

Modification proposal:	Uniform Network Code (UNC) 0240: Promoting Competition in Operating Margins Provision		
Decision:	The Authority ¹ directs that this proposal be made ²		
Target audience:	The Joint Office, Parties to the UNC and other interested parties		
Date of publication:	16 February 2009	Implementation Date:	To be confirmed by the Joint Office

Background to the modification proposal

Operating Margins (OM) gas is the term for gas that is used to maintain system pressures under certain operational circumstances, such as a sudden loss of supply or a sharp increase in demand. OM gas allows time for National Grid Gas (NGG) to reconfigure the National Transmission System (NTS) or for the market to deliver additional supply. This protects against the need to declare emergency conditions so that normal market operation can be maintained where possible. The requirement to hold OM gas is set out in NGG's Safety Case and in the Uniform Network Code (UNC).

As part of the Transmission Price Control Review (TPCR)³, NGG NTS accepted special licence condition C25⁴ which requires it to use reasonable endeavours to promote competition in the provision of OM services by 1 April 2009. Implementation of this obligation is currently restricted by Section K of the UNC which only allows provision of OM services from storage facilities and LNG importation facilities.

The modification proposal

To meet the requirements of special condition C25, NGG NTS raised modification proposal UNC 240 on 11 December 2008. The primary aim of the proposal is to increase flexibility in the provision of OM gas and extend the range of potential OM service providers. The particular features of the modification are described below.

The definition of OM Gas Delivery Arrangements⁵ under the UNC has been extended so that OM services can be provided by NTS-connected supply and demand sources, and Distribution Networks (DNs). Further, as new providers may not be storage-based, the modification proposal requires NGG NTS to specify and procure OM requirements on the basis of a new Operating Margins Year (OMY) rather than a Storage Year as is currently the case.

¹ The terms 'the Authority', 'Ofgem' and 'we' are used interchangeably in this document. Ofgem is the Office of the Gas and Electricity Markets Authority.

² This document is notice of the reasons for this decision as required by Section 38A of the Gas Act 1986.

³ For TPCR Final Proposals, see:

http://www.ofgem.gov.uk/Networks/Trans/PriceControls/TPCR4/ConsultationDecisionsResponses/Documents1/16342-20061201_TPCR%20Final%20Proposals_in_v71%206%20Final.pdf.

⁴ Special Condition C25: Promoting competition in the provision to the licensee of operating margins services. For the full text, see: http://epr.ofgem.gov.uk/document_fetch.php?documentid=13306.

⁵ OM Gas Delivery Arrangements are currently defined as arrangements whereby a third party agrees to hold capacity and gas in storage facilities and LNG importation facilities which can be used to maintain system pressures under certain operational circumstances. UNC Mod 240 would extend this definition so that OM services can be provided by NTS-connected supply and demand sources and DN's.

Where NGG NTS has entered into OM Capacity Arrangements⁶ and OM Gas Delivery Arrangements, UNC 240 provides for it to have greater flexibility, subject to contract terms, to terminate these arrangements, sell Storage Capacity and enter into alternative arrangements within the OMY. The proposal also seeks to modify the Closing Margins Adjustment Charge calculation. This allows NGG NTS, where at the start of or during a Storage Year it sells gas that had previously been held in storage under OM Capacity Arrangements, to recover the costs of procuring and injecting that gas, as well as the costs of any sale. UNC 240 proposes that the calculation also include Pre-Storage Year Transfers and sales of gas.

In addition to facilitating the implementation of special condition C25, UNC 240 proposes that OM gas may be used up to 24 hours after damage to or failure of any part of the NTS, rather than only on the Gas Day⁷ on which the event occurs.

The proposal also seeks to clarify the existing processes outlined in Section K, particularly the role of the Relevant System Manager, and resolves a number of legal drafting errors, some of which stem from the implementation of Network Code Modification 0311⁸.

UNC Panel⁹ recommendation

At the UNC Panel (the 'Panel') meeting on 22 January 2009, the Panel unanimously recommended implementation of this proposal.

The Authority's decision

The Authority has considered the issues raised by the modification proposal and the Final Modification Report (FMR) dated 4 February 2009. The Authority has considered and taken into account the responses to the Joint Office's consultation on the modification proposal which are attached to the FMR¹⁰. The Authority has concluded that:

1. implementation of the modification proposal will better facilitate the achievement of the relevant objectives of the UNC¹¹; and
2. directing that the modification be made is consistent with the Authority's principal objective and statutory duties¹².

We also note that NGG NTS is currently engaged in a tendering process for the procurement of OM gas. Given the timetable of this process going forward, the Authority encourages the Joint Office to implement UNC 240 with immediate effect.

Reasons for the Authority's decision

⁶ OM Capacity Arrangements are arrangements whereby NGG NTS holds capacity and gas in storage facilities and LNG Importation Facilities which can be used to maintain system pressures under certain operational circumstances. UNC Mod 240 does not increase the scope of this definition.

