

National Grid’s specific response to questions raised in E10-GNM-13-03b: ERGEG consultation on Pilot Framework Guidelines on gas balancing rules.

| Problem identification, scope, definitions, purpose, policy objectives and compliance |
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| <p>Question 1: Do you agree that the problems identified in the problem identification chapter are the main ones? Are there additional problems that should be addressed within the gas balancing pilot framework guideline?</p> |
| <p>The chapter does indeed capture the key problems but care must be taken when considering the kind of balancing actions that the TSO must take and whether the balancing actions of a TSO should be expected to reduce if shippers are able to balance their portfolio efficiently.</p> |
| <p>Question 2: Do you agree with the scope (section 1) and objectives (section 3) of this pilot framework guideline? Are there policy issues that should, but are not currently addressed by the draft document?</p> |
| <p>National Grid supports the scope and objectives of the framework guideline in so far that they meet the over-arching objective of encouraging and facilitating gas trade across systems and the development of competition within the EU.</p> |
| <p>Question 3: In your view, should the European network code for gas balancing lead to an amendment of national balancing rules? If so, how detailed should the European target model be?</p> |
| <p>It is inevitable that if the objectives of the balancing code are to be met that amendments are likely to be required to national balancing rules within member states. The level of detail for the European target model must be mindful that different solutions may need to be employed by different transporters to reflect the physical design and inherent flexibilities of each network. For example, the characteristics of a large meshed network, such as that operated by National Grid, are very different to the networks of other TSO’s which may be simply a single transit pipeline.</p> |
| <p>Question 4: Do you agree with the approach of defining a target model for the network code and allowing interim steps subject to NRA approval?</p> |
| <p>A target model is useful for describing a goal that different regimes should aim for. Network specificities will dictate the realistic pace that different transporters can move towards the target model, therefore describing a series of interim steps towards the target is both practical and prudent.</p> |
| <p>Question 5: What timescale is needed to implement the provisions in the target model outlined in Part II after the network code is adopted? Is 12 months (as in section 10) appropriate or should it be shorter or longer?</p> |
| <p>12 months is not realistic and will be highly dependent on the existing physical and commercial designs of each specific regime in the Member States. The key is to accept the concept that different transporters will be able to progress towards the target model at different rates. This may involve a number of interim steps with the requirement that each interim step must first be successfully demonstrated before the TSO progresses to the next step towards the target model.</p> |
| <p>Question 6: Should the pilot framework guideline be more specific regarding the purpose and policy objectives for network codes (section 3), in particular areas including nomination procedures?</p> |
| <p>No, National Grid feel the amount of detail contained in the framework guideline with regards to</p> |

the purpose and policy objectives for network codes is adequate and that any additional detail should be developed as part of the development of the gas balancing code itself.

Question 7: With reference to section 3 (proposed policy objectives), do you have comments on how Article 21 of the Gas Regulation 715/2009 should be reflected in the gas balancing network code?

National Grid has no strong views as to how this regulation should be reflected in the gas balancing code but it would guard against the Code being overly prescriptive in detailing approaches to achieve compliance with Article 21. The principle of subsidiarity should be followed to allow NRAs to approve solutions that reflect the physical design and inherent flexibilities of each network.

The role of network users and TSOs

Question 8: Is it necessary to have a harmonised approach to the network user and TSO roles regarding gas balancing?

It is necessary to have a coherent approach, which may involve some harmonisation of the roles of the network user and the TSO.

Question 9: What are your views on the proposals for the target model to be reducing the need for TSOs to undertake balancing activities?

The target model is consistent with the arrangements in Great Britain (GB) and these arrangements have ultimately reduced the need for the TSO to undertake balancing actions. This target model may not necessarily be easily applicable to all systems and other systems may need to progress through the interim steps as a means of reaching the target model.

As a daily balancing period is adopted across Europe and balancing zones are merged to become geographically greater in size there may be an increase in the requirement for some TSOs to consider locational actions and there may also be an increased requirement to structure the flow profiles to accommodate potential temporal imbalances, even though the shippers have an increased ability to balance efficiently within the balancing period. This can be achieved in a number of ways and should not detract from the benefits of a daily balancing period.

Question 10: Is it appropriate for the target model to impose within-day constraints on network users? If so, should such constraints be imposed on all network users or only on certain groups of network users? If within-day constraints should only be imposed on certain groups of network users, which ones are these? How could this be justified?

