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To: Joint Office of Gas Transporters,
relevant Gas Transporters, Shippers and other interested partiers

Consultation response to UNC Mod 636, 636A, 636B, 636C and 636D 'Updating the parameters for the NTS Optional Commodity Charge'

GM&T is the UK registered wholly-owned subsidiary of Gazprom Group ("Gazprom"), responsible for the optimisation of Gazprom's energy commodity assets through GM&T's marketing and trading network.
GM&T Ltd is active as a trader and marketer of gas at various points in Europe, and especially in the UK. Therefore, it has a keen interest in maintaining transparent and cost-reflective transmission charges that ensure the most efficient operation of the gas market in the UK.

In light of Mod 621 that includes a review of the Optional Commodity Charge (OCC), we do not believe change is required at this time. The current timing of Mod 636 and its alternate proposals is not sensible, however we recognise that the industry is going forward with an update to the parameters of the OCC regardless. We are of the opinion that robust and cost reflective transmission charges cannot be maintained if isolated elements are changed materially .Please find below our responses to the consultation questions as outlined on the Joint Office website.

Indication of support or opposition for implementation of the UNC Mod 636 and its alternate proposals

Proposal	Support/oppose
0636	Oppose
0636A	Oppose
0636B	Qualified support
0636C	Oppose
0636D	Support – our preference

1. As the industry seeks to make comprehensive changes to UK gas market design, proper consideration is needed for IPs given the significance and severity of the proposals being discussed under Mod 621. IPs require an enduring solution that recognises the European Tariff Network Code requirements and avoids short-term disruption. Therefore close consideration must be given to the impacts on cross border trade, market liquidity and security of supply of the neighbouring countries (including Ireland, which is highly dependent on the gas exports from GB). The impact analysis for 636 fails to quantify these risks, which should be deemed as fundamental, when considering such a change in the OCC.

2. National Grid, Ofgem and industry stakeholders are hard at work consulting and preparing for a new charging methodology that will take effect from October 2019. The requirement to add further tension to current activities seems unnecessary at this time.

3. Although we do not really believe that this is the right time to implement isolated change, we believe our proposal 0636D is the most pragmatic solution. This has to be the case as it seeks to minimise the erosion of cross border flows. We are concerned that proposals 636, 636A, 636C do not give sufficient consideration to the impact they will have at UK borders.

4. We must also consider that the consultation process for these proposals is taking place during a crucial time of transition ahead of the new gas year, where supply contracts are being renewed and concluded. Typically the standard provisions within gas contracts that allow for re-negotiation or termination in the case of fundamental changes in the regulatory environment, require notice of between 6-12 months. With this in mind, we believe our proposal Mod 0636D is the least disruptive to these commercial activities. Due to the sensitivity of such arrangements, they have not been quantified in the impact analysis. We would like to emphasise that the 636 Workgroup Report is designed to be high level and does not sufficiently assess and validate the impacts on industrial and commercial customers, in addition to UKCS producers that are striving to maximise the economic recovery of remaining reserves, in line with the government’s MER strategy. An unnecessary change in the OCC in line with mods 636, 636A or 636C could erode the value of qualifying UKCS gas supply contracts.

5. Consideration should also be given to the role of gas in power generation and the impacts of the proposals on power prices in the UK and consequently domestic customers.

The next section of our representation outlines our assessment of each mod proposal against the relevant code and charging methodology objectives.

<u>**GAZPROM MARKETING & TRADING ASSESSMENT OF EACH MODIFICATION IN FACILIATING THE RELEVANT CHARGING OBJECTIVES**</u>

Relevant Objective A) The charging methodology results in charges which reflect the costs incurred by the licensee in its transportation business

636 and 636C – Negative

These proposals extend the pipeline portfolio to include larger pipeline sizes as set out in GCD11 Option 1. In our view there is a lack of evidence that private pipeline systems are built using the larger pipeline diameters and therefore their inclusion does not accurately replicate the cost of construction (this being the principle behind the application of an OCC). Pipeline construction should be recognised as a sunk cost, therefore in our view it's erroneous to refer to updated pipeline and steel costs. It's highly unlikely the investment economics at the time of construction would have been used in this way.

