CODE MODIFICATION PROPOSAL No 0285
"Use it or lose it"(UIOLI) Interruptible Capacity only to be released when firm entry capacity is at least 90% sold out
Version 1.0

Date: 10/03/2010

Proposed Implementation Date: 01/10/2010

Urgency: Non Urgent

1 The Modification Proposal

a) Nature and Purpose of this Proposal

Where capitalised words and phrases are used within this Modification Proposal, those words and phrases shall usually have the meaning given within the Uniform Network Code (unless they are otherwise defined in this Modification Proposal). Key UNC defined terms used in this Modification Proposal are highlighted by an asterisk (*) when first used. This Modification Proposal, as with all Modification Proposals, should be read in conjunction with the prevailing Uniform Network Code* (UNC).*

For clarification this Modification Proposal* covers the release of daily average unutilised firm capacity* known as Use It Or Lose It (UIOLI) Interruptible capacity (as detailed in section B2.5.11 of the UNC TPD)

Background

TO NTS Entry Commodity Charges* have increased year on year. This is due to growing under-recovery of TO Entry Capacity Revenue as a result, in part, of the large quantities of zero reserve priced capacity.

A reserve price* is set for entry capacity released via auctions i.e. Quarterly NTS Entry Capacity* (QSEC), Monthly NTS Entry Capacity* via the annual and rolling monthly* (AMSEC & RMTTSEC) auctions, and Daily NTS Entry Capacity* via the day-ahead and within-day (DADSEC & WDSEC) auctions. A 33% discount is applied to the day-ahead daily firm NTS Entry Capacity auction reserve prices and the within-day firm NTS Entry Capacity auction has a zero reserve price (100% discount) in compliance with the NTS Licence obligation to hold at least one clearing auction for each Aggregate System Entry Point * (ASEP) for each day.

Currently, Daily Interruptible NTS Entry Capacity* (DISEC) is released with a zero reserve price at the day ahead stage and any resulting revenue is treated as SO revenue in accordance with the NTS Licence. This may be a factor in how much NTS Entry Capacity* Shipper Users* procure via the longer term auctions. The under recovery of TO capacity revenues via the NTS Entry Capacity Charges* impacts the TO Commodity Charge*. Any shortfall in the recovery of revenues by National Grid NTS* through entry charges is picked up through the TO Commodity Charge which is paid by all Shipper Users.

The Interruptible quantity to be made available is currently defined as the daily average unutilised firm capacity, referred to as the UIOLI quantity, plus a discretionary amount of NTS Entry Capacity which National Grid NTS determines and is currently released at zero price. National Grid NTS is concerned that this interruptible capacity can be released while firm capacity remains unsold, potentially making the interruptible capacity firm (if the unsold firm capacity is not procured) due to the low likelihood of curtailment.

Industry concern about the increased TO Entry Commodity Charges led to National Grid NTS launching a fundamental review of the entry charging principles through the formation of the industry entry charging review group (ECRG).

A major priority identified by the review group was to reduce the significant quantities of NTS Entry Capacity which are auctioned at zero reserve price. This could be achieved by the removal of the firm NTS Entry Capacity discounts, and by amending the circumstances under which Daily Interruptible NTS Entry Capacity is released, hence reducing the circumstances under which Interruptible NTS Entry capacity is made available.

The removal of the firm capacity discounts will be covered by a further UNC Modification Proposal and by an NTS Charging Methodology Proposal.

Proposal

National Grid NTS proposes that National Grid NTS only releases UIOLI interruptible Capacity at an Aggregate System Entry Point* (ASEP) when at least 90% of firm entry capacity (that National Grid NTS is obliged to release in accordance with Licence Special Condition C8D(C)) has been sold out at the relevant ASEP prior to the daily auctions. The sold out quantity would be established prior to daily auctions.

This would be effective from implementation date of 01 October 2010.

Placing a limit on the circumstances under which Daily Interruptible NTS Entry Capacity is released would reduce the quantities of entry capacity auctioned at zero reserve price. The 90% threshold is consistent with the proportion of obligated capacity made available in the QSEC auctions and is designed to avoid the circumstances when a small quantity of firm capacity remains unsold which would have resulted in no interruptible capacity being released had the threshold been set at 100%.

For the avoidance of doubt this proposal does not affect the ability of National Grid NTS to release discretionary amounts of Daily Interruptible NTS Entry Capacity. This proposal does not place any restrictions on the circumstances when the discretionary amount might be released to avoid a potential scenario where the release of such quantities might have a positive impact on security of supply.

For the avoidance of doubt, on the day the release of Available Daily Capacity* (section B2.4.13(a) of the UNC) would be assessed throughout the Gas Day, on an hourly basis, via the firm daily allocation process. The Available Daily Capacity (other than the element of any additional Daily NTS Entry Capacity which National Grid NTS may choose to make available in its sole discretion) would be reduced within Day to take into account the implied hourly rate for the remainder of the Day.

For the avoidance of doubt, the zero reserve price for Daily Interruptible NTS Entry Capacity would still apply.

