Joint Office of Gas Transporters

Representation - Draft Modification Report

UNC 0621; 0621A; 0621B; 0621C; 0621D; 0621E; 0621F; 0621H; 0621J; 0621K*; 0621L

Amendments to Gas Transmission Charging Regime

* Amendments to Gas Transmission Charging Regime and the treatment of Gas Storage

Responses invited by: 5pm on 22 June 2018

To: enquiries@gasgovernance.co.uk

Representative:	Christiane Sykes
Organisation:	Shell Energy Europe Limited (SEEL)
Date of Representation:	
Support or oppose implementation?	0621 - Oppose 0621A - Oppose 0621B – Qualified Support 0621C - Oppose 0621D - Oppose 0621E - Qualified Support 0621F - Oppose 0621H - Oppose 0621J - Oppose 0621K - Oppose 0621L – Qualified Support

Expression of Preference:	*If either 0621; 0621A; 0621B; 0621C; 0621D; 0621E; 0621F; 0621H; 0621J; 0621K or 0621L were to be implemented, which ONE modification would be your preference?* *0621B*

Reason for support/opposition and preference: Please summarise (in one paragraph) the key reason(s)

The flexibility and transparency offered to market participants through the GB gas governance process has enabled the GB gas market to continuously evolve to reflect the dynamic needs of the industry and has served the industry well for many years. It is with great regret, therefore, that proposed changes to the GB charging regime as part of modification 0621 and 0636, has brought the entire process into disrepute. We hope that this does not lead to any knee-jerk reactions, which would limit or restrict the flexibility in the governance process, which has so far enabled the NBP to develop as one of the most competitive, liquid markets in Europe. Moreover, we have serious concerns that the process followed could lead to fundamental changes to the charging regime which, owing to the fragmented, complex and confused approach to seeking to comply with the EU TAR NC, could lead to sub-optimal outcomes at best and at worst, damage the liquidity, competition and attractiveness of the GB energy market.

The Significant Code Review (SCR) mechanism is designed to facilitate complex and significant changes to the codes that energy companies are required to abide by and it is regrettable that this process was not followed for fundamental changes to the charging regime, which in our view, fits exactly with the type of change the SCR was designed for. National Grid and 0621 Working Group participants have worked tirelessly to assess changes to the GB charging regime, required to comply with the TAR NC whilst seeking solutions, which build on the successes and address the failures of the existing regime.

The breath of the changes and the complexity of the process have generally constrained market participants' ability to put forward proposals which significantly diverge from NG's proposed modification. An SCR process and consistent steer from Ofgem would have enabled wider industry discussion and the formation of proposals, which might better meet National Grid's Relevant Objectives and TAR NC compliance.

In light of the issues highlighted above, we are very concerned as to whether implementation of any of the proposals would better facilitate the Relevant Objectives, compared to the status quo. Many of the proposals, including SEEL's, have sought to address limitations or unintended consequences of National Grid's proposal. It should, therefore, be taken into account that the alternative proposed incremental changes to National Grid's modification do not constitute a general acceptance that National Grid's proposal is the optimal solution, only that anything else would have a limited chance of success and would be a further waste of industry time and resources.

We recognise the challenge Ofgem and the industry now face in terms of understanding the complexities of these proposals and even more so, the impact on the GB gas market and on the competitive landscape between market participants. We are also concerned that industry uncertainty will be prolonged in the context of RIIO-2 and how potential changes to the entry:exit split, allowed revenues and entry capacity baselines will interact with proposed changes to the charging regime.

To ensure enduring solutions can be found that meet compliance with the TAR NC and National Grid's Relevant Objectives, the most pragmatic approach is to retain as much as possible of the existing regime, without unduly discriminating between IPs and non-IPs and implement the minimum for TAR NC compliance. This would afford stakeholders sufficient time to fully appraise and implement an overarching proposal which better meets the Relevant Objectives and limits industry uncertainty.

In sum, SEEL's view is that the case for moving away from the current marginal cost based approach to an as yet undefined forecast bookings approach, has yet to be made.

