditure this cost is spread over the lifetime of the plant and is sufficiently low so as to represent a “cheaper” alternative. We believe this in itself provides the incentive not to bypass and in instances where the connecting party can bypass the system at a lower NPV cost then this would represent an economic and efficient development.

The short haul charge also provides a benefit to consumers in general, however EDF Energy believes that this is not accurately targeting costs as customers are receiving a benefit from reduced SO costs, based on the allocation of TO costs. It would appear that if there is a benefit of offtaking gas close to an entry point, this would also come from the perspective of reduced system operator costs, as arguably costs are reduced as the NTS does not have to Transport the gas as far in its system, thereby reducing compressor usage etc. It would appear that the short haul charge should be developed to reflect the reduced system operator costs from connecting close to an entry point.

EDF Energy therefore believes that NGG should develop the Optional NTS Commodity Tariff so that it is more closely related to the SO charges and costs, and reflects the system operator costs avoided by connecting close to an entry point. We therefore support Option 2 in the Discussion Document. In relation to this option, EDF Energy would make the following high level observations:

- It is not clear why the proposed reform and charge should continue to be influenced by distance. This may have been appropriate when the short haul charge was based on TO costs, which vary with distance; however it is not clear how the costs that NGG are attributing to the short haul charge under Option 2 are influenced by distance. It would therefore appear appropriate to move to a p/kWh charge. This would meet the EU regulations requirements and appear to be more cost reflective. Further by combining this with the rule that only sites between the entry point and the next NTS compressor could qualify would ensure that only truly short haul sites could qualify for this discount.
- EDF Energy is unclear why connection costs have been included in the methodology. It appears that NGG is basing this on the assumption that the exit points avoided terminal connection costs. We would note that this does not appear as a relevant objective in NGG’s Licence. In addition whilst the exit point may avoid the terminal connection cost they will however have to fund the NTS connection cost, which are funded outside of transportation charges.
- The load factor is only required as NGG is attempting to convert fixed connection costs to a p/kWh/km charge. We are not convinced that a distance based charge is cost reflective, and removing the distance and connection based charges would avoid this requirement. This would therefore lend itself to a short haul charge at 34.6% of the SO commodity charge.

I hope you find these comments useful, however please contact my colleague Stefan Leedham (Stefan.leedham@edfenergy.com, 0203 126 2312)

Yours sincerely

A handwritten signature in blue ink, appearing to read "Seb Eyre".

Dr. Sebastian Eyre
Energy Regulation, Energy Branch

Appendix 1 Response to Detailed Questions

Q1. Do respondents consider the cost assignment under methodology option one or option two, to be most consistent with the relevant objectives? Do the methodologies;

- **Reflect the costs incurred by the licensee?**

Option 1 appears to utilise a methodology based on the costs avoided by the exit connection. And so is inconsistent with the relevant objectives. Option 2 appears to be more cost reflective as it relates to the costs incurred by the System Operator. However we are not convinced that the SO costs identified and attributed to short haul are related to distance. We believe it is more appropriate to develop a p/kWh charge and limit application to exit points between the entry point and next NTS compressor.

- **Take account of developments in the transportation business?**

The current short haul charge has not been reviewed since 1998. Therefore Option 1 and Option 2 meet this relevant objective as developments in the Transportation Business will be accommodated in this review. However Option 2 better meets this objective as it takes account of the implementation of GCM01, whereas Option 1 appears to replicate the outcomes of GCM01.

- **Facilitate effective competition?**

EDF Energy believes that effective competition is facilitated by ensuring that costs are correctly targeted. This ensures that there is no cross subsidises between market sectors. Therefore as Option 2 is cost reflective, it will also facilitate effective competition.

Q2. Do respondents have any views on the appropriateness of the costs and parameters used in the derivation of the tariff under option one? Specifically;

We do not believe that Option 1 is cost reflective, and our response to these questions should not be seen as providing support for implementation of this option.

- **The connection cost approach?**

An exit point will have to fund the connection costs regardless of whether it bypasses the NTS or not. By including connection costs the methodology appears to assume that these will not be incurred if it connects to the NTS. It therefore does not appear to be appropriate to include these costs as they will be funded by the exit point regardless of whether it connects to a terminal or the NTS.

- **The annuitisation period; 10 years, 45 years or other?**

A 45 year annuitisation period appears appropriate as this is aligned with the depreciation of NTS pipelines.

- **The load factor?**

NGG has ruled out the ability to apply a site specific load factor, and so an industry load factor has not been applied, on the grounds that site specific is too complex. However we would note that for large GDN sites their capacity and commodity charges are a function of SOQ which is derived from their load factor. Given that there are significantly more GDN sites that fall into this category than NTS, we are surprised NTS can not utilise a site specific load factor.