The M factor proposed in these mods is not cost reflective. Its method of deriving the future load factor is deficient as it assumes that historical flows are a sound indicator of future flows. This is incorrect particularly in the example of power generation demand, which varies depending on spark spreads derived in the power market. National Grid, for example, does not make CAPEX decisions purely based on annual flow changes. Instead they invest on the basis of operational *peak* flow expectations, which will allow flows to be accommodated at all levels of demand.

636A - Negative

The imposition of an arbitrary distance cap to the OCC formula is not borne from cost reflective principles.

636B – Positive

This proposal is consistent with GCD11 Option 2 and also Mod 621 and a number of its alternatives (noting that these proposals include a distance cap). The use of RPI to update costs, coupled with the inclusion of the methodology in the UNC, is an appropriate method for ensuring that the OCC remains cost reflective. We believe these proposals are more cost reflective than Mod 636 as it recognises that investments which have been made are correctly cost escalated and not exposed to pipeline costs that are not relevant to existing infrastructure.

636D - Positive

The same arguments regarding cost reflectivity apply to this proposal as stated for Mod 636B. Additionally, this proposal recognises the limitations imposed on tariff changes by the EU Tariff Code and adopts RPI escalation on those non-IP routes which the UK is able to apply.

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Relevant Objective B) The charging methodology properly takes account of developments in the transportation business

Mod 636 – Negative
As stated above, we believe this proposal is not cost reflective, unstable and will not generate charges that reflect the economics of building and operating private pipelines. Its application could result in inefficiencies in investment decisions and use of the NTS.

Mod 636A – Negative
For same reasons to those set out for Mod 636.

Mod 636B – Positive
This proposal gives consideration to Mod 0621 and therefore takes account of the evolving transportation business.

Mod 636C – Negative
This proposal incorrectly applies OCC to entry and exit points at IPs. As outlined in UNC TPD Section Y, paragraph 3.5 the OCC service is intended to limit charges relating to a direct route between a nominated exit point and a selected entry point, and not the inverse.

Mod 636D – Positive
These proposals furthers the relevant objective as it protects the OCC methodology applicable at cross border points until further analysis is made in 621.

Relevant Objective C) The charging methodology facilitates effective competition between gas shippers and between gas suppliers

Mod 636,636A and 636C – Negative
These proposals are not cost reflective and do not effectively promote use of the NTS, as described above. On this basis, we do not believe it promotes effective competition.

Mod 636B – Positive
This proposal is cost reflective and therefore ensure that charges paid by all Users are equitable. In this case, competition is facilitated, however amending the application of the OCC at IPs at this time may cause further disruption to IPs in the transition to the enduring regime under consideration in Mod 621.

Mod 636D – Positive
This proposal is cost reflective for the same reasons at 636B however furthers the relevant objective by facilitating continuous trade as cross border points.

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Final remarks

The impact analysis misses key information on the secondary impacts such as, industrial and commercial customers, power prices, cross border flows and neighbouring markets such as Ireland. Given the materiality of these impacts, we suggest that Ofgem conducts an Impact Assessment prior to making a decision on these proposal.

In the instance that Ofgem has to consent to a shorter notice period for publication of 2018/19 Optional Commodity Charge, we hope that consideration will be given to the commercial deadlines that typically occur ahead of the new gas year (1st October 2018) as described above. We do not believe it is the right time for this change but if industry disagrees, we believe our proposal Mod 636D is the least disruptive solution to current activities in the gas industry.

We hope the comments above prove helpful. Please do not hesitate to contact me on +44 (0)20 7756 9732 or at sinead.obeng@gazprom-mt.com if you wish to discuss any aspect of our response in further detail.

Yours faithfully,

Sinead Obeng

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