0621

Multipliers

SEEL welcomes National Grid's approach to set short-term capacity multipliers at 1 as the minimum required in the TAR NC. However, the TAR NC stipulates that in duly justified cases, the level of the respective multipliers may be less than 1. Multipliers for short-term capacity products act as a barrier to trade and risk impeding market liquidity and cross-border flows. In our view, there is a duly justified case too set a lower multiplier for within-day and day-ahead capacity products as this would better align with the CAM network code in promoting short-term capacity products to facilitate trading and market liquidity.

Optional Commodity Tariff

As we noted in our response to modification proposal 0636 and the associated alternatives, the proposed changes to the Optional Commodity tariff will have a significant impact on persons engaged in the shipping and supply of gas and in the generation of electricity, yet there has been limited analysis to enable these parties to understand the magnitude of the impact. We trust Ofgem will take this into account in their Impact Assessment.

Until we have fully understood the impact, we cannot support any changes to the optional commodity tariff. Given the complexities of the suite of proposed changes, a more streamlined approach to changes to the GB charging regime may be appropriate, affording industry participants more time to develop solutions to specific issues, which are not immediately required as part of the TAR NC implementation.

0621A

The impact of any modifications which propose favourable terms to a specific source of gas or flexibility need to be fully assessed with respect to meeting the Relevant Objectives of securing effective competition and avoiding undue preference in the supply of transportation services. Furthermore, the use of the network from either a domestic entry point or an interconnection point should be the same so this proposal should also be assessed against the Relevant Objective of cost reflectivity.

0621B

Forecasting Contracted Capacity on the basis of Obligated baseline levels ensures the values used to derive charges are constant and free from manipulation, facilitating stable and predictable capacity tariffs and furthering the Relevant Charging Objective (a) of cost reflective charges and in line with Article 4(3) of the TAR NC, which stipulates that an exception to capacity based tariffs may be approved where flow based charges 'levied for the purpose of covering the costs mainly driven by the quantity of the gas flow' and 'calculated on the basis of forecasted or historical flows, or both, and set in such a way that it is the same at all entry points and the same at all exit points'.

This proposal has the further advantage of addressing some of the concerns SEEL has sought to address through 0621L by proposing a more equitable approach to calculating capacity tariffs and revenue recovery by reducing cross subsidies between network users, independent of when the network user buys the capacity, thereby sharing revenues across the network users who buy the same capacity product.

With respect to the proposed changes to revenue reconciliation, please see our response to 0621A.

0621C

This proposal is the only proposal which seeks to address the flaw in all other proposals, in that there is no enduring regime to manage inefficient bypass of the NTS. Whilst we welcome the initiative, it is challenging within the short timescales to fully assess the methodology and the potential impact. Based on an initial assessment, however, calculating the optional charge on the basis of daily variable factors instead of ex-ante fixed factors risks undermining the value of such a charge by making it unpredictable and difficult to take into account when negotiating contracts. Consequently, we are unable to support this proposal.

0621D

SEEL does not support this proposal as it removes the Optional Commodity tariff from 2019 onwards. This could have significant implications for flows towards GB and to neighbouring markets, jeopardising market liquidity, in conflict with the EU network access regulation, which stipulates that tariffs must not restrict liquidity nor distort trade across borders.

As we stated in our response to proposal 0636, Ireland in particular, could be exposed to a material impact as it relies on gas flows through the Moffat Interconnector. The impact is exacerbated if there are any field issues for Irish domestic gas production, as it would lead to increased flows through Moffat and potentially high and unpredictable tariffs, which could have a consequential impact on end consumers.

0621E

As per our response to 0621B, calculating FCC on the basis of obligated capacity levels will ensure the values used to derive charges are constant and free from manipulation, facilitating stable and predictable capacity tariffs. This proposal highlights the exposure to transmission-connected gas-fired generators bidding in the T-4 2021-2022 electricity Capacity Market Auction, facing unpredictable and uncertain gas capacity tariffs. Basing the FCC on obligated capacity for the enduring regime will ensure the risk identified by Uniper cannot arise in later Capacity Market Auctions as well.