It appears that NGG is proposing to use a 75% load factor as if a 50% load factor is used; there is a risk that new connections with a higher load factor will continue to bypass the system as they will be “over charged”. We do not believe that the objective to avoid bypass is consistent with NGG’s Licence. In addition whilst some sites with higher load factors may be “over charged”, the proposed load factor would result in the majority of short haul sites being “under charged”. If a national load factor is to be used then it would appear more appropriate to utilise an average load factor. This will ensure that as a “sector” short haul sites pay an appropriate charge, although there will be winners and losers at a site specific level. We would note that this is also consistent with the GDN proposed methodology for interruptible sites under DNPC03, whereby as a sector interruptible sites would continue to pay the same level of distribution charges, but there were winners and losers at a site specific level depending on their load factors.

Q3. Do respondents have any views on the appropriateness of the costs and parameters used in the derivation of the tariff under option two? Specifically;

- **Whether the minimum cost should be based on a connection cost approach or a proportion of the SO costs related to short-haul?**

As previously noted EDF Energy believes that the short haul tariff should be related to a proportion of SO costs as this is the most cost reflective. However we do not understand why this charge also has to be distance related. NGG has identified in the discussion document that the SO costs that should be included for short haul are Un-accounted for Gas (UAG), and internal costs. This provides a 34.6% cost proportion which would also cover a fair share of “K” and incentive costs. These costs do not appear to alter with distance, and so it is questionable why a distance related charge should be applied. If SO charges are cost reflective with a p/kWh charge, then it would appear that a short haul p/kWh charge would also be cost reflective.

- **Whether the SO costs associated with short-haul (34% for the indicative charges) should be set on an annual basis or fixed, based on a long term trend?**

Varying the proportion year on year would create issues with predictability of charges, and potentially require additional reporting by NGG to the TCMF. Our preferred approach would be to base the split on a long term trend (e.g. 5 years) and review this split at the start of each price control period. This would aid predictability for Shippers, whilst also ensuring that the charge remained cost reflective.

Q4. Do respondents have any views on the application of the methodology? Specific comments on the following are requested:

- **Distance from the exit point to the ASEP – in the case of ASEPs with more than one SEP is it appropriate to measure the distance to the nearest SEP?**

As previously noted EDF Energy does not believe that a distance related charge should be applied to the cost reflective option. We are also not convinced on basing the distance from the nearest SEP. In particular we would note that were gas is flowing from the furthest SEP and not the closest then the distance will be (potentially significantly) underestimated and so the short haul rate too low. The current methodology of using the mid-point therefore appears the most appropriate as on average this should be the most reflective of distance travelled (provided that the load factors of the SEPs are the same).

- **Load factor – is it appropriate to use a system load factor or an exit point load factor?**
 As previously noted given that the GDNs can apply charges based on SOQs which are derived from load factors, we believe that the NTS should also apply an exit point load factor. The number of sites that would be impacted by this is significantly less than those on the GDNs and so this should be simpler. However if NGG does not wish to use a site specific load factor than an average load factor would be more appropriate, either at a system or short haul level depending on the methodology adopted.
- **Minimum charge – should there remain a minimum charge? If so, what level should this be set at? Should this be related to the exit point capacity (EPC)?**
 EDF Energy believes that a minimum charge should be applied, as otherwise this would imply that there are no costs incurred. We believe that setting the short haul charge at 34.6% of the full SO commodity charge would resolve this issue.
- **Annual updating of charge – should the charge be updated in parallel with other transportation tariffs?**
 Yes. This will ensure that charges remain cost reflective, and expose short haul sites to the same risk faced by all other NTS Exit points. We would note that if short haul sites were provided with the ability to lock in their charges, then it would appear unduly discriminatory to not provide the same option to other NTS Exit Points. However this in turn could create issues with under recovery of revenue.
- **Application to multiple exit points from a single entry point – do respondents agree that the present default allocation rule should apply when the input allocations are below the output allocations?**
 EDF Energy recognises that currently system limitations prevent the application of alternative arrangements. However another potential solution would be to allow the application of alternative arrangements as a User Pays service.
- **Application at storage exit points – do respondents agree that the ‘short-haul’ tariff should not be applicable at storage exit points?**
 EDF Energy agrees with NGG that short haul should not be available to storage exit points. As recognised by NGG this appears to be an oversight from when commodity charges were only applied to entry flows.
- **Do respondents agree that the charge should only be applicable to the exit points that are connected between an ASEP and the next downstream compressor?**
 This solution would appear most compatible with implementation of Option2 based on a discounted SO commodity charge without a distance related element. The methodology for Option 2 excludes compression costs and so any site past a compressor would benefit from this service but not pay the costs associated with this. In addition by implementing this limitation it removes the requirement to have a distance related charge, and so ensure compliance with EU Regulations.

Q5. Do respondents support either an implementation date of 1st October 2010 or an alternate implementation date?

EDF Energy supports a 1 October 2010 implementation.