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Dear Les,

Re: UNC Modification Proposals 0541/A/B – Removal of Uncontrollable UNC Charges at ASEPs which include sub-terminals operating on a 06:00-06:00 gas day

Thank you for your invitation seeking initial representations with regards to UNC Modification Proposals 0541/A/B (the "Proposals"). This response is submitted on behalf of National Grid NTS and is a combined response applicable to all of the Proposals.

We understand that NTS Shippers have raised the Proposals to mitigate a risk they have identified which is associated with the continued application of 06:00-06:00 gas day arrangements by upstream producers, whilst the NTS and downstream networks move to 05:00-05:00 gas day arrangements under the direction of EU legislation and as implemented through UNC Modification Proposal 0461 (Changing the UNC Gas Day to Align with the Gas Day in EU Network Codes).

We have been actively involved in the Gas Day Industry Workgroup chaired by DECC, with some involvement in the sub-group that has developed the Proposals. This response includes a number of points we have already highlighted in discussions with that sub-group prior to the Proposals being raised, and which we believe should be considered further by the UNC Workgroup.

As a result of our involvement in pre-modification discussions, we have a good understanding of the issue that the proposers are seeking to address, i.e. Shippers who may feel they are exposed to an increased system clearing imbalance risk (as a consequence of their current upstream production contracts) are looking to mitigate this risk by amending the downstream regulatory regime administered under the UNC. However, we have concerns that seeking a resolution of this issue in the downstream UNC arrangements may not be an efficient, targeted or equitable approach for all Shippers. Specifically, some Shippers who do not have input allocations at the affected NTS entry points may incur additional financial risk via the energy balancing neutrality mechanism. We would therefore suggest that further work continues, alongside the UNC Workgroup, to consider alternative upstream solutions that sit outside the UNC framework.

There are a number of areas that we suggest should be discussed further as part of the Workgroup development and have detailed our initial thoughts below.

Comment [AP1]: Shippers don't feel they will be exposed to an increased risk. They are exposed and they will be charged through no fault of their own.

Comment [AP2]: The opposite will happen. National Grid will be smearing the negative/positive impacts of non-real imbalance charges.

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1) EU Network Code Compliance (CAM and Balancing)[1]

A suite of Modifications has been developed by National Grid NTS over the past 2 years in order to achieve GB compliance with the legislative requirements of the EU Network Codes. Many of these Modifications will be implemented in October/November 2015, including the change to the UNC gas day under UNC Modification 0461, to ensure consistency with the definition detailed in the EU Capacity Allocation Mechanism (CAM). We have concerns that some fundamental elements of the Proposals are not compliant with the requirements of the EU Balancing Code, specifically around the calculation of Shippers' daily imbalance quantities and charges. For example, the Workgroup may need to consider whether knowingly utilising a 06:00-06:00 User Daily Quantity Input (UDQI) in the calculation of daily imbalance quantities and charges for a 05:00-05:00 gas day is consistent with the obligations placed upon TSOs and Shippers by the EU Balancing Code (Articles 19, 21 and 37).

Comment [AP3]: Article 19.3: "Daily imbalance charges shall be cost reflective…."These mods are trying to make the charge cost reflective.

Comment [AP4]: If National Grid comply with the strict rules of Article 21 and 37 they cannot comply with the principles of Regulation 715/2009 Article 21.3.

2) Principles of the GB Balancing Regime

The GB Balancing Regime has been developed with the Shipper as the primary energy balancer, and the Transmission System Operator (TSO) as the residual balancer. This model, which has subsequently been adopted by the EU Balancing Code, explicitly prescribes that the Shipper is incentivised to balance its own portfolio[2]. If it is unable to do so, the Shipper pays costs associated with its imbalance position for the relevant gas day (the 'polluter pays' principle).

We believe the Workgroup may wish to consider whether the solutions described within Modification Proposals 0541A and 0541B weaken this principle. Under the balancing neutrality model, if UNC charges are removed from one Shipper, they will be allocated elsewhere in order that the Shipper community as a whole remains cash-neutral. This could result in some Shippers who do not have input allocations at the affected NTS entry points being liable for a proportion of these charges. The Workgroup should consider whether this creates the potential for cross-subsidisation of imbalance costs, and whether this could therefore be viewed as undermining effective competition between Shippers.

Comment [AP5]: The charges don't really exist so should be removed. National Grid has incurred no cost that needs to be passed on. Non affected shippers would remain non affected.

Comment [AP6]: The mods do exactly the opposite they restore equality between shippers.

3) Industry System Changes and User Pays

Our current understanding of the solutions described is that there are likely to be changes required to industry systems (UKLINK) which are managed by the Transporters' Agency (Xoserve). We note that the User Pays Guidance Document[3] published on the Joint Office of Gas Transporters website states that "…*any Modification Proposal which has the potential to incur incremental Transporter Agency costs… will be classified as a User Pays Modification Proposal*". If the Proposals were to be classified as User Pays, as we believe they should be, the Workgroup will need to consider which UNC parties would benefit from implementation to identify how such User Pays costs should be apportioned.