0621F

See our response to 0621A.

0621H

SEEL does not support this proposal as it exacerbates the distortion already caused by National Grid's proposal by creating an undue preference for the supply of transportation services to existing capacity holders, which is not in line with the Relevant charging objective (aa) (iii).

Existing capacity contracts on fixed tariffs, which have not been subject to indexation make up approximately 50% of all capacity bookings. Excluding these contracts from future capacity based revenue recovery charges creates an unfair competitive advantage to existing capacity holders and leaves future capacity holders picking up a significant proportion of the cost of any under-recovery, which could also act as a barrier to entry.

See also our response to 0621L.

0621J

SEEL does not support this proposal. As identified by Energy UK, the current level of Exit PARCA activity and the PARCA window for Entry capacity in the south west suggests that there remains a requirement for locational signals, which would not be supported by as postage stamp charging methodology in GB.

0621K

See our response to 0621F. In addition, according to the TAR NC, interruptible discounts must reflect the probability of interruption, which has not been demonstrated in this proposal.

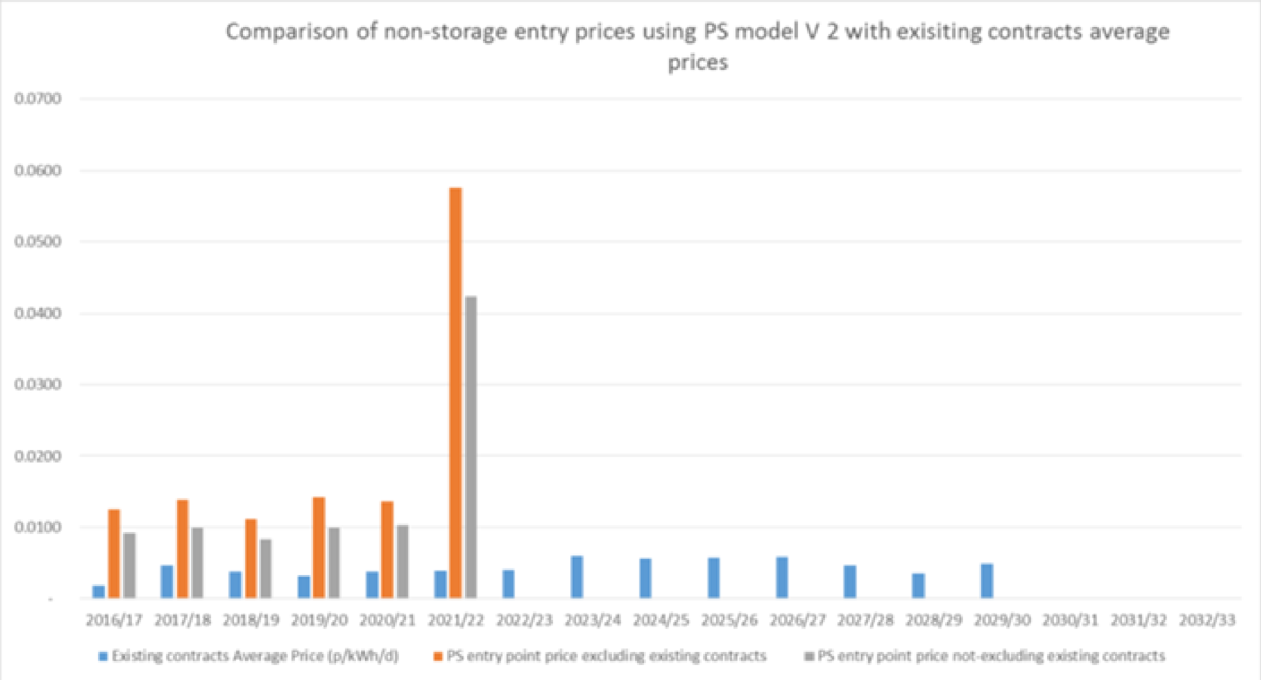
0621L

Whilst National Grid's proposal does not provide the best solution out of the proposals put forward for an enduring, cost-reflective charging regime, the aim of this proposal is at least to mitigate some of the worst impacts with respect to removing distortive terms inherent in National Grid's proposed calculation of FCC. The motive for offering only qualified support is that, for the reasons set out below, 0621L better furthers the relevant objectives, compared to 0621 but overall, the status quo or a more commodity based charging regime better meets the objectives of cost-reflectivity and securing effective competition between relevant shippers and suppliers.

Including existing contracts in the CWD calculation ensures the share of allowed revenue collected from each entry and exit point is proportionate to its contribution to the costs of the provision of system capacity. Where existing capacity bookings make up approximately 50% of all capacity bookings, including such contracts avoids undue preference in the supply of transportation services by ensuring that transmission services revenue is obtained on an equal basis from all entry and exit points.

According to National Grid's NTSCMF / Sub-Group paper - Forecasting Contracted Capacity (FCC), it was understood in the TAR NC ENTSOG working group that the intention behind the definition of FCC was that generated prices would constitute 'all capacity that has been sold to date plus everything [that] is expected to be sold in remaining auctions/application windows'. Whilst the TAR NC lacks sufficient detail in this regard, this proposal is in line with the initial intention of the TAR NC.