We are not convinced it is appropriate for the target model to impose within-day constraints on network users, other than for local balancing purposes where the TSO is addressing imbalances at particular locations in the system. However as such arrangements will be subject to consultation and need to be approved by the NRA this will ensure there are no impacts on new market entrants.

Question 11: Is balancing against a pre-determined off-take profile a useful interim step?

The target model is consistent with the arrangements in Great Britain and therefore we are not best placed to comment on the interim target.

Question 12: Should TSOs have the option to sell flexibility provided by the gas transmission pipelines system (linepack) subject to the NRAs' approval? If so, should this be mandatory?

TSOs should have the option to allocate or sell linepack, subject to the NRA's approval. We do not believe it should be mandatory to do so as there could be physical network characteristics that may not make selling or allocating linepack feasible because it is always required by the TSO to operate the network. As highlighted in the balancing guideline the amount of flexible gas (and in particular linepack) available to TSOs is limited and increasing access to flexible gas may be the priority in a number of EU member states.

In consultation with shippers and other interested parties National Grid are developing a linepack product (end of day product) that looks to allocate line-pack to network users. Work to date has concentrated on understanding what volume is available, in what circumstances it is made available for allocation to a network user and how any allocation is valued. To date there have been no discussions on simply selling linepack, although the above allocation of linepack may involve a competitive auction process. We believe that this linepack product if implemented would be consistent with the guidelines.

Question 13: Should the target model enable TSOs to provide tolerances to market participants for free or should this be an interim step?

We feel it is appropriate for the use of tolerances to be confined to the interim steps. Tolerances reduced the incentives on users to maintain their balance across the period.

TSO obligations on information provision

Question 14: Are there any additional information requirements that you believe should be included? In particular, should the pilot framework guideline oblige TSOs to provide information beyond the requirements set out in the revised Article 21 and Chapter 3 of Annex 1 to Regulation (EC) No 715/2009 (as recently approved through comitology)? If so, please provide details?

It is unclear from the draft framework guideline whether the information set out in Article 21 is sufficient and what additional information needs to be provided. It is therefore recommended that the market be given time to assess if the new transparency requirements arising from EC 715/2009 are sufficient before embarking on further changes.

Question 15: What are the benefits and disadvantages of TSOs providing network users with system information?

See above.

Questions 16: What are the costs of TSOs providing network users with system information? How do these compare against the benefits and/ or disadvantages?

See above.

Balancing periods

Questions 17: What are your views on our assessment of the policy options?

We agree that Daily is the most appropriate balancing period. Although as stated earlier, as a daily balancing period is adopted across Europe and balancing zones are merged to become geographically greater in size there may be an increase in the requirement for some TSOs to consider locational actions and there may also be an increased requirement to structure the flow profiles to accommodate potential temporal imbalances. This can be achieved in a number of ways and should not detract from the benefits of a daily balancing period.

Questions 18: Are there relevant additional policy options on balancing periods which have not been considered in this section? Should these be considered going forward?

Not as far as we are aware.

Questions 19: Is it necessary to harmonise balancing periods? If so, what are the benefits of a regional or pan-European harmonised balancing period? If not, why is it not necessary?

Please explain your answer.

We feel that it is appropriate to harmonise the balancing period if the goal is to encourage the integration (harmonisation) of gas markets across the EU and promote cross-border trade.

Questions 20: If you agree with a harmonised balancing period, what do you consider is the appropriate length of the balancing period?

