nationalgrid

National Grid House
Warwick Technology Park
Gallows Hill, Warwick
CV34 6DA

Stuart Cook
Senior Partner, Transmission & Governance
Ofgem
9 Millbank
London
SW1P 3GE

Anne Bennett
Charging and Revenue Manager

anne.bennett@uk.ngrid.com
Direct tel +44 (0)1926 653445

www.nationalgrid.com

3 November 2010

Dear Stuart,

Indicative notice of NTS Charges to apply from 1st February 2011 and 1st April 2011

I am writing to give notice of our intention to make changes to NTS gas charges. This notice covers two sets of changes:

- changes that will take effect on 1 February 2011 in respect to 2010/11 revenues; and
- additional changes on 1 April 2011 in respect to 2011/12 revenues.

Indicative NTS Charges to apply from 1st February 2011 (SO Charges Only)

The SO charges that applied from 1 October 2010 were set on 30 July 2010 in order to give the required two months notice of the change. When setting SO charges National Grid is required to forecast the system operation costs for the year, including the cost of shrinkage. The October 2010 charge was set considering the prevailing volume of unaccounted for gas (UAG) and prior to the discovery of a significant meter error at the Aberdeen offtake. The meter error was discovered and corrected on 10 August 2010; notified to the industry on 24 September 2010[1]; and discussed at the October 2010 Offtake Arrangements Workstream meeting[2]. Following the correction of the Aberdeen meter error and other actions to reduce underlying UAG, there is now evidence of a sustained reduction in absolute UAG volumes of 33% (comparing July and October). This, coupled with a reduction in wholesale gas prices from those forecast when charges were set, results in a significant reduction in forecast shrinkage costs for 2010/11 and therefore the SO allowed revenue for 2010/11. Since this was not known when SO Commodity Charges were set for October 2010, they will recover a higher level of costs that are now expected to be incurred during 2010/11.

This has been compounded by the ongoing process to reconcile previously notified meter errors. To reflect the progress that has been made in assessing these since charges were last set, including the expectation that the Braishfield meter error[3] will be reconciled by the end of

[1] Meter Error SC006, Scotia Gas Networks
[2] http://www.gasgovernance.co.uk/OA/081010
[3] Meter Error SC001, Scotia Gas Networks

2010/11[2], we have increased our forecast of meter error reconciliations in 2010/11 from c.£19m to c.£28m. The associated credit to shrinkage costs in 2010/11 is therefore larger than previously expected, further reducing the SO allowed revenue in 2010/11.

The combined effect of reduced shrinkage costs due to declines in underlying UAG and credits from meter error reconciliations means that the forecast SO collected revenue in 2010/11 is expected to exceed the SO allowed revenue by approximately 13%.

We consider a third price change in 2010/11 is necessary to ensure that charges remain cost reflective in 2010/11 to shippers currently using the system. To this end, we believe a shorter indicative notice period of 3 months (compared to the standard 150 days) can be justified, particularly given the extent of the predicted over-recovery. **Final notification of these changes will be published by 1 December 2010 to provide 2 months notice before coming effective**. The change would apply to the SO Commodity Charge and the St. Fergus Compression Charge and would be levied on relevant flows during February and March. This will have the impact of reducing the forecast over-recovery to zero for 2010/11.

The following are our current central forecasts for charges to **apply from 1st February 2011**:

- The indicative **NTS SO Commodity charge**, as applied to both entry and exit flows, is 0.0057 p/kWh. This is a decrease of 70 % and is caused mainly by the changes to shrinkage costs in 2010/11. Due to the length of the period that the price change will apply to we believe the range to be -20% & +26%, corresponding to 0.0046 p/kWh to 0.0072 p/kWh.

- The **St.Fergus Compression charge** levied at the Total Oil Marine (TOM) sub-terminal at St. Fergus is expected to decrease to an indicative level of 0.0115 p/kWh, a reduction of 17% on the current rate. This reduction is due primarily to adjustments in wholesale gas prices.

Indicative NTS Charges to apply from 1st April 2011

The following are our current central forecasts for charges to **apply from 1st April 2011**.

- The **NTS TO Commodity Charge** levied on entry flows is estimated to increase marginally from its current rate of 0.0174 p/kWh to 0.0196 p/kWh, representing an increase of 13%. Whilst the revenue to be collected from the TO Commodity Charge has increased due to a rise in the TO allowable revenue, this has been mostly offset by an increase in chargeable volumes. The charge has been set based on the assumption that it will be applied for the full financial year and it will be reassessed in October 2011 following further entry capacity auctions. Against this background, the charge has been calculated taking into account the uncertainties around forecasting auction revenues and entry volumes, therefore our indicative range around this charge is 0.0186 (-5%) to 0.0206 (+5%) p/kWh.

- The indicative level of the **NTS SO Commodity Charge**, as applied to both entry and exit flows, is 0.0174 p/kWh. Compared to the average charge for 2010/11, taking into account the price change in February 2011, the charge has decreased by 1% from

0.0175 p/kWh[4]. Shrinkage costs for 2011/12 are comparable to the latest forecasts for 2010/11 and include the reductions in forecast UAG expected in 2010/11.

The indicative charge includes an adjustment for the expected reconciliation of the Aberdeen meter error during 2011/12. Prior to the appointment of an Independent Technical Expert, we have forecast the impact of the reconciliation using the error volume noted in the Offtake Arrangements Workstream[2] (3.2TWh) and the system average price over the period of the meter error. Against this background, we have made an initial adjustment of c.£30m to SO allowable revenue 2011/12. We will update this view as further information becomes available from the Independent Technical Expert.

We believe that the variation in our estimate of this charge taking into account forecast costs and volumes and excluding any variances in meter adjustments is in the region of -15% / +15%.

- The **St Fergus Compression Charge** levied at the Total Oil Marine (TOM) sub-terminal at St. Fergus is expected to decrease from the indicative February 2011 rate to an indicative level of 0.0113 p/kWh, a decrease of 2%. However, compared to an average rate of 0.0094 p/kWh[4] during 2010/11, this is an increase of 20%. The increase is due to a combination of forecast increased compressor fuel costs and forecast reduced volumes through the TOM sub-terminal. We estimate the range on this charge to be -20% / +20%. When setting this charge we have taken account of the expected installation of electric drives during 2011/12, both in terms of the forecast efficiency and resultant fuel costs. The charge is set based on the assumption that it will be applied for the full financial year but will be reassessed in October 2011.

- The **CSEP administration charge** has been reviewed and the indicative rate is a small decrease from 0.1233 to 0.1020 pence per supply point per day (£0.37 per annum). Other administration charges (those for allocation of shared supply meter points and interconnector arrangements) are being reviewed.

If you have any questions about this Indicative Notice, or NTS charges in general, please contact myself or the Charging and Revenue Team on 01926 654633.

Anne Bennett
Charging and Revenue Manager

[4] This is calculated based on the forecast annual revenue collectable from the charge and the relevant forecast annual chargeable volumes