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|------------------------|---|----------------------|-------------------------------------|
| Modification proposal: | <b>Uniform Network Code (UNC) 625: Extension of 4 months to 10 months to transfer non-mandatory sites from Class 1 (UNC625)</b> |                      |                                     |
| Decision:              | The Authority <sup>1</sup> directs this modification be made <sup>2</sup>   |                      |                                     |
| Target audience:       | The Joint Office, Parties to the UNC and other interested parties   |                      |                                     |
| Date of publication:   | 24 November 2017  | Implementation Date: | To be confirmed by the Joint Office |

## Background to the modification proposals

The UNC requires any supply point with an Annual Quantity (AQ)<sup>3</sup> above 58,600,000 kWh to be Daily Metered (DM). The UNC has also traditionally allowed for Larger Supply Points<sup>4</sup> below this threshold to be DM on a voluntary basis (DMV). In both cases the meter reading services are provided by the relevant Gas Transporter (GT)<sup>5</sup>, via their agent the DM service provider (DMSP), utilising equipment owned or leased by the GT.

UNC224<sup>6</sup> was implemented in November 2010 in order to allow shippers to competitively procure their own reads and/or utilise their own Automated Meter Reading (AMR) equipment. Supply Points which utilised competitively procured DM services were to be classified as DM elective (DME) supply points, though in practice there was zero take up of this option.

Subsequent to the implementation of UNC224, UNC345<sup>7</sup> was raised in order to phase out DMV by the end of 2012. It was argued that it was no longer necessary or efficient for the GTs continue providing DM reads for supply points which did not meet the mandatory DM requirements. We agreed that it would be more efficient for non-mandatory DM services to be procured competitively rather than through a regulated offering and therefore directed the implementation of UNC345.

Due to concerns that DME did not provide an effective substitute for DMV, UNC441<sup>8</sup> then deferred the date by which DMV was to be phased out, to coincide with the Project Nexus Implementation Date (PNID). At PNID, any existing DMV were expected to be registered against one of the available settlement products, with product 2 being the closest comparable service.

Subsequently, some shippers expressed concern that withdrawing the DMV service at the same time as the implementation of Project Nexus would not facilitate a seamless transition between DMV and product 2, given the need to carry out site visits in order to remove GT DRE and/or reconfigure the AMR installation. This created a risk that the existing DMV supply points would default to a Non Daily Metered (NDM) service, which

<sup>1</sup> References to the "Authority", "Ofgem", "we" and "our" are used interchangeably in this document. The Authority refers to GEMA, the Gas and Electricity Markets Authority. The Office of Gas and Electricity Markets (Ofgem) supports GEMA in its day to day work. This decision is made by or on behalf of GEMA.

<sup>2</sup> This document is notice of the reasons for this decision as required by section 38A of the Gas Act 1986.

<sup>3</sup> The Annual Quantity (AQ) is an estimate of the quantity of gas that will be consumed in the relevant Gas Year, which commences 1 October.

<sup>4</sup> A Larger Supply Point (LSP) has an AQ greater than 73,200kWh

<sup>5</sup> UNC Section M, paragraph 4.1.4

<sup>6</sup> UNC224: ['Facilitating the use of AMR in the Daily Metered Elective Regime'](#)

<sup>7</sup> UNC345: ['Removal of Daily Metered voluntary regime'](#)

<sup>8</sup> UNC441: ['Continuation of Daily Metered \(Voluntary\) service until the implementation of Project Nexus'](#)

was considered to be a retrograde step. UNC514<sup>9</sup> extended the GT provision of the DMV service for a further six months beyond the implementation of Project Nexus. This meant such supply points are deemed Class 1 (i.e. registered against settlement product 1) for an interim period, notwithstanding they do not meet the Class 1 criteria.

### **The modification proposal**

UNC625 proposes a further extension of the DMV service, allowing any non-mandatory DM supply points to remain in settlement Class 1 for a further 4 months.

The consequence of not doing so is that shippers will be expected to re-classify the former DMV supply points, utilising any of settlement products 2 – 4 by the end of November 2017, being the end of the post-PNID interim period identified in UNC514. In the event that the shipper has failed to reclassify any supply point by 30 November 2017, it will default to being a Class 4 supply point.