In pre-Modification discussions with the proposers, it was suggested that National Grid NTS should pay the system change costs associated with any solution from our RIIO-T1

[1]Commission Regulation (EU) No 984/2013 establishing a Network Code on Capacity Allocation Mechanisms in Gas Transmission Systems, and Commission Regulation (EU) No 312/2014 establishing a Network Code on Gas Balancing of Transmission Networks

[2] Article 4.1 of Commission Regulation (EU) No 312/2014 establishing a Network Code on Gas Balancing of Transmission Networks

[3] http://www.gasgovernance.co.uk/sites/default/files/User%20Pays%20Guide%20Doc%20v2.pdf: page 3 paragraphs 4 and 6

EU market facilitation funding. However, we do not believe that the solutions outlined are necessitated by EU legislation and therefore we do not consider these to be EU related Modifications. As a result, we do not believe the use of RIIO-T1 EU market facilitation funding is appropriate.

Comment [AP7]: The solutions are necessitated by EU legislation as CAM and BAL have changed the downstream gas day. As stated above National Grid will not comply with Regulation 715/2009 one of these solutions in not implemented.

National Grid NTS has also met with Xoserve to discuss the Proposals. After reviewing the level of detail provided within the current stated solutions, and taking into account both parties' interpretation of the Proposals, Xoserve has advised us that, at this stage, there is insufficient detail to complete a cost assessment ('Rough Order of Magnitude' - ROM) which is meaningful. However, we recognise that the Proposers have suggested (and the Modification Panel subsequently directed) that the Proposals be issued to a Workgroup for further development. We believe that the Workgroup should seek to strengthen and provide further detail in respect of each of the solutions (likely to be in the form of detailed Business Rules) at an early stage in the Workgroup discussions, so the impacts can be understood and a ROM completed at the earliest opportunity.

4) Cost Benefit

The Workgroup may wish to consider whether a cost benefit analysis is required to ensure that any implementation costs are justified as there is no quantification of the impact of 'Time Shift Charges' (and therefore the extent of the impact on neutrality charges) detailed in the Proposals for impacted Shippers. Although a level of cost benefit analysis could be completed based on past information, the Workgroup may wish to consider whether a thorough and accurate quantification of the additional imbalance risk is achievable prior to implementation and evaluation of the impacts of the gas day industry solution (otherwise known as 'Option A').

If such a quantification cannot be completed prior to this point, then as Option A will not be implemented until October 2015, it may be appropriate to allow a minimum evaluation period (for example 3 months) to fully assess the extent of 'Time Shift Charges' whilst operating in accordance with Option A in order to provide an accurate cost benefit assessment of the solutions presented in the Proposals.

5) Relevant Objectives

The Workgroup may wish to make an assessment of whether the proposers' suggestions that the Proposals would have a positive impact on Relevant Objective (d) "*Securing of effective competition"* and Relevant Objective (g) "*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*" are correct. Our initial thoughts in respect of this are outlined below:

- **Relevant Objective d):** We believe the Proposals have the potential to have an adverse impact on competition between Shippers, by creating additional undue Neutrality cashflows for parties who do not have input allocations at the relevant sub-terminals, and creating cross-subsidies that may weaken the proposers' balancing incentives. Further, the potential for retrospective application of the solutions from the point of direction from the Authority (should this be forthcoming) may arguably undermine competition still further.

Comment [AP8]: Without one of the modifications being implemented unreal imbalance charges will be smeared around the industry.

- **Relevant Objective g):** As previously mentioned, we do not believe that the solutions as described in the Proposals are mandated by the EU Network Codes; therefore we would question whether this Relevant Objective is better facilitated. The Workgroup

Comment [AP9]: As stated above the mods are needed to comply with the principle of Regulation 715/2009.

may need to consider whether the Proposals may negatively impact upon this Relevant Objective as they have the potential to jeopardise TSO and Shipper compliance with EU Regulation, by effectively seeking to retain a 06:00 to 06:00 gas day for a subset of Shippers within the framework of the UNC neutrality regime. This may be contrary to the requirements of the EU Balancing Code.

Comment [AP10]: The BAL network code and the Regulation are incompatible given the facts, so principle should prevail.

6) Implementation and Retrospective Adjustment

We note the proposers' ambition to implement one of the Proposals by 1st October 2015. Due to the timescale for development of the Proposals in the Workgroup, the lead time for development and implementation of a robust system/process solution and the existing change congestion associated with Xoserve system delivery, we believe this implementation date is not achievable.

The proposers have also suggested that if 1st October 2015 implementation cannot be achieved, the adjustment to Shippers' UNC charges should be calculated retrospectively from 1st October 2015. Modifications with retrospective application have historically been heavily debated within UNC Workgroup discussions, and in previous decision letters Ofgem has documented its concerns associated with such retrospective application[4]. Such concerns include introducing uncertainty into the market and an increase in the perception of risk, which can negatively impact on competition. The Workgroup will need to consider whether the retrospective element of the Proposals could be seen as anti-competitive (as described above), especially if new entrants to the market may be liable for costs at a time when they were not active market participants.

Comment [AP11]: There will be uncertainty in the market until these unreal charges are removed.

In summary, we believe there are several aspects of the Proposals that are unclear, or require further consideration, and which need to be further developed and understood as part of the Workgroup development. National Grid NTS welcomes further discussion on the points highlighted in this initial representation at the forthcoming Workgroup meetings.

Yours sincerely,

Phil Lucas
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National Grid NTS

[4] For example, UNC Modification 451V and 451AV Individual Payments for Pre-Payment and Smart Meters