Transmission Workstream Discussion

The following has been raised at the Transmission Workstream and is included for information only.

Consideration has been given to the possible inclusion of the daily quantities in the sold out quantity. Due to the close out of the Day Ahead Auctions (DADSEC) at 0200 at D-1 there is insufficient time remaining, prior to the 0600 close of day, to hold the interruptible auction (DISEC) and so it would not be possible to include the full DADSEC allocation within the calculation of the at least 90% sold figure. An alternative of including the first DADSEC allocation only (2pm) has also been considered but there is again insufficient time prior to the 3pm allocation of DISEC.

An alternative to the restriction of the release of UIOLI was discussed at the Entry Charging Review meetings. This would be to continue to release the UIOLI as now but to put a reserve price on the UIOLI above the present zero value. This would not require a UNC Modification but a Charging Consultation instead. National Grid NTS would be happy to progress this as an alternative if Users consider it a more appropriate solution.

b) Justification for Urgency and recommendation on the procedure and timetable to be followed (if applicable)

Urgent Procedures are not requested

c) Recommendation on whether this Proposal should proceed to the review procedures, the Development Phase, the Consultation Phase or be referred to a Workstream for discussion.

National Grid NTS will discuss this issue at the February and March Transmission Workstreams and subsequently submit this Modification Proposal to the March Panel. It is proposed that this proposal now proceeds to the Consultation Phase with a view to submitting the Final Modification Report in May.

2 User Pays

a) Classification of the Proposal as User Pays or not and justification for classification

No changes to Xoserve systems or processes have been identified and therefore the proposal is not a User Pays proposal.

b) Identification of Users, proposed split of the recovery between Gas Transporters and Users for User Pays costs and justification

N/A

c) Proposed charge(s) for application of Users Pays charges to Shippers

N/A

d) Proposed charge for inclusion in ACS – to be completed upon receipt of cost estimate from xoserve

N/A

3 Extent to which implementation of this Modification Proposal would better facilitate the achievement (for the purposes of each Transporter's Licence) of the Relevant Objectives

- National Grid NTS believes that in respect of Standard Special Condition A11 (a), the efficient and economic operation of the pipeline system, this proposal would encourage longer term bookings of entry capacity by removing the price incentive to buy later and therefore be consistent with the economic and efficient development of the system.

- National Grid NTS believes that in respect of Standard Special Condition A11 (d) so far is consistent with sub-paragraphs (a) to (c) the securing of effective competition (i) between relevant shippers, this proposal would reduce the large quantities of zero priced Interruptible NTS Entry Capacity being released, therefore possibly encouraging Shippers to purchase longer term capacity, encouraging further utilization of the secondary capacity market, and not be so reliant on interruptible capacity when firm is available. This proposal is part of a suite of proposals that are seeking to reduce the level of the TO Entry Commodity charge and hence seeking to avoid potential cross subsidies which may arise when this commodity charge represents a significant proportion of TO entry revenue. National Grid believes that removing potential cross subsidies is consistent with this objective.

- National Grid NTS believes that in respect of Standard Special Condition A11 (c) so far as is consistent with sub-paragraphs (a) and (b), the efficient discharge of the licensee's obligations under this licence, this proposal would better facilitate the charging methodology objectives as set out in Standard Special Condition A5 5 including cost reflectivity, promoting efficiency and avoiding undue preference. For more detail see 'Advantages' in section 11 below.

4 The implications of implementing this Modification Proposal on security of supply, operation of the Total System and industry fragmentation

National Grid NTS believes this proposal would benefit operation of the Total System* with the GB as an attractive destination for gas through increased regulatory and charging certainty.

5 The implications for Transporters and each Transporter of implementing this Modification Proposal, including:

a) The implications for operation of the System:

National Grid NTS believes that the operation of the system* would not be adversely affected. This Proposal could prove beneficial to the operation of the system as more capacity could be booked long term thereby creating greater certainty.

b) The development and capital cost and operating cost implications:

No cost implications have been identified

c) Whether it is appropriate to recover all or any of the costs and, if so, a proposal for the most appropriate way for these costs to be recovered:

N/A.

d) The consequence (if any) on the level of contractual risk of each Transporter under the Uniform Network Code of the Individual Network Codes proposed to be modified by this Modification Proposal

No such consequences have been identified.

6 The extent to which the implementation is required to enable each Transporter to facilitate compliance with a safety notice from the Health and Safety Executive pursuant to Standard Condition A11 (14) (Transporters Only)

Not applicable

7 The development implications and other implications for the UK Link System of the Transporter, related computer systems of each Transporter and related computer systems of Users

No changes to UK Link, NTS systems or User systems have been identified

8 The implications for Users of implementing the Modification Proposal, including:

a) The administrative and operational implications (including impact upon manual processes and procedures)

National Grid NTS believes there are minor administrative or operational Implications.

b) The development and capital cost and operating cost implications

National Grid NTS believes there are no development, capital or operating cost implications.

c) The consequence (if any) on the level of contractual risk of Users under the Uniform Network Code of the Individual Network Codes proposed to be modified by this Modification Proposal

No consequences on the level of contractual risk have been identified.