### **UNC Panel<sup>10</sup> recommendation**

At its meeting of 9 November 2017 UNC Panel voted by a majority to recommend the rejection of UNC625.

### **Our decision**

We have considered the issues raised within the Final Modification Report (FMR) dated 9 November 2017 and the consultation responses published on the Joint Office website and summarised within the FMR<sup>11</sup>. We have concluded that:

- implementation of the modification proposal will better facilitate the achievement of the relevant objectives of the UNC;<sup>12</sup> and
- directing that the modification be made is consistent with our principal objective and statutory duties.<sup>13</sup>

### **Reasons for our decision**

We note that the views of the eight respondents to the Joint Office's consultation were balanced, with three respondents being in support of the proposal, three opposed and the remaining two offering comments only. Respondents in favour of UNC625 suggested that its implementation would further relevant objective (d), whilst two of those opposed considered it would be detrimental to that objective. The final respondent opposed considered that it would be detrimental to relevant objective (f). We agree that relevant objectives (d) and (f) are impacted by UNC625.

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<sup>9</sup> UNC514: '[Extending the Daily Metered 'voluntary' service to Project Nexus Implementation Date plus six months'](#)

<sup>10</sup>The UNC Panel is established and constituted from time to time pursuant to and in accordance with the UNC Modification Rules.

<sup>11</sup> UNC modification proposals, modification reports and representations can be viewed on the Joint Office of Gas Transporters website at [www.gasgovernance.com](http://www.gasgovernance.com)

<sup>12</sup> As set out in Standard Special Condition A11(1) of the Gas Transporters Licence, available at: <https://epr.ofgem.gov.uk/Content/Documents/Standard%20Special%20Condition%20-%20PART%20A%20Consolidated%20-%20Current%20Version.pdf>

<sup>13</sup> The Authority's statutory duties are wider than matters which the Panel must take into consideration and are detailed mainly in the Gas Act 1986 as amended.

Relevant objective (d): the securing of effective competition between relevant shippers and suppliers

Our decision to accept UNC345 which sought to phase out DMV, was on the basis that competitive metering services are likely to provide greater incentives to reduce cost and to innovate than the regulated DMV service. Therefore, when accepting the subsequent modifications to delay the phasing out of the DMV service we acknowledged the trade-off between the impacts on competition and the practical issues involved in the transition. Whilst it was disappointing that shippers did not utilise that DME service, we acknowledge that circumstances changed and the imminent prospect of being able to utilise settlement product 2 superseded any immediate concerns with the DMV service. The subsequent delays to Project Nexus and the availability of settlement product 2 were not at that time foreseeable.

In accepting UNC514 we agreed that allowing supply points below the mandatory DM threshold to nonetheless remain in Class 1 for an interim period of 6 months would mitigate some of the practical problems posed by this transition. This was not simply to provide a softer landing for shippers, but recognised the potential impacts on the accuracy of cost allocation and customer service if hitherto DM sites became NDM en-masse. It is therefore disappointing that despite this additional period of grace, and having had several years notice of these changes, the same arguments are again being put to us. We do not dispute that these arguments remain valid, but consider that gas shippers have now had more than sufficient notice and have the ability to manage these risks.

We are also very conscious that there are now charging implications associated with the classification of supply points that did not exist when previous extensions to the DMV service were agreed. In particular, the classification of a supply point into one of the four settlement products now determines the amount of unidentified gas (UIG) that will be allocated to the supply point. Supply points within Class 1, which was designed to contain only those commercial sites with consumption above the mandatory DM threshold, have a lower weighted UIG applicable to them than other Classes. Indeed, before 1 October 2017, such DM sites attracted no UIG allocation at all.

We agree with those respondents who suggested that the ongoing classification of these DMV supply points as Class 1 is not fully cost reflective, and risks acting as a perverse incentive on relevant shippers taking the necessary action to migrate those supply points onto an appropriate settlement product. In the long-term, we are clear that these sites must be re-classified.

