

## Representation – Modification

### UNC 0728/A/B/C/D (Urgent)

#### Introduction of a Conditional Discount for Avoiding Inefficient Bypass of the NTS

0728	Introduction of a Conditional Discount for Avoiding Inefficient Bypass of the NTS
0728A	Introduction of Conditional Discounts for Avoiding Inefficient Bypass of the NTS
0728B	Introduction of Conditional Discount for Avoiding Inefficient Bypass of the NTS with 28km distance cap
0728C	Introduction of a Capacity Discount to Avoid Inefficient Bypass of the NTS
0728D	Introduction of Conditional Discounts for Avoiding Inefficient Bypass of the NTS

**Responses invited by: 5pm on 26 June 2020**

**To:** [enquiries@gasgovernance.co.uk](mailto:enquiries@gasgovernance.co.uk)

*Please note submission of your representation confirms your consent for publication/circulation.*

<b>Representative:</b>	Debbie Baker
<b>Organisation:</b>	CF Fertilisers UK Limited
<b>Date of Representation:</b>	26 June 2020
<b>Support or oppose implementation?</b>	<p>0728 - Oppose</p> <p>0728A - Oppose</p> <p>0728B – Oppose</p> <p>0728C - Oppose</p> <p>0728D - Support</p>
<b>Expression of preference:</b>	<p><i>If either 0728, 0728A, 0728B, 0728C or 0728D were to be implemented, which would be your preference?</i></p> <p>0728D</p>
<b>Relevant Objective:</b>	<p>0728A:</p> <p><b>c)</b> Positive</p> <p><b>d)</b> None</p>

	0728D: <b>c)</b> Positive <b>d)</b> Positive
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<b>Relevant Charging Methodology Objectives:</b>	0728A: <b>a)</b> None <b>aa)</b> None <b>b)</b> None <b>c)</b> None <b>e)</b> Positive  0728D: <b>a)</b> Positive <b>aa)</b> Positive <b>b)</b> Positive <b>c)</b> Positive <b>e)</b> Positive
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**Reason for support/opposition: Please summarise (in one paragraph) the key reason(s)**

#### **0728:**

The exclusion of any discount to Non-Transmission Services Commodity Charges will increase the likelihood of offtakes bypassing the NTS in instances where it would be disadvantageous to UK customers in general (via overall increases in Transmission and Non-Transmission Charges).

The proposal also fails to reflect the reality of “project clustering”, instead employing a strict point to point relative cost assessment resulting in the imposition of NTS Charges which will be significantly higher than the costs of bypass. Again, this will result in sub-optimal outcomes for UK customers.

#### **0728A**

The proposal fails to reflect the reality of “project clustering”, instead employing a strict point to point relative cost assessment resulting in imposition of NTS Charges which will be significantly higher than the costs of bypass. Again, this will result in sub-optimal outcomes for UK customers. It does, however, include a discount for Non-Transmission Services so does more accurately reflect the costs of bypass than 0728/B/C.

#### **0728B**

The proposal sets an unrealistic distance cap, overestimating the probability of bypass for those offtakes located further from the relevant entry points.

The exclusion of any discount to Non-Transmission Services Commodity Charges will increase the likelihood of offtakes bypassing the NTS in instances where it would be disadvantageous to UK customers in general (via overall increases in Transmission and Non-Transmission Charges).

The proposal also fails to reflect the reality of “project clustering”, instead employing a strict point to point relative cost assessment resulting in the imposition of NTS Charges which will be significantly higher than the costs of bypass. Again, this will result in sub-optimal outcomes for UK customers.

#### 0728C

The exclusion of any discount to Non-Transmission Services Commodity Charges will increase the likelihood of offtakes bypassing the NTS in instances where it would be disadvantageous to UK customers in general (via overall increases in Transmission and Non-Transmission Charges).

The proposal also fails to reflect the reality of “project clustering”, instead employing a strict point to point relative cost assessment resulting in NTS Charges which are significantly higher than the costs of bypass. Again, this will result in sub-optimal outcomes for UK customers

#### 0728D

The proposal takes a more realistic stance on:

1. The probability and cost of bypass. The likelihood of bypass is far greater over relatively short distances, as geological and commercial obstacles will be minimised.
2. The likelihood of “project clustering”. When assessing the costs of bypass, it is evident that where there are two or more offtakes in relatively close proximity, parties will share infrastructure, thereby minimising individual costs. A methodology which assumes that all bypasses will be point to point will by its very nature overestimate actual costs where customers undertake “project clustering” to cooperate to develop common pipeline solutions. This proposal properly reflects the likelihood of “project clustering.”
3. Further, it is essential that any “discount” to standard NTS charges is based on the total cost of shipping and as a result must incorporate Transmission and Non-Transmission Charges. It is incorrect to assume that a customer will only consider Transmission Charges when assessing the potential to bypass and as such any methodology which excludes Non-Transmission discounts will result in sub-optimal outcomes for all GB customers. This proposal properly take Non-Transmission Service Commodity Charges into account.

#### **Implementation:** *What lead-time do you wish to see prior to implementation and why?*

We support implementation in October 2020. Any delay beyond this date will create a very real risk that a number of customers, including CF Fertilisers, will execute plans to bypass the NTS.

We are aware that Xoserve systems have been developed to support implementation of any of the proposals. Given that any delay to the introduction of an Optional Charge will a) impose significant, unwarranted and artificial costs on potential OCC customers; and b) a number of potential OCC customers will implement plans to bypass the network, the result will be damaging to UK industry and inefficient for all GB customers.

