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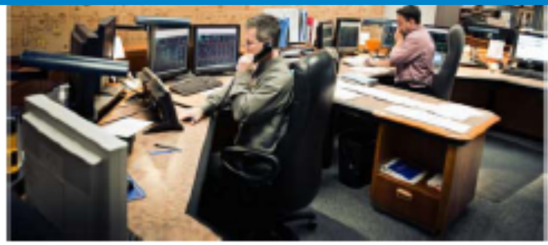
March 2012 Business plan
Incentives

1 May 2012
Transmission Workgroup





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SO incentive development (1)

- We are currently developing our May SO incentive submission
- We would welcome your views on our current thinking
- There is a written consultation open which closes on 9th May
- We are also happy to have bi-lateral discussions, if interested, please contact:
  - email soincentives@nationalgrid.com,
  - or call Juliana Urdal on 01926 656195
  - or Phil Lucas on 01926 653546.

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SO incentive development (2)

- This session covers our proposals for incentives in two areas:
  - Delivery of timely connections
  - Constraint Management
- Plus our consideration of potential new areas for incentivisation:
  - Maintenance
  - Capacity Scaleback
  - Provision of enhanced services for NTS users

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Timely connections

- Both a physical connection and capacity rights are required to input gas to- or offtake gas from- the NTS
- In order to ensure timely connections, we are proposing potential incentives in three areas:
  - Connection offers
  - Pre capacity application activities
  - Post capacity application activities

Connection offers

- Mod 373 sets out a clearly defined offer process
- The timescales in that mod are a reflection of our current ability to deliver that work
- But they are longer than those originally envisaged by the industry
- It may be the case that in the future innovative ways of working can be employed to optimise those timelines further
- Is it appropriate that a financial incentive is introduced to encourage us to actively explore those innovative opportunities?

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Pre-capacity application delivery

- Through our Talking Networks activities we have presented a generic timeline that demonstrates our understanding of The Planning Act requirements
- Stakeholders have expressed concern about the length of this timeline and asked whether it can be optimised
- The timeline represents our current understanding of the legislation’s requirements
- It may, however, be possible to optimise and shorten this timeline as our experience develops and/or legislative requirements develop
- We therefore propose that we are subject to a reputational incentive on the time taken to progress from PCA signature to capacity application
- Does this assure you that the process will be flexible?

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Post-capacity application delivery

- We propose development of a specific scheme to manage agreed capacity delivery timescales under the PCA:
  - This would be separate from the constraint management scheme (referred to in later slides);
  - Covering both early and late delivery such that if we agree a delivery date under the PCA:
    - we deliver early, we receive an incentive payment,
    - if late, then we receive a penalty
  - To be of sufficient value to cover costs of accelerating construction and financing costs (if funding delayed).
- What, in your opinion, is the appropriate price to use in this incentive?

Constraint Management -1

- Within the RIIO-T1 submission (Managing Risk and Uncertainty Annex) we have outlined our proposed approach regarding constraint management.
- At a high level, we propose:
  - Single scheme to apply across Entry and Exit*;
  - Consideration of 'Maintenance Days' on Entry;
  - Retention of cap/collar within incentive scheme;
  - Consideration of RIIO-T1 plan when setting relevant target for scheme.
- Details to be firmed up in May SO submission hence further industry discussion.

* Note that the delivery incentive is covered via a separate scheme which was discussed previously.

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Constraint management - 2

- Our proposal to determine the appropriate annual constraint management target is to consider two different, but complimentary approaches;
- Target will be a combination of what can be set ex-ante and what will be considered as part of application of specific uncertainty mechanisms, so will be calculated as follows:

Constraint management target	=	Ex-ante operational constraints	+	Ex-ante investment constraints	+	Incremental operational constraints	+	Incremental investment constraints
		(1)		(2)		(3)		(4)

- Note that the target does not include the impact of, as yet, un-triggered uncertainty mechanisms which may have an impact through commissioning or other operational actions

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Constraint management - 3

- Target is made up of:

