

FUNDING, GOVERNANCE AND OWNERSHIP

KPMG / XOSERVE PAPER FOR POB / UNC FGO WORKGROUP ON POTENTIAL INVOICING APPROACHES

1. Introduction

This paper has been written following a request from the FGO charging and cost allocation workgroup on 5th April for a high level paper (to be circulated to POB and the UNC0565 workgroup) setting out the broad options around invoicing in order to facilitate an informed comparison and consideration of options.

2. Current invoicing arrangements

The majority of Xoserve's costs relate to the provision of ASA Core Services, which are funded by the GTs through allowed revenues as determined during RIIO-GD1 and RIIO-T1. Transportation charges from GTs to Shippers enable the GTs to recover these allowed revenues, but do not provide Shippers with separate visibility of Agency costs (except to the extent that these are disclosed in Ofgem's RIIO-GD1 and RIIO-T1 Final Proposals).

The table below sets out the prevailing regulatory and contractual framework that governs the provision of Agency Services and other bilateral services provided by Xoserve.

Contract		Services	Funding	Invoicing
Agency Services Agreement with GTs	No Framework contracts with Shippers	Core Services for which GTs have UNC responsibilities and regulatory licence obligations	Xoserve is funded by GTs through their allowed revenues set under periodic price control reviews <i>(If Agency charges exceed or out-perform GTs' allowed revenues, the commensurate risk or benefit contributes to GTs' overall performance under their RIIO arrangements).</i>	Xoserve raises invoices against the GTs for ASA Core Service Charges that are calculated by reference to Xoserve's approved annual budget and the ASA Charging Methodology. The GTs recover allowed revenues through transportation charges to Shippers.

Contract		Services	Funding	Invoicing
		User Pays Services for which GTs have UNC obligations	Charges are cost reflective and based on the utilisation of the service. For the purposes of GTs' price controls, the GTs' income for these services may be treated as excluded from price controlled revenue.	Xoserve raises invoices against the GTs for Code User Pays Service Charges. The GTs raise invoices against Shippers to recover Code User Pays Service Charges. Individual Shipper charges for Code User Pays Services are calculated in accordance with the Agency Charging Statement.
	Framework Contracts with Shippers	User Pays Services for which GTs do not have UNC obligations	Xoserve receives payment from service users.	Xoserve raises invoices against users of non-Code User Pays Services. Individual user charges for non-Code User Pays Services are calculated in accordance with the Agency Charging Statement
Other bilateral contractual arrangements		Services are individually tailored to meet specific customer requirements and are outside the scope of GTs' UNC responsibilities and regulatory licence obligations	Xoserve receives payment directly from those parties that request the services	Xoserve invoices the customer that requests the service in accordance with bilateral contract arrangements.

3. Ofgem decision letter, October 2013

Ofgem's FGO decision letter of October 2013¹ stated '*transparency will be further reinforced through...an invoicing approach which ensures users have sight of the costs they are exposed to.*' It went on to say that '*what needs to be achieved- transparency and accountability...can only be achieved if users are able to distinguish between transportation charges and charges for using the Central Service Provider.*'

Ofgem also indicated its concern that the invoicing approach adopted should not create undue additional costs.

The letter went on to set out the two options Ofgem considered could deliver the transparency and accountability required:

1. **Direct invoicing:** Xoserve would invoice and collect charges from all users directly, and would need to be protected from failure of one or more of its users to pay its invoice; or
2. **Indirect invoicing:** GTs would invoice and collect charges from shippers and transfer funds to Xoserve, similar to the way Code User Pays services are currently invoiced (albeit that Xoserve's contract for the provision of Code User Pays services is with the GTs).

4. Options

Preliminary discussions around the approach to invoicing have taken place under the FGO charging and cost allocation workgroup and at the Programme Overview Board (POB), although a detailed evaluation of options has not been undertaken.

Potential approaches to invoicing are set out in the table below, with an assessment of the potential implications of direct and indirect invoicing approaches using Ofgem's criteria of transparency, accountability and cost, and taking into account wider considerations.

It is assumed throughout that the UNC will have been modified with associated changes to the CDSP contracting model such that there is a mixture of:

- A direct contractual relationship between the CDSP and each CDS user for services that become the CDSP's direct responsibility to deliver; and
- Continuation of elements of the CDSP's services being delivered as GT Agency services, whereby the GTs are the contractual counter-party to Shippers (as defined by the UNC) and the CDSP is their agent or sub-contractor.

The 'Direct' and 'Indirect 1' options become operationally further apart as the extent of UNC modification that moves obligations from GTs to CDSP increases.