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

We singularly support implementation of UNC 0728D. The implementation of this proposal will not generate any development or ongoing costs. Implementation of any of the other alternatives will greatly inflate our transportation costs beyond the costs of bypass.

**Legal Text:** *Are you satisfied that the legal text will deliver the intent of the Solution?*

Yes

**Respondents are requested to provide views on the following points:**

*Q1: Respondents are requested to provide a view as to whether the solution provided within the Modification(s) is fully compliant with the relevant legislation (including, but not limited to, Articles 28-32 of the Tariff Network Code).*

All solutions are compliant with the EU Tariff Network Code. Capacity charges were published by National Grid on 5<sup>th</sup> June. The Modifications propose discounts to the reserve prices based on an ex-post assessment of the eligible amounts, i.e. the discounts are applied to the standard reserve prices.

In the case of Modifications 0718A/D, it is proposed that an additional discount, is provided to eligible amounts from the standard Non-Transmission Services Commodity Charges. These charges are required to be set no later than 30 days before the respective tariff period.

Art 4.2 of the EU Tariff Network Code permits the setting of tariffs to take into account conditions for firm capacity products, which captures the application of Optional Charges.

In the case of Transmission revenue under-recovery caused by the implementation of a Optional Charge, Art 17 requires that such revenue should be minimised, recovered in a timely manner and that differences in tariff levels across two consecutive periods should be avoided to the extent possible. This implies that a Revenue Recovery Charge (RRC) should be applied, in particular during the transition phase if implementation is to be permitted on 1 October 2020. The RRC is consistent with Art 4.3 in that the RRC is a capacity-based tariff.

We note that there is explicit reference to the provision of information related to transmission and non-transmission tariffs in Art 30.1.(c), which sets out those tariffs that can be published up to 30 days prior to the tariff period. A discount applied to Non-Commodity charges as set out in 0728A/D is consistent with this Article and can be published in time to enable a 1 Oct 2020 implementation. In addition, as the RRC is not required to be published in accordance with Art. 29, by extension it is a relevant charge for the purposes of Art. 30.

In the case of Art. 29, the provisions are particular to Interconnection Points (IP) and Points subject to the CAM Code (which is not the case at non-IP points in GB) and as such generally is only relevant where changes to the reserve prices at IPs are required. This is not the case with any of the 0718 Proposals.

*Q2: Respondents are requested to provide views on the proposed implementation date(s).*

Please refer to earlier answer. To prevent inefficient bypass, it is vital that Ofgem implement by October 2020.

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

No

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

### **1. The Cluster Opportunity**

Whilst we are aware that other offtake points do have cluster opportunities, the one we are aware of in detail is at Teesside. At Teesside, there is more than one alternative option for companies working together to effect bypass options. The simplest and quickest option is to reinstitute a pre-existing mothballed pipeline for the benefit of neighbouring sites with high volumes of gas use (0.6% of current national transmission system overall). The pipeline runs along established pipeline corridors linking our sites with the nearest grid entry point at CATS terminal. Potentially this could be part of a wider Teesside cluster approach involving several of the other large gas users using more of the existing pipeline infrastructure. Based on the costs that will be incurred a collective bypass project has the potential to payback within a month or two. This can be implemented within several months of the new charging arrangements. The work that is required is primarily on site and there are no land consenting issues. There is sufficient security of supply available as a consequence of the two gas processing plants and upstream in this location to make this viable short and long term.

### **2. Detailed Assessment of the Need for An Impact Assessment**

We set out below additional analysis as to why Ofgem is not required to carry out an Impact Assessment (IA) for the supported proposals. We consider that this analysis is key to ensuring that the acknowledged urgency of the proposal is maintained.

In summary, we do not believe that the proposal should be regarded as “important” under s. 5A(1) of the Utilities Act 2000 (the Act) such that an IA is required; or in the alternative, if that provision is engaged, the requirement for an IA does not apply because the urgency of the matter makes it impracticable or inappropriate for the Authority to comply with the requirements of s. 5A(1).

By way of context, we understand that the timetable set out in each of the proposals is tight, recommending implementation on 1<sup>st</sup> October 2020. This is however, a direct result of the timing of Ofgem’s decision on UNC0678A (28 May 2020) and Ofgem’s decision to implement 0678A on 1 October 2020 to coincide with the start of the Gas Year. This has restricted industry’s ability to put forward shorthaul product proposals until now. Nevertheless, it is critical that Ofgem works to this accelerated timetable to ensure that users located close to the entry terminals are not forced to take steps to bypass the NTS

in the very short term to avoid being subject to ‘standard’ charges from 1 October 2020. Once such bypass investment decisions are taken and underway, then such users will have committed to arrangements with the associated longer term inefficient bypass impact on the NTS regardless if these changes are set to be implemented in 2021.

### **The proposals do not engage s. 5A(1) of the Act**

Section 5A(1) of the Act, sets out that Ofgem is required to carry out an IA where it is carrying out its functions and it appears to Ofgem that the proposal is important (as defined in s. 5A(2)). The potentially relevant examples of what falls within the definition of important in s. 5A(2) would relate to a *significant impact* on persons engaged in the shipping, transportation or supply of gas, or engaged in commercial activities connected therewith, and the general public.

The proposