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Dear John

Timing of 12 monthly Procurement Guidelines Review and subsequent Procurement Guidelines Report

Thank you for your letter dated 21 March 2005 in relation to the timing of the Procurement Guidelines (PGs) review and the associated PGs Report.

As you note in your letter, standard condition C16 (formerly special condition AA4) of the transmission licence requires National Grid Company plc (NGC) to carry out a 12 monthly review of its PGs and to publish subsequently a statement setting out the new version of its PGs. In line with standard condition C16.4, NGC is then required to prepare a report outlining the balancing services it has bought and acquired during the previous 12 months (excluding those procured through the Balancing Mechanism) within one month of the publication date of the new PGs.

Ofgem acknowledges that the current timing of the PGs review and PGs report presents some issues for NGC and potentially for market participants. While the annual PGs review will take place in time for the new version of the PGs to be published on 1st of May each year, Ofgem recognises that the period covered by the subsequent PG report would be inconsistent with the standard financial accounting year. In achieving NGC's stated objective of realigning the reporting period with the financial year, Ofgem also recognises the limitations imposed by standard licence conditions C16.3(a) and C16.4, which states that Ofgem can only increase (not decrease) the relevant timetables beyond 12 monthly intervals to such a period that the Gas and Electricity Markets Authority (the "Authority") may approve.

Ofgem agrees that NGC's proposal to delay the formal annual review of the PGs and the PGs report timetable by 11 months offers a pragmatic way in which to re-align these timetables with the financial year going forward, such that the annual review and the PGs report will be prepared at 12 monthly intervals in line with the financial year (unless otherwise directed by the Authority). Ofgem considers that NGC's commitment to conduct an informal PGs review and to

provide an equivalent to the formal PGs report in the coming months should, importantly, ensure that the benefits of the annual PGs review and the PGs report will be retained despite the delay in the formal timetable.

Therefore, the Authority approves NGC's request for an 11 month extension to the formal timetable for preparing a revised version of the PGs in accordance with standard condition C16.3(a) of the transmission licence. In doing so, Ofgem approves NGC's request that the next formal PGs Report will be prepared to cover the period 1 April 2005 to 31 March 2006.

For the purpose of ensuring wider transparency on this issue, Ofgem welcomes NGC's commitment to publish both its original letter and this letter on the NGC industry information website. Ofgem also welcomes NGC's commitment to publicise the rationale for this approach and details of the process to be followed at the next NGC Operational Forum.

Going forward, Ofgem is of the view that it may be appropriate to consider, in consultation with interested parties, potential revisions to standard condition C16 of the transmission licence in order to improve the operation of the provisions in the future. This would be based upon the experience gained by Ofgem, NGC and market participants during the application of these provisions to date. Ofgem also considers that it may be appropriate to review concurrently the equivalent provisions presently contained in special condition 27 of Transco's gas transporter licences. Ofgem would welcome the opportunity to discuss any potential revisions to these provisions with NGT and other market participants prior to initiating any consultation.

Please do not hesitate to contact me on the above number if you have any queries in relation to the issues raised in this letter or alternatively contact Simon Bradbury on 020 7901 7249.

Yours sincerely

Sonia Brown
Director, Markets

Signed on behalf of the Authority and authorised for that purpose by the Authority