

Modification proposal:	Uniform Network Code (UNC) 390: 'Introduction of a Supply Point Offtake Rate Review and Monitoring Process' (UNC390)		
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:	24 February 2012	Implementation Date:	1 April 2012

Background to the modification proposal

In March 2010, we published our decision letter³ on Scotland Gas Networks plc (SGN)'s application to re-open the 2008-2013 Gas Distribution Price Control to provide additional capital expenditure. The additional funding was required to reinforce SGN's network to accommodate the change of certain 'Interruptible' customers to 'Firm' status from October 2011, under the current Interruptible reform⁴. In the March 2010 decision letter, we approved an adjustment to SGN's Interruption Incentive⁵ allowance to allow for specific reinforcement projects, but outlined our concerns about the existing charging and contractual arrangements. We noted in our decision letter that there was limited evidence to demonstrate that there were adequate incentives in place to obligate users to provide Supply Point offtake Rates⁶ (SPORs) data which reflect actual usage patterns. The SPORs were referred to as the Supply Point Hourly Quantities (SHQs) in our decision letter.

Gas Distribution Networks (GDNs) use SPORs information provided by gas shippers to meet certain legislative requirements placed upon them to ensure the operation of a safe and economic gas transportation system. The SPORs also form a key data element used in the construction and operation of the network planning and analysis models used in stimulating gas network performance. Under the UNC, registered users are required to report significant increases in SPORs. However, there is no direct requirement on registered users to either amend, or take reasonable steps to ensure they become aware of **reductions** (as opposed to increases) in SPORs at a Daily Metered (DM) Supply Point. We also noted in our March 2010 decision that customers' capacity charges seemed broadly independent of contracted SPORs, despite the fact that the SPORs may trigger additional investment costs. We indicated that GDNs needed to initiate a review of the concerns raised. We noted that failure on the part of GDNs to review this situation might lead to the disallowing of all or part of future expenditures where GDNs cannot demonstrate that their contractual and charging arrangements place appropriate incentives on Users to provide accurate SPORs.

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 Our decision letter can be found at the following link-

<http://www.ofgem.gov.uk/Pages/MoreInformation.aspx?docid=501&refer=Networks/GasDistr/GDPCR7-13>

⁴ In March 2007, the Authority directed UNC090 'Revised DN Interruptible Arrangements' to be made. The revised interruptible reform changed the way capacity rights were allocated. Rather than allowing eligible customers to determine their firm or interruptible status at only one year's notice, the reform arrangements now allow GDNs to offer interruptible capacity solely in the locations and volumes they require via annual auctions with three year lead times. See <http://www.gasgovernance.co.uk/0090>

⁵ The interruption incentive is a package that incentivises GDNs to contract for interruption up to the point at which it becomes more efficient to reinforce their networks to make customers' rights firm.

⁶ SPORs is defined as the maximum instantaneous rate in kWh/hour that the user is permitted to offtake gas from the Total System at a directly metered supply point component. It is a key data input used in the construction and operation of GDN network analysis models.

This modification proposal seeks to address these concerns. It reflects the output of the Uniform Network Code (UNC) Modification 0329 Review Group⁷ in terms of modifying the current charging and contractual regime to improve the SPORs review and monitoring process between shippers and GDNs.

The modification proposal

UNC390 was proposed by SGN in July 2011 to address the concerns raised in Ofgem's March 2010 decision letter. The modification aims to introduce two new obligations into the UNC:

- shippers and GDNs will have a joint obligation to review the SPORs for DM Supply Points on an annual basis to ensure they accurately reflect end consumer capacity requirements; and
- shippers will be obliged to apply for revised SPORs where they become aware that the maximum offtake rate at a registered DM Supply Point component may be or has been subject to any **reduction**. Shippers will also be required to take all reasonable steps to ensure they become aware of any such **reduction** in SPORs.

The proposal does not intend to cause SPORs to fluctuate on an annual basis in line with usage, but aims to ensure that the SPORs accurately reflect annual potential maximum capacity requirements. National Transmission System (NTS) Supply Point Components are excluded from the new provisions under the proposal. It is anticipated that the proposal will improve GDNs' network planning and analysis activities and mitigate the risk of unnecessary reinforcement expenditure.

