

Bob Fletcher
Joint Office of Gas Transporters
31 Homer Road
Solihull
B91 3LT

Michael Lapper
Stakeholder Delivery
National Grid Distribution
Michael.lapper@nationalgrid.com
Direct tel +44 (0)7917 722287

www.nationalgrid.com

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Your Reference: UNC Modification Proposal 0563S

UNC Modification Proposal 0563S – Moving the NTS Optional Commodity Charge Formula into the UNC

Dear Bob,

Thank you for your invitation seeking representation with respect to the above Modification Proposal. I can confirm National Grid Gas Distribution does not support Modification Proposal 0563S.

Do you support or oppose implementation?

0563S – Oppose

Please summarise (in one paragraph) the key reason(s) for your support/opposition:

Whilst we sympathise with the need for appropriate governance around the methodology of the Optional Commodity Charge (OCC) within TPD Section Y of the UNC, our opposition is based upon the fundamental principle that it effectively places a fixed unit price into Network Code. Such a move would be entirely inconsistent with existing capacity and commodity based charging principles and would set a precedent that detracts from the ability of the Transporter to set its charges without subsequent approval from parties to the UNC, in addition to a number of other issues considered below.

We do not believe the proposed Modification should be self-governance, given that the modification impacts upon the commercial activities connected with the transportation of gas. If such a proposal were implemented, it would remove the ability for NTS to update the OCC formula which calculates the OCC unit rates to produce more cost reflective values. The impact is such that the full year-on-year movements in revenue (such as RPI Indexation) can only be apportioned to traditional entry and exit commodity users. Therefore, removing the ability of the NTS to alter the OCC unit rates has the potential to increase the level of cross-subsidy between users of the NTS. The options in GCD11 would potentially increase OCC revenue by c.£30m which is a step towards reducing the amount recovered through traditional commodity charges.

Within the recent consultation responses published by NTS, reference was made to the need for market certainty regarding timeliness of changes to the OCC rate. It is our view that implementation

of the Modification Proposal does not provide additional market certainty but conversely could add additional uncertainty given that it provides the ability for any parties to the UNC to propose changes the formula that calculates the unit rates by raising a subsequent modification. It is presently only possible for NTS to change the OCC unit rates (and indeed any other unit rate), and only twice in any charging year in either April or October in line with the UNC and Licence.

In addition to the points above, it is our view that the Modification Proposal does not better facilitate Relevant Objective (b) or (e), for the reasons that are set out further below, and that no reference has been made as to how subsequent modifications may detract from the ability of NTS to meet their licence obligations regarding charging notification periods given that any party to the UNC may be able to seek changes to OCC unit rates during the year.

Are there any new or additional issues that you believe should be recorded in the Modification Report:

We have no additional comments to those above.

Self Governance Statement:

We do not agree that the Modification Proposal should be subject to self-governance procedures. Although on the face of it the Proposal is a 'lift and shift' of the existing formula from the Transportation Statement into the UNC, the resulting move impacts the commercial activities connected with the transportation of gas conveyed through pipes. To be more specific, it impacts the ability of NTS to set appropriate commodity unit charges given that the OCC formula that calculates the OCC rates will effectively be placed directly into UNC at a fixed level. In setting the commodity rates to recover movements in their Maximum Allowed Revenue (MAR), NTS would be restricted and may be unable to make synchronised changes to the full suite of unit rates, the result of which would mean the full impact of movements in MAR would be subjected to the traditional Commodity Charge users as the OCC would be based on firm values and not updated in line with how other charges are recalculated. This could in our view, constitute a cross-subsidy, given that the underlying profile of movements in MAR can only be met by a portion of NTS commodity users and not others (OCC users).

Relevant Objectives:

The proposer states that the modification would further the following relevant objectives:

- b) That, so far as is consistent with sub-paragraph (a), the charging methodology properly takes account of developments in the transportation business
- e) Compliance with the Regulation and any relevant legally binding decisions of the European Commission and/or the Agency for the Co-operation of Energy Regulators

As alluded to previously, we have concerns that Modification 0563 does not meet the Relevant Objectives identified above.

The proposer argues that the Proposal is "consistent with good practices elsewhere in the UNC" in relation to Relevant Objective b). Whilst sympathetic to the call for governance around the OCC methodology, the Modification proposal has been unable to separate the methodology and the prevailing unit rate, and as the proposal stands it effectively places a unit rate into network code. This is entirely inconsistent with practice elsewhere in the UNC, and we believe it sets a precedent that compromises the ability of gas transporters to set its charges. Furthermore, we consider that the

Proposal would make the OCC less responsive to developments in the transportation business because any change would require subsequent UNC modification and limit the NTS ability to track unit rates to the influences that impact Maximum Allowed Revenue (e.g. inflation) in the usual way.

With regard to Relevant Objective e), Article 13 of Regulation 715/2009 states tariffs, or the methodologies used to calculate them "shall be transparent". It is our view that because unit rates are already required to be published in both Price Change Notifications and Annual Charging Statements, lifting and shifting a formula from one published document into another published document provides no additional transparency.

In addition, the proposer states the "modification will provide Ofgem a means of approving the Optional Commodity Charge, which is currently denied". It is our view that Ofgem (or its former entity Ofgas) has already approved the OCC in its decision letter dated 08th January 1998 following consultation paper PC9A and has furthermore provided guidance for the parameters in which updates to the tariff should be made, which have been met in the recent NTS consultation and subsequent proposed options. Placing the OCC formula into UNC as per the Modification Proposal detracts from the previous Decision enabling NTS to update the rate.

It is therefore our view that Modification 0563 does not better facilitate Relevant Objective (b) or (e).

Impacts and Costs:

We acknowledge that charging review GCD11 (Optional Commodity Charge) would be delayed by this modification.

Implementation:

We acknowledge the statement in the Draft Modification Report that the proposal should be implemented as soon as possible following approval.

Legal Text:

We believe that implementation of this Modification would give rise to the possibility of UNC parties raising future Modifications to change the Optional Commodity Charge formula (and subsequent unit rate) outside of the traditional NTS charging notification periods. This may subsequently impact the ability for NTS to meet their obligatory charging notice periods under Licence, and we feel this point has not been adequately addressed within the legal text of the current Draft Modification Report.

Is there anything further you wish to be taken into account?

No further points

We trust that this information will assist in the compilation of the Final Modification Report. Please contact me should you require any further information.

Yours sincerely,

Michael Lapper
Pricing Specialist
National Grid Distribution