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| Daily. |
| Question 21: Do you agree with the target model? (Please explain your answer). |
| Yes - a 24 hour balancing period allows for sufficient incentive to be placed on network users to balance their inputs and offtakes. A shorter period (hourly) restricts such activities. However, we feel it is appropriate to consult on the costs and benefits of harmonising the balancing period, including the requirement for a common starting time and ending time. |
| Question 22: What would be the costs of implementing the target model in (and beyond) your Member State or balancing zones(s) (as the case may be)? |
| The costs and benefits of harmonising the period, including the requirement for a common starting time and ending time are not yet known. |
| TSO buying and selling of flexible gas and balancing services |
| Question 23: Do you agree with our assessment of the policy options? |
| Yes - it is appropriate for TSOs to utilise a wholesale market to buy and sell balancing gas. |
| Questions 24: Do you agree with the target model? (Please give reasons). If so, what do you consider are the benefits and disadvantages of the target model? |
| Yes. The experience in the GB market has led to appropriate incentives on users and the system operator resulting in fewer (and smaller) market balancing actions by the TSO, leading to greater efficiency and ultimately reduced costs to consumers. Also the adoption of the within day wholesale market as the primary balancing tool by National Grid has helped develop the NBP into one of the most liquid and efficient gas markets in the world. |
| Questions 25: What are the costs of implementing the target model in your Member State? |
| The target model is consistent with the arrangements in Great Britain, so the costs should be minimal but have not yet been confirmed. |
| Questions 26: What interim steps, if any, may be needed in your Member State or balancing zone(s)? |
| N/A |
| Questions 27: Is it appropriate for balancing platforms to be part of the target model subject to NRA approval, even where markets are sufficiently liquid to enable TSO procurement on wholesale markets? |
| This should be restricted to the interim steps only. |
| Questions 28: Is it appropriate for TSOs to procure balancing services on the wholesale market and/or or is appropriate for these to be procured on the balancing platform? Should TSOs be permitted to reserve long-term contracts for flexible gas and/ or associated capacity for this purpose? |
| In Great Britain the TSO procures balancing services predominately from the wholesale market but we recognise that network configuration and market liquidity may make this difficult in other member states. We feel it is appropriate for localised balancing services to be procured via other means. |
| Question 29: In your view is it possible in your market to reduce TSOs' reliance on long-term products? If so, how may this be best achieved? |
| Yes. Since the introduction of the current arrangements, in GB, National Grid's reliance upon longer term products has reduced to the minimum required to prevent a minor issue on the network from resulting in an emergency. |
| Imbalance Charges |
| Question 30: Do you agree with our assessment of the policy options? |

Yes.

Question 31: Do you agree that methods for calculating imbalance charges should be harmonised? If so please explain what the benefits may be. If not, please explain why not.

It is our view that the harmonisation of imbalance charges should be encouraged through the adoption of high-level principles (reflective of costs, include a small uplift, etc.) as defined in the EU balancing guideline and as such the calculation of imbalance charges itself should not necessarily have to be harmonised/be the same.

The draft balancing guidelines indicate that:

- Where TSOs use the wholesale market or a balancing platform to buy or sell balancing gas, the imbalance charges shall be based on the marginal price paid by the TSOs.
- The Imbalance charges of network users that contribute to the system imbalance should reflect the balancing actions taken by the TSO.
- Where no balancing action is taken by the TSO, the imbalance charge shall be based on the price on the wholesale market.
- The imbalance charge may also include a small uplift in order to incentivise the network users to balance.

The current System Marginal Prices (SMPs) used in GB are derived from either the price of National Grid's Market Balancing Actions (MBA), or System Average Price* (SAP) plus or minus a default value (cashout fixed differentials). The cashout fixed differentials used in GB are the way that a small uplift is calculated and applied to SAP to create the imbalance charge. This approach is consistent with the above balancing guideline principles.

National Grid is currently seeking to introduce an updated default SMP in consultation with shippers and other interested parties. The intent is that any updated imbalance charges will be consistent with the target model.

The guidelines also indicate that network user imbalance charges that reflect the balancing actions taken by the TSO, may reflect whether the network user's imbalance contributes to the overall imbalance on the system or helps to reduce the overall system imbalance. This is not currently a feature of the prices set as a result of a balancing action or being considered by National Grid as part of the aforementioned work to update the default SMPs. We do not believe that this is the most economic and efficient solution, as the over-arching principle of imbalance charges is that they should incentivise network users to balance and rewarding any fortuitous imbalance is not productive in this regard .

*"System Average Price" is the volume weighted average price of all trades (including network user to network user trades) on the OCM in relation to the day.

Question 32: What are your views of the target model? In particular, please provide your views on:

- **Whether an imbalance charge should be applied when TSOs do not take balancing actions;**
- **What the imbalance charge should be based on, if it is applied when the TSO has not taken a balancing action, whether imbalance charges should be dual or single priced;**
- **Whether imbalance charges should be based on the marginal price.**

a) Yes, we feel it is appropriate for imbalance charges to be applied when the TSOs do not take balancing actions. This answer reflects what happens in GB. In GB the TSO only takes a balancing action on less than 50% of days.