By excluding existing contracts from the CWD calculation, the magnitude of the discrepancy between the average price paid for existing capacity holders and the postage stamp price for future capacity bookings, can be seen in the table below. From 2021, at the start of the enduring regime, this marked difference risks distorting competition between shippers as it gives a competitive advantage to shippers holding existing capacity. This distortion could run long in to the future and as late as 2035.



SOURCE: Energy UK

TAR NC Article 6.3 stipulates that the same reference price methodology shall be applied to all entry and exit points in a given entry-exit system. Including Existing Contracts for exit reference price calculations and excluding them for entry reference price calculations is inconsistent with this Article and so the proposal to include Existing Contracts for entry and exit reference price calculations ensures changes to the UK charging regime are compliant with TAR NC.

TAR NC Article 6.4 stipulates that adjustments to the application of the reference price methodology to all entry and exit points may only be made as a result of benchmarking, equalisation, rescaling or to account for tariff discounts. Amending data inputs by netting off existing contracts at entry points is not one of the permissible adjustments. By including existing contracts in the CWD calculation, this proposal ensures compliance with the TAR NC.

Moreover, where existing contracts are netted off and the model results in a zero price, using the price from the nearest point, which in the case of entry points can be a considerable distance, represents an adjustment to the application of the reference price, which is not in accordance with this Article. Including existing contracts in the FCC and RPM resolves these issues and ensures the proposal is TAR NC compliant.

TAR NC Article 7(b) & (e) states that the reference price methodology shall comply with Article 13 of Regulation (EC) No 715/2009 and…shall aim at: b) taking into account the actual costs incurred for the provision of transmission services considering the level of complexity of the transmission network. By including existing contracts in the RPM and FCC, reference prices will reflect costs incurred.

Implementation: *What lead-time do you wish to see prior to implementation and why? Please specify which Modification if you are highlighting any issues.*

Lead times on publications of tariffs in line with Appendix 1 in the Draft Modification report should be the minimum lead times if Ofgem decides to approve any of the proposals. A decision on whether to approve the proposals would be welcomed as soon as practically possible to give industry sufficient time to assess their capacity booking strategies, update their systems and respond accordingly.

Impacts and Costs: *What analysis, development and ongoing costs would you face?*

This is very challenging to determine for all of the proposals as there has been insufficient time to fully analyse the impacts of each modification. We trust Ofgem's Impact Assessment will draw out the associated costs and benefits of each proposal, at which stage we will respond to the follow-up consultation.