⁷ The gas day begins at 06:00 and ends at 06:00 the following day.

⁸ Network Code Modification 0311: Operational Use of Storage Post Unbundling.

⁹ The UNC Panel is established and constituted from time to time pursuant to and in accordance with the UNC Modification Rules.

¹⁰ UNC modification proposals, modification reports and representations can be viewed on the Joint Office of Gas Transporters website at www.gasgovernance.com.

¹¹ As set out in Standard Special Condition A11(1) of the Gas Transporters Licence, see: http://epr.ofgem.gov.uk/document_fetch.php?documentid=6547.

¹² 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.

Seven responses were received by the Joint Office. All seven supported implementation of the proposal and considered that it would better facilitate relevant objectives (a), (c) and (d) of the UNC.

The Authority agrees that this proposal will further relevant objectives (a), (c) and (d), but considers that it will also facilitate relevant objective (f). Our reasons for this are set out below. Please note that unless directly stated, Ofgem considers the proposal to be neutral against the aims of the relevant objectives.

Relevant objective (a): the efficient and economic operation of the pipe-line system to which this licence relates

In the event of damage to or failure of any part of the NTS, Section K of the UNC currently permits OM gas to be used during the Gas Day on which the incident occurs. The Authority agrees with the proposer and all respondents that by allowing OM gas to be used up to 24 hours following damage to or failure of any part of the NTS, UNC 240 removes the operational difficulties that could arise if damage or failure occurred near the end of a Gas Day. We also believe this change enhances security of supply by reducing the possibility that an emergency is declared and normal operation of the market suspended.

We further note that the proposal expands the range of potential OM service providers which may increase the diversity of OM service provision and location. The potential for an increased range of OM service providers under the modification proposal allows the opportunity for such services to be provided in a more economic and efficient manner. The effect of this would be to improve the ability of NGG NTS to manage operational stresses.

Relevant objective (c): so far as is consistent with sub-paragraphs (a) and (b), the efficient discharge of the licensee's obligations under this licence

The proposal facilitates the implementation of special condition C25 by promoting effective competition in the provision of OM services. Further detail on how UNC 240 facilitates competition is provided in relation to relevant objective (d) below.

Relevant objective (d): so far as is consistent with sub-paragraphs (a) to (c) the securing of effective competition: (i) between relevant shippers; (ii) between relevant suppliers; and/or (iii) between DN operators (who have entered into transportation arrangements with other relevant gas transporters) and relevant shippers

The Authority agrees with the proposer and all respondents that the proposal will better facilitate relevant objective (d). Competition in the provision of OM services is facilitated primarily by removing the current restriction limiting OM service provision to storage facilities and LNG importation facilities. The proposal allows OM services to be procured from NTS-connected supply and demand sources and DNs, as well as storage facilities and LNG importation facilities. On this point the Authority notes that procurement in this way is still prevented by the Safety Case, which defines OM gas as gas held in storage. As such a material change to the Safety Case will also be required, which we understand NGG is in the process of seeking from the Health and Safety Executive.

In order to accommodate new OM service providers, UNC 240 also enhances the clarity and accuracy of Section K and increases the flexibility of NGG NTS to procure OM

services. Notably it proposes that NGG NTS specifies and procures OM requirements on the basis of the OMY.

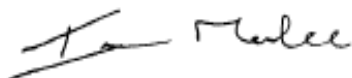
Relevant objective (f): so far as is consistent with sub-paragraphs (a) to (e), the promotion of efficiency in the implementation and administration of the network code and/or the uniform network code

The correction of legal drafting errors will also assist in the accurate implementation of the UNC. In particular, the proposal corrects errors stemming from Network Code Modification 311 which unintentionally modified the formula relating to Net Margins WACOG and introduced a number of cross-referencing errors. As NGG NTS has continued to calculate Net Margins WACOG according to the provisions set out in the Network Code prior to Modification 311, UNC 240 will ensure that Section K corresponds with current practice.

However, there remains a further cross-referencing error which has not been corrected by the proposal. This error was in place prior to UNC 240 being raised and this modification does not impact on this error. Paragraph 3.8.4 of the revised legal text provided with UNC 240 should reference 4.3.4 not 3.7.4. Having been made aware of this NGG NTS has indicated that it will raise a separate Consent to Modify the UNC in order to correct this error. As this error was in effect prior to the modification proposal, we do not consider that it impacts on our conclusion that the proposal better meets relevant objective (f).

Decision notice

In accordance with Standard Special Condition A11 of the Gas Transporters Licence, the Authority, hereby directs that modification proposal UNC 0240: "Promoting Competition in Operating Margins Provision" be made.



Ian Marlee
Director, Trading Arrangements

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