National Grid believes that the primary responsibility to balance should rest with the network user and we believe that an imbalance charge is the most efficient mechanism to incentivise this

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| <p>behaviour even where the TSO does not take a balancing action.</p> <p>It should be recognised that National Grid (TSO) is also influenced by the System Operator (SO) incentives that accompany these UK balancing rules. These incentives actively encourage the TSO not to take a balancing action.</p> <p>b) The answer to question 31 provides details of how the imbalance charge is calculated when no balancing action is taken and it can be seen that a dual price approach is undertaken (SAP plus or minus a default value (cashout fixed differentials)).</p> <p>This fits in with the target model in the guidelines:</p> <ul style="list-style-type: none"> - Where no balancing action is taken by the TSO, the imbalance charge shall be based on the price on the wholesale market. - The imbalance charge may also include a small uplift in order to incentivise the network users to balance. <p>c) Yes, the answer to question 31 provides details of how imbalance charges (System Marginal Prices (SMPs)) are calculated based on SAP.</p> |
| <p>Question 33: What would be the costs and benefits of implementing your preferred options in your Member State?</p> |
| <p>The balancing rules in GB are consistent with the target model for imbalance charges and therefore no additional costs or benefits are envisaged.</p> |
| <p>Question 34: What are your views on the interim steps in the document?</p> |
| <p>The target model is consistent with the arrangements in Great Britain and therefore we are not best placed to comment on the interim target.</p> |
| <p>Cross-border cooperation</p> |
| <p>Question 35: Are there any other relevant policy options on cross-border cooperation that should have been included in this section?</p> |
| <p>No.</p> |
| <p>Question 36: Do you agree with our assessment of the policy options in this section?</p> |
| <p>Yes but we agree that harmonisation of balancing rules is a prerequisite and further work is required in this area, which shall include an IA on the cost benefits impact.</p> |
| <p>Question 37: Are Operational Balancing Accounts (OBAs) useful to deal with steering differences? Should the network code make it mandatory on TSOs to put in place OBAs?</p> |
| <p>We understand that the majority of gas transporters (TSOs) within the European gas market which operate at cross-border Interconnection Points (IPs) utilise the concept of Operational Balancing Agreements (OBAs) and undertake the matching of shippers' nominated flows across the IPs. In essence, the TSOs are operating a central dispatch function (matching nominations) both across the IPs and, within their own gas transmission networks.</p> <p>However, at this stage we feel the network code should not make it mandatory for TSOs to put in place OBAs. The emphasis should be on TSOs working together to define what a steering difference is in terms of magnitude and what mechanisms (high-level principles) would be appropriate for dealing with such steering differences.</p> <p>The implementation of a fully liberalised GB gas market in 1996 and its subsequent development since means that there are fundamental differences between the commercial operations of the GB and other European gas markets. In the GB gas market, the purposes, provision, exchange and</p> |

validation of nominations differ from that elsewhere in Europe. Under the auspices of the Uniform Network Code, shippers and traders are obliged to provide nominations (and/or renominations) to National Grid to indicate their intended physical gas flows and gas trades that have occurred at the National Balancing Point (NBP). The NBP is a notional accounting point i.e. it does not physically exist but through which all physical gas must 'pass' and it is also the point at which the participants in the UK gas market register "over the counter" (bi-lateral) gas trades.

The introduction of OBAs would have a significant impact on the role of National Grid as the TSO, the legislative and contractual arrangements currently in place, GB's market based balancing tools, the energy allocation and ownership transfer and accounting processes and the IT systems that support these arrangements.

OBAs also seem to contradict a number of the other key elements of the EU balancing guidelines, which are seeking to:

- Encourage Network Users to balance their own inputs and offtakes, resulting in the TSOs buying/selling less gas;
- Ensure Network Users have access to relevant and transparent information; and
- Move Europe to adopt liquid market based balancing zones and arrangements and for TSOs to procure gas via these mechanisms.

We agree with the reference in the guideline that OBAs "shall eliminate the balancing risk for network users purely transporting gas through one or more balancing zones to another balancing zone". We believe that GB's current approach to dealing with steering differences does not place TSOs or Network Users with an undue balancing risk.