Invoicing Option	Description	Transparency	Accountability	Cost	Other
'Direct'	<p>The CDSP will be providing services either 'directly' or as 'GT Agency'.</p> <p>The CDSP raises CDS invoices against GTs for services provided in its capacity as GT Agency, and for services provided directly to GTs.</p> <p>The CDSP raises CDS invoices against Shippers, iGTs and non-Code parties for services provided directly to those parties.</p> <p>Dependent on Ofgem's GT funding policy decision, GTs recover from Shippers through transportation charges either:</p> <ul style="list-style-type: none"> • Allowed revenues for GT funding of CDSP; or • Under a 'pass through' arrangement, actual CDS charges as invoiced by the CDSP against the GTs. 	<p>Each CDS user has visibility of charges for the services that they contract to take from the CDSP.</p> <p>Unless GTs' charges separately identify the elements relating to CDSP, Shippers do not have visibility of their 'share' of GT funding of the CDSP.</p> <p>The requirement for such visibility needs to be explored further.</p> <p>Solutions could include a 'CDS charges' line item on transportation invoices from GTs to Shippers.</p>	<p>Direct invoicing would promote accountability on the part of each CDS user to fund the CDSP for the services that it takes.</p>	<p>The CDSP would incur additional cost in respect of the development and maintenance of processes to calculate charges for each CDS user.</p> <p>There may be a requirement for GT invoices to be amended to provide transparency of the CDSP-related elements.</p> <p>The required invoice flows already exist (or, for iGTs, will be in place prior to April 2017):</p> <ul style="list-style-type: none"> • Xoserve to GT • GT to Shipper • Xoserve to Shipper • Xoserve to iGT • Xoserve to non-Code party 	<p>Credit risk arrangements are directly between the CDSP and each CDS user.</p> <p>GTs are directly exposed in the event of Shipper failure to pay only in relation to the GT Agency element of the CDSP charges,</p> <p>The CDSP risk under a 'not for profit' model would presumably be syndicated across all CDS users.</p>
'Indirect 1'	<p>The CDSP will be providing services either 'directly' or as 'GT Agency'.</p> <p>The CDSP raises CDS invoices against GTs for services provided in its</p>	<p>GTs have visibility of charges for the services that they contract to take from the CDSP.</p> <p>Shippers do not have the same visibility</p>	<p>Indirect invoicing would not promote accountability on the part of non-GT CDS users to fund the CDSP for the services that it takes.</p>	<p>The CDSP would incur additional cost in respect of the development and maintenance of processes to calculate charges for each CDS</p>	<p>This model would mean that there would be an inconsistency between the contractual relationship between CDSP and non-GT CDS users and the</p>

Invoicing Option	Description	Transparency	Accountability	Cost	Other
	<p>capacity as GT Agency, and for services provided directly to GTs.</p> <p>The CDSP also raises CDS invoices against the GTs for services provided directly to Shippers and iGTs.</p> <p>The CDSP also raises CDS invoices against non-Code parties for services provided to those parties.</p> <p>Dependent on Ofgem's GT funding policy decision, GTs recover from Shippers through transportation charges either:</p> <ul style="list-style-type: none"> • Allowed revenues for GT funding of CDSP; or • Under a 'pass through' arrangement, actual CDS charges as invoiced by the CDSP against the GTs. <p>GTs also raise invoices against Shippers and iGTs to recover the amounts invoiced by the CDSP to the GTs for services provided to Shippers and iGTs.</p> <p>It is assumed that these invoices would be separate and distinct from GTs' own</p>	<p>unless GT invoices are backed up by supporting information (similar to prevailing Code User Pays arrangements).</p> <p>Shippers do not have visibility of their 'share' of GT funding of the CDSP.</p> <p>The requirement for such visibility needs to be explored further.</p> <p>Solutions could include a 'CDS charges' line item on transportation invoices from GTs to Shippers.</p>	<p>.</p>	<p>user.</p> <p>It is assumed that the CDSP would provide an invoice production service to the GTs to raise invoices to recover the amounts invoiced by the CDSP to the GTs for services provided by the CDSP directly to Shippers and iGTs.</p> <p>The required invoice flows already exist (or, for iGTs, will be in place prior to April 2017):</p> <ul style="list-style-type: none"> • Xoserve to GT • GT to Shipper • Xoserve to Shipper • Xoserve to iGT • Xoserve to non-Code party 	<p>flows of invoices and funds.</p> <p>GTs may be exposed to risk in the event of Shipper failure to pay.</p> <p>It is unclear how the CDSP would manage relationships with non-GT CDS users.</p>

Invoicing Option	Description	Transparency	Accountability	Cost	Other
	transportation charges from GTs to Shippers.				
'Indirect 2'	As 'Indirect 1', except that the GT recovery of amounts invoiced by the CDSP to the GTs for services provided to Shippers is included within transportation charges	Shippers will have no visibility of the extent to which they are funding the CDSP	Indirect invoicing would not promote accountability on the part of non-GT CDS users to fund the CDSP for the services that it takes.	Invoicing flows are simplified, i.e., the existing Code User Pays style arrangements lapse	GTs may be exposed to risk in the event of Shipper failure to pay.