

**Gas System  
Operator**

**Review of the charging methodology to  
avoid the inefficient bypass of the NTS**

**UNC621 Decision Review**

**NTSCMF 0670R Workgroup**  
10<sup>th</sup> January 2019

**nationalgrid**



# UNC621 Ofgem Decision Review – 0670R Considerations

Highlighting key elements of the decision letter relevant to the **NTS Optional Charge (NOC)** for discussion within the 0670R Workgroup, for consideration against any future proposals.

# UNC621 Ofgem Decision Review – 0670R Considerations

## The NTS Optional Charge and Optional Commodity Charge

Annex 2, Page 16

Ofgem consider the existing OCC, and proposed NOC, provide a **cross-subsidy between those who can, and those who cannot, utilise the charge.**

The proposed updates... would **reduce the level of cross-subsidy** created by the NOC, and therefore have a **positive impact on effective competition** relative to the status quo.

In Ofgem's view there is **insufficient evidence that parties would by-pass the NTS** in the absence of the NOC and they consider that the NOC in the form proposed in the UNC621 modifications would still have a negative impact on competition

In the event there is a **genuine risk of construction or use of a competing pipeline** that could increase the level of charges for remaining consumers, then the **development of any charges to account for that would need to ensure that they comply with relevant legislation.**

# UNC621 Ofgem Decision Review – 0670R Considerations

## The NTS Optional Charge – Non-compliance

Decision Letter, Page 8

The NOC as proposed is for the transmission of gas from a specific entry point to a specific exit point.

Article 4(1) of TAR NC sets out the defining characteristics of a “transmission service”, Ofgem consider NOC is the provision of a transmission service. The **compliance of tariffs for transmission services** must then be assessed against **Article 4**.

**Article 4(2)** states that “Transmission tariffs may be set in a manner as to take into account the conditions for firm capacity products”.

The term “firm capacity” is defined in Article 2(16) of Regulation (EC) No 715/2009 as “gas transmission capacity contractually **guaranteed as uninterruptible** by the transmission system operator”.

The NOC, in the majority of modifications, is levied on flows, without reference to the underlying capacity booking, and in all cases, the **NOC is available to both firm and interruptible products**.

**Article 4(3)** of TAR NC establishes the rule that the transmission services revenue shall be recovered via **capacity-based transmission tariffs**.

# UNC621 Ofgem Decision Review – 0670R Considerations

## The NTS Optional Charge – Non-compliance, NOC at non-IPs

Decision Letter, Page 9/10

As an exception to the rule that the transmission services revenue shall be recovered via capacity-based transmission tariffs, commodity-based tariffs may be allowed, subject to the approval of Ofgem and the requirements set out in Article 4(3)(a) and 4(3)(b)

### Article 4(3)(a)

a “flow-based charge” which may be established to cover costs that are mainly driven by the volume actually flowed

TAR NC requires any exempt flow-based charge to be 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.

Cannot be justified:

**NOC is not available at all entry and exit points.**

NOC unit rate is derived using an **unsuitable proxy for “forecasted” or “historical” capacity allocations and flows**

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### Article 4(3)(b)

a “complementary revenue recovery charge” to manage revenue under- and over-recovery

Cannot be justified:

**NOC is based on the hypothetical cost of investment in a by-pass pipeline. Hence it cannot be considered a tariff determined to meet an allowed revenue target**

**Does not appear that it can be the vehicle for a negative charge** in the event that there is over-recovery of transmission services revenue

The fact that the NOC is proposed to be an **alternative to charges which are revenue recovery charges does not affect that conclusion.**

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## The NTS Optional Charge – Non-compliance, NOC at non-IPs

Decision Letter, Page 9/10

TAR NC requires Ofgem to assess **the cost-reflectivity** of the NOC and its impact on **cross-subsidisation between IPs and non-IPs**.

The NOC is intended to be broadly reflective of the estimated cost of laying and operating a dedicated pipeline of NTS specification.

Ofgem note **deficiencies** in the **cost-reflectivity** of the charge related to **load factor assumptions** and **use of hypothetical straight-line distances that are unlikely to reflect actual pipeline routes**

**The service of the NOC is the standard transmission service.**

The NOC does not reflect the costs of the service—**those costs incurred in making the NTS available.**

Although better managed UNC621C (a capacity-based NOC that is calculated as a discount on the reference price), it is **not apparent that such a discount could be reconciled with the TAR NC**

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## The NTS Optional Charge – Non-compliance, NOC at non-IPs

Decision Letter, Page 9/10

**Proposed distance cap of 60 kilometres** would reduce the number of routes where the NOC may be used but rationale for the choice of distance cap was based on uptake of the existing Optional Commodity Charge

Ofgem concerned that this **does not take account of the real risk of bypass and would enable the NOC to result in favourable tariffs and a cross-subsidy to users who do not represent a real risk of bypassing the NTS**

**Ofgem** do not consider that there is a cross-subsidy between IPs and non-IPs **but remain concerned with the risk of cross-subsidy** between those who can access the NOC compared to those who cannot.



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## The NTS Optional Charge – Non-compliance, NOC at non-IPs

Decision Letter, Page 9/10

UNC0621C proposes enduring 'NOC' arrangements.

Discount to the capacity charge and payment of the NOC instead of the General Non-Transmission Services Revenue Recovery Charge.

The issues around commodity-based tariffs identified above would not apply

Ofgem still have **concerns regarding cost-reflectivity are relevant** to that modification proposal as well.

Ofgem are also concerned that the **availability of NOC entails a cross-subsidy** from those who cannot access it under UNC0621C to those who can.

# UNC621 Ofgem Decision Review – 0670R Considerations

## The NTS Optional Charge – Non-compliance, NOC at IPs

Decision Letter, Page 10

The UNC621 modifications (with the exception of UNC621D) convert the NOC into a capacity-based charge at IPs and hence to that extent complies with the requirement of Article 4(3) TAR NC to levy tariffs for transmission services on a capacity basis.

Ofgem concerns regarding **cost-reflectivity and cross-subsidisation remain.**

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