SGN considers that the proposal will better facilitate the achievement of the following relevant objectives:

- (a) Efficient and economic operation of the pipeline system of its Gas Transporters (GT) Licence. It considers that this objective will be met to the extent that the modification proposal helps to identify where capacity requirements are excessive or insufficient; and
- (c) Efficient discharge of the licensee's obligation. There are several references to the efficient and economic development of the relevant pipeline throughout the GT licence. The provision of more accurate capacity requirement information by shippers to transporters would facilitate efficient discharge of the relevant licence obligation.

UNC Panel⁸ recommendation

At the Modification Panel meeting held on 19 January 2012, the Panel reached a majority decision in favour of the modification proposal, with six members voting in favour, three against and one member abstaining. The proposal was therefore recommended for implementation.

⁷ This Review Group comprised transporters, shippers and end user representatives and was set up to review the Industry's Charging and Contractual Arrangements.

⁸ The UNC Panel was established and is constituted from time to time pursuant to and in accordance with the UNC Modification Rules.

The Authority's decision

We have considered the issues raised by the modification proposal and the Final Modification Report (FMR) dated 20 January 2012. We have also taken into account the responses to the Joint Office's consultation on the modification proposal which are attached to the FMR⁹. We have concluded that:

1. implementation of the modification proposal will better facilitate the achievement of the relevant objectives of the UNC¹⁰; and
2. directing that the modification be made is consistent with the Authority's principal objective and statutory duties¹¹.

Reasons for the Authority's decision

We have assessed the modification proposal against the relevant objectives of the UNC. We consider that this modification proposal better facilitates relevant objectives (a), (c) and (f). The effect of the proposal is neutral with respect to all other relevant objectives.

Relevant Objective (a) – The efficient and economic operation of the pipe-line system

We agree with the proposer's view that accurate SPORs aid an efficient network planning process and hence support the efficient and economic development of the pipeline system. SPORs data have both safety and investments implications and we welcome proposals to improve their accuracy. By requiring transporters and shippers to work together to introduce a process that gives assurance about the accuracy of SPORs, the proposal has the potential to mitigate the risk of over or under investments in the system. By avoiding investments in the system to meet overstated SPORs, the transporters would be using capital investment in a more efficient and economic manner.

A further benefit of the proposal is that transporters would be able to offer identified spare capacity to other users and, as a result, make effective use of existing capacity. The provision of accurate SPOR information could also stop transporters from incurring avoidable last minute systems operation costs due to provision of insufficient capacity. This would be likely to lead to a reduction in overall costs within the industry, working in favour of all parties, including existing and future customers.

Relevant Objective (c) – Efficient discharge of the licensee's obligations

GDNs have a licence obligation to operate their pipeline system in an efficient and economic manner under standard licence condition 9(1)(a)¹². We consider that the changes proposed in the modification facilitate the discharge of this obligation.

Relevant Objective (f) – The promotion of efficiency in the implementation and administration of the code.

⁹ UNC modification proposals, modification reports and representations can be viewed on the Joint Office of Gas Transporters website at www.gasgovernance.com

¹⁰ As set out in Standard Special Condition A11(1) of the Gas Transporters Licence, see: <http://epr.ofgem.gov.uk/index.php?pk=folder590301>

¹¹ 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.

¹² See: http://epr.ofgem.gov.uk/document_fetch.php?documentid=16035

A number of respondents and Panel members were concerned that the administrative costs associated with the implementation of this proposal were onerous and could potentially outweigh the benefits. Specifically, they noted that the additional obligation might place an undue burden on smaller niche shippers in the industry. We also note the view that the status quo should be maintained to the extent that the registered user is prepared to pay for the potentially excessive capacity in instances where predicting future demand is difficult.

We note that there is an existing UNC obligation requiring shippers to have processes in place to monitor **increases** in the maximum offtake rate at DM Supply Points. As such, the proposal to incorporate a **SPOR reduction** monitoring process should be an extension of existing processes, imposing minimal costs to the Shipper. It is unlikely that the additional costs associated with the provision of the required additional reports and analysis of SPOR data would undermine the efficient implementation and administration of the code. Rather, we believe that the modification proposal provides a channel for increased dialogue and discussion on the issue of capacity requirement across the industry, and has the potential to enhance relationships between transporters and shippers.

Decision notice

In accordance with Standard Special Condition A11 of the Gas Transporters Licence, the Authority hereby directs that modification proposal UNC390 'Introduction of a Supply Point offtake Rate Review and Monitoring Process' be made.

Andrew Burgess
Associate Partner, Transmission and Distribution Policy
Signed on behalf of the Authority and authorised for that purpose