However, as we set out in our recent open letter<sup>14</sup>, the levels of UIG resulting from the new business rules have been of a higher volume and more volatile than most shippers expected. We are concerned that as things stand, the current rules could result in a large proportion of these sites reverting to Class 4. As a Class 4 Supply Point, the UNC would restrict the submission of meter reads to no more than one every 25 days<sup>15</sup>, even though daily reads may still be available from those sites. While there would be incentives for shippers to reclassify these sites to other product classes, in the meantime the unavailability of these daily reads may have an adverse impact on settlement accuracy. To the extent that some gas shippers may look to pass this additional risk,

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<sup>14</sup> Ofgem open letter on UIG 8 November 2017 – See: [www.ofgem.gov.uk/system/files/docs/2017/11/uig\\_letter.pdf](http://www.ofgem.gov.uk/system/files/docs/2017/11/uig_letter.pdf)

<sup>15</sup> UNC Section M 5.9.2

however temporary, through to their customers in the form of a tariff premium, we consider that there may be a detrimental impact on consumers.

We therefore consider there is a trade-off between achieving our objective to ensure more cost reflective gas settlement – including UIG – and mitigating the transitional risk as industry adjusts to and refines the new gas settlement business rules introduced on 1 June.

On balance, we consider that implementing UNC625 would better facilitate relevant objective (d).

However, we would also welcome consideration by the Performance Assurance Committee (PAC) of whether supply points should remain registered to the shippers chosen settlement product in instances where they have failed to meet the requirements of that product for a prolonged period. For instance, we are aware that there are a number of Class 1 sites (made up of both mandatory DM and DMV) that are still failing to submit meter readings, almost six months after PNID. This undermines the basis on which those supply points receive a lower weighting of UIG. Whilst we welcome the ongoing focus on resolving the issues that are preventing meter reads from these sites being entered into settlement, it may in due course be appropriate to put a hard stop to this asymmetric arrangement. This could take the form of a reasonable deadline by which issues must be resolved, with the possible consequence of the supply point being disqualified, albeit temporarily, from a product classification for which they are not fulfilling the associated requirements.

*Relevant objective (f): the promotion of efficiency in the implementation and administration of the UNC*

Some respondents considered that sufficient time has been allowed for the planning and undertaking of the transition from DMV to one of the permitted settlement products. They raised concerns that given the history of delay in the removal of DMV, there was no certainty that the new deadline would be heeded and that a further modification could be raised. We note that one of the respondents in favour of UNC625 suggested that a later deadline of 31 May 2018 may be appropriate in order to extend beyond the ratchet period. Whilst it is speculative to suggest that a further extension may be sought, suggestions of a later alternative date together with the history of these DMV service extensions may allude to there not being a universally convenient time to withdraw this service and that a further delay is at least possible.

Whilst we recognise the attention that shippers have had to give to resolving DM read validation issues since PNID, it is not clear to us that this activity should in any way have precluded work on the re-registration of supply points into a permitted settlement product, or mitigates their failure to have done so. We therefore agree with the comments that there has been adequate notice for the planning and undertaking of the transition from DMV. We also understand that both the GTs and DM Service Providers would be open to a continuation - on commercial terms - of the provision of DM equipment at the existing DMV sites. However, at this stage it may be difficult if not impossible for all such supply points to be re-classified in an orderly manner before the expiration of the regulated service. We are not aware of any legitimate reason why this could not be achieved by the revised 1 April 2018 date proposed in UNC625.

We are also concerned that continually extending deadlines for actions that are hard-wired into the UNC will erode certainty and market parties' confidence in the

arrangements. As such, we recognise that the implementation of UNC625 may be detrimental to the effective implementation and administration of the UNC and as such, would be inconsistent with relevant objective (f). However, under the current circumstances we consider that these concerns are outweighed by the benefits as set out under relevant objective (d).

### **Decision notice**

In accordance with Standard Special Condition A11 of the Gas Transporters Licence, the Authority hereby directs that modification proposal UNC625: *'Extension of 4 months to 10 months to transfer non-mandatory sites from Class 1'* be made.

**Rob Salter-Church**  
**Partner, Competition and Consumers**

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