9 The implications of the implementation for other relevant persons (including, but without limitation, Users, Connected System Operators, Consumers, Terminal Operators, Storage Operators, Suppliers and producers and, to the extent not so otherwise addressed, any Non-Code Party)

No consequences on the implementation for other relevant persons have been identified.

10 Consequences on the legislative and regulatory obligations and contractual relationships of the Transporters

National Grid NTS has not identified any such consequences.

11 Analysis of any advantages or disadvantages of implementation of the Modification Proposal not otherwise identified in paragraphs 2 to 10 above

Advantages

National Grid NTS believes that the benefits of this proposal are that the Proposal:

- Should increase the proportion of NTS TO target entry revenue recovered through entry capacity charges. The forward looking analysis suggests that, with the reduction of quantities of Daily NTS Interruptible Capacity made available combined with the removal of firm Daily NTS Entry Capacity reserve price discounts, entry capacity revenue will increase as more firm capacity is procured other than at a zero price. This is a necessary first step en route to achieving the maximum proportion of NTS TO target entry revenue, which can be recovered through entry capacity charges.

- Provides a more apt redistribution of charges. The TO Entry Commodity Charge was designed as a correction mechanism for under recovery of allowed revenue from auctions. Using this charge to collect a large amount of under-recovered income from entry capacity auctions may currently result in a redistribution of charges from Users, acquiring Entry Capacity at a discounted rate, to those Users that have previously paid a "full" rate for capacity.

- Promotes secondary trading. The availability of capacity with zero reserve prices may be a factor that inhibits entry capacity trading at ASEPs when there is unsold Obligated NTS Entry capacity. Some Users may have surplus capacity holdings and others are seeking short-term rights but the value of sold capacity is minimised by the existence of zero priced capacity. Removal of discounts should promote the secondary market in entry capacity.

- Should reduce the amount of Interruptible NTS Entry Capacity that is effectively firm NTS Entry Capacity*, as a result of firm capacity remaining unsold at the relevant ASEP.

- Could prevent cross subsidies between Shippers who buy Interruptible NTS Entry Capacity (short term) rather than firm (long term). Shippers have an incentive to purchase Interruptible NTS Entry Capacity rather than QSEC or AMSEC. This could mean that short-term capacity buyers are having their costs paid by Shippers who have previously paid the longer-term rate for capacity creating cross subsidies between Shippers who buy firm rather than interruptible.

- Should increase the proportion of revenue recovered through capacity, as opposed to commodity, charges through increasing the incentive to make longer-term bookings (e.g. QSEC), which might improve price certainty.

- When capacity becomes constrained at an entry point, where previously there was a perception of surplus capacity, and where long-term signals for incremental capacity investment have not been received from QSEC auctions, high and volatile prices and more frequent scale back of Interruptible NTS Entry Capacity may be observed until Incremental NTS Entry Capacity is signalled and provided.

Disadvantages

- Users may see a decrease in the UIOLI quantities available and this may be viewed as limiting their ability to access entry capacity; however, the UIOLI quantities would continue to be released when firm capacity was close to selling out.

- A change to the release of the UIOLI quantities will not necessarily remove the shortfall between TO target entry revenue and TO entry capacity revenue (depending on shipper booking behaviour); however, it is a necessary step prior to further options being developed, as required, including price multipliers and/or further changes to products.

- The "daily average unutilised firm capacity", referred to as the 'use it or lose it' UIOLI quantity, was designed as an anti hoarding measure. The scenario where a small quantity of firm NTS Entry Capacity remains unsold, and precludes the release of the UIOLI quantity where the UIOLI quantity implies unutilised capacity, would need to be avoided; however, this proposal seeks to overcome this issue by releasing the UIOLI quantity when at least 90% of obligated capacity has sold out rather than 100%.

12 Summary of representations received as a result of consultation by the Proposer (to the extent that the import of those representations are not reflected elsewhere in this Proposal)

Not applicable.

13 Detail of all other representations received and considered by the Proposer

Not applicable.

14 Any other matter the Proposer considers needs to be addressed

Not applicable.

15 Recommendations on the time scale for the implementation of the whole or any part of this Modification Proposal

Draft Proposal discussed at Transmission Workstream	04 Feb 2010
Draft Proposal further discussed at Transmission Workstream	04 Mar 2010
Proposal submitted to Mod Panel	18 Mar 2010
Closeout for representations	13 Apr 2010
FMR produced (provided to Ofgem in parallel with Pricing Consultation GCM19)	22 Apr 2010
Modification Panel decide upon recommendation	20 May 2010
FMR submitted to Ofgem	May 2010
Proposed implementation date	01 Oct 2010

16 Comments on Suggested Text

To be advised

17 Suggested Text

To be advised

Code Concerned, sections and paragraphs

Uniform Network Code

Transportation Principal Document

Section(s) B – System Use and Capacity

Proposer's Representative

Debra Hawkin (National Grid NTS)

Proposer

Debra Hawkin (National Grid NTS)