	Funded ex-ante in RIIO-T1 settlement	Driven by uncertainty mechanism
Operational constraints Driven by the inherent level of risk on the network which results from: • changing flow conditions from existing supply and demand capabilities • unplanned maintenance • residual risk relating to the application of the uncertainty mechanisms	***1*** Ex-ante operational constraint management	***3*** Incremental operational constraint management
Investment constraints Driven by investments proposed in our TO investment plan relating to: • construction activities (such as pipeline tie-ins) • commissioning activities (such as in-line inspections & compressor commissioning)	***2*** Ex-ante investment constraint management	***4*** Incremental investment constraint management

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Constraint management - 4

- What does the table on the previous slide mean in practice?
  - The “Operational constraints” row is the ongoing risk on the system
  - The “Investment constraints” row is a level of additional risk for a predefined period of time
  - The “Funded ex-ante” column relates to investments which we’re asking to be included within the agreed baseline revenue allowance for the RIIO-T1 period, so can be considered now
  - The “Driven by uncertainty mechanism” column relates to changes in constraint costs which result from one or more of the uncertainty mechanisms being triggered.

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Constraint management - 5

- In relation to provision of Incremental capacity, we are proposing that the agreed methodology statement for calculation of revenue driver allowances would include the relevant allowance to cover constraint risk during construction and commissioning:
  - This would be for a defined period of time (Box 4 in the table).
- Additionally, where build alone was not the efficient solution, the methodology would propose:
  - The application of a factor of 80% (as per TPCR4 precedent) for a contractual solution;
  - Or could propose that a step change is made to the constraint management target (if additional/reduced on-going risk is felt to be economic answer) (Box 3 in the table).

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Constraint management - 6

- Additionally, consideration of an appropriate adjustment to the constraint management target should be made when other uncertainty mechanisms are triggered, such as:
  - Network Flexibility
  - Asset Health
  - Industrial Emissions Directive (IED)
  - Critical National Infrastructure (CNI)
  - GB & EU market facilitation

Transitional projects – link with constraint management

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- Alongside the above, we need to consider the impact of the proposed changes to the regulatory and commercial framework on so-called ‘transitional projects’ – those that already have planning permission and are ready to apply for capacity
  - Consider development of a longer-term non-firm product to allow capacity to be released and managed in the absence of or until reinforcement is achieved;
  - Alternatively, we could consider:
    - The introduction of an agreed and specifically targeted buyback incentive to manage the potential constraints;
    - Making release of incremental capacity discretionary rather than obligatory.

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Potential new areas for incentivisation?

- We have identified some areas where the introduction of new incentives could be explored further over the RIIO-T1 period:
  - Maintenance
  - Capacity Scaleback
  - Provision of enhanced services for NTS users
- We are interested in your views

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Maintenance

- Through our March RIIO-T1 business plan submission we have put forward an option to introduce maintenance days on entry as well as exit in order to minimise constraint costs to end consumers
- Through previous consultations stakeholders have expressed concern about the scheduling of, and flexibility around, maintenance activities
- Changes to maintenance schedules can be both an inconvenience and of benefit
- We work closely with our customers to find the best approach for all
- Would you support the introduction of an incentive relating to scheduling of maintenance (notice periods and flexibility)?
- What value should this have?

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Capacity Scaleback

- Under the UNC we have obligations to release defined quantities of non-firm capacity
- There is no obligation to restore curtailed rights at the earliest opportunity
- Enduring exit introduces off-peak product
- The introduction of an incentive in this area may lead to the optimisation of, and increase the relative value of, non-firm capacity
- Would an incentive in this area maximise the level of capacity available in the market?
- What is the appropriate value of such an incentive?

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Provision of enhanced services

- We currently accept requests for additional services where we can accommodate them, such as:
  - Facilitating higher ramp rates or
  - Accepting shorter notice periods
- Some customers have suggested that they would be willing to pay for additional services and products to meet their needs
- We recognise there is a linkage with the Network Flexibility uncertainty mechanism
- Do you value such additional services?