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Consultation on "The Entry Capacity Substitution Methodology Statement"

Dear Jan,

We welcome the opportunity to comment on the issues raised in this consultation document. This response reflects the views of RWE npower and the UK based business of RWE Trading GmbH.

We have previously expressed support for the concept of entry capacity substitution (and entry capacity transfers and trade) to the extent that this has the potential to improve efficiency and prevent unnecessary network investment. However, we do have sympathy with the view expressed at the last UNC Transmission Workstream¹ that there needs to be a wider, and more informed debate, about the trade off between potential savings in entry capacity investment and the potential increase in commodity costs that may result.

Whilst we recognise that National Grid's actions in this area are driven by anticipation of new licence conditions we believe that the piecemeal approach to reform of the entry capacity regime we have witnessed over the last six months has been detrimental, as it has created a climate of uncertainty and unease within the shipping community. As shippers are largely ignorant of the amount of, and potential for, entry capacity substitution/transfer that may realistically be possible in future, and were not party to decisions which led to the revised baselines, it is hardly surprising that concerns have been raised about the risk of gas being stranded and the consequent impact this could have on wholesale gas prices. These risks may or may not be real, but if they are it is likely that the costs involved will far exceed any efficiency benefits resulting from the combined application of the proposed entry capacity substitution, transfer and trades methodology statements in their current form.

That said, we have a number of concerns and uncertainties regarding the methodology statement which we have expressed below.

Paragraph 10a - We note that the obligations in respect of capacity substitution apply only where National Grid is proposing to release incremental capacity (i.e. on condition that the economic test has been met). This is consistent with the anticipated licence drafting and our current opinion is that this is

¹ 7th June 2007

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correct. However, we note the views expressed at the aforementioned Transmission Workstream that capacity substitution would be more efficient if applied to any incremental signal regardless of whether the economic test had been met, and believe that due consideration of this should be given as part of a wider debate.

Paragraph 16 - We are not convinced that considering the recipient ASEP with the lowest licence revenue driver first is the most appropriate way to substitute capacity where more than one incremental requirement has been signalled. National Grid claim that this will ensure that priority is given to the ASEP which required the least infrastructure to satisfy the incremental demand, which may be the case. However, without analysing the avoided investment cost created by capacity substitution for each ASEP it is not possible to be certain which would be the most efficient. This suggests capacity substitution should be determined following analysis of all incremental signals rather than being based on this ex ante modelling criteria.

Paragraph 20 - Whilst we accept National Grid's desire to avoid an incremental change in risk arising from capacity substitution we believe this should be qualified by reference to a "material incremental change in risk".

Paragraph 23 - We assume that the intent of this paragraph is that where it is only economic to make investment which exceeds the residual reinforcement requirement (because of set pipeline diameters for example), proposed capacity substitution will be re-adjusted back at donor terminals equivalent to the difference between the actual incremental capacity to be built and the and the residual requirement.

Paragraph 24 - Capping capacity substitution exchange rates between donor and recipient ASEPs seems sensible in order to avoid potential sterilisation of large quantities of capacity in future QSEC auctions. However, at this point we are not able to gauge what an appropriate cap might be. A similar effect to capping could be created by restricting capacity substitution only from donor ASEPs within the same zone (or adjacent zones), but in the absence of further understanding of the potential for substitution in the future it is difficult to say how practical or effective this might be.

We hope these views are helpful and if you wish to discuss them further please contact Charles Ruffell on 01793 893983 or myself on 01793 892068.

Yours sincerely,

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