Legal Text: *Are you satisfied that the legal text will deliver the intent of the Solution? Please specify which Modification if you are highlighting any issues.*

Ensuring the legal text accurately reflects the intent of the proposals and ensures the proposals can work in practice is paramount but we have not had time to adequately review the legal text of each of the 11 proposals.

Modification Panel Members have requested that the following questions are addressed:
Please specify which Modification your views relate to.

1. *Do you believe there is specific issues that should be considered by Ofgem's Regulatory Impact Assessment?*

   We trust that Ofgem's overarching impact Assessment will use uniform base data to ensure the suite of proposals are analysed from the same starting point to avoid any misleading outcomes.

Ofgem requested that the following questions be included as part of the consultation. Panel agreed to include these:

2. *The rationale in the report for having an interim period and using the obligated capacity as the Forecasted Contracted Capacity (FCC) is to avoid significant changes to charges and have a period to understand how booking behaviour changes. How does this compare to having two structural changes to charges (one at the start of the interim period and another at the enduring period)?*

   According to the TAR NC, 'existing' fixed price contracts must have been concluded before the TAR NC entered into force in April 2017. The concept of Interim contracts is not envisaged. Whilst we understand the principle for introducing 'interim contracts', this has led to a level of unacceptable risk and uncertainty with regards to the relevant capacity auctions as users booking in the AMSEC and QSEC auctions would not know if the price agreed to would be subject to a fixed or floating capacity tariff. Some of this risk could be mitigated my delaying the associated capacity auctions until after the TAR NC is implemented, ensuring network users have sufficient time to assess their booking strategy. This would, however, have the same effect as removing the concept of 'interim contracts', which will prevent any potential for distortion and undue discrimination which might otherwise result from network users booking long-term capacity on fixed price contracts, which could give them an unfair competitive advantage if they are not subject to future revenue recovery charges, depending on which proposal is implemented and comparatively lower capacity tariffs.

3. *What (if any) consequences do you see from 'interim contracts' being allocated at QSEC and AMSEC auctions in 2019 given the timings of these auctions in the UNC and possible date of Ofgem decision on UNC621? What options are there to deal with these consequences and what impact would these options have?*

   See above.

4. *Do you consider the proposals to be compliant with relevant legally binding decisions of the European Commission and/or the Agency for the Co-Operation of Energy Regulators?*

Comments to be provided as part of the ACER consultation or in response to Ofgem's consultaiotn.

5. *In what way do you consider the reference price methodologies proposed (Capacity Weighted Distance (CWD), CWD using square root of distance and Postage Stamp) to be cost reflective and meet the criteria in Article 7 of TAR?*

Comments to be provided following Ofgem's consultation and Impact Assessment.

6. *The proposals have different combinations of specific capacity discounts for storage sites and bilateral interconnection points. In what way do you consider the different combinations facilitate effective competition between gas shippers and gas suppliers?*

   See our response to the specific proposals above.

Are there any errors or omissions in this Modification Report that you think should be taken into account? *Include details of any impacts/costs to your organisation that are directly related to this.*

Updated analysis was only provided by National Grid just over a week before the deadline for responding to this consultation. This is has not given industry participants sufficient time to fully assess the impact and adequately identify the costs and benefits of each proposal, which ideally, would have fed into the modification report.

Moreover, there is a risk that the analysis provided so far could be misleading as it has not been adequately assessed and consequently, may not be fully understood by those attempting to use it to inform their response to this consultation.

The interaction of these proposed changes with government objectives such as the MERUK should also be considered. MERUK is the central government obligation, which requires oil and gas operators to maximise economic recovery of the UK Continental Shelf (UKCS: UK Offshore area). The impact of the proposals on the MERUK and the associated benefits of ensuring the UKCS is an attractive basin to invest in facilitates diversity of supply, an economic and efficient network, ultimately, lowering costs for consumers.

We trust Ofgem's Impact Assessment will include quantitative analysis on the impact on the cost of energy and supply security for Scottish consumers as the CWD regime increases the cost of transporting gas at some entry points in the north of the country.

Please provide below any additional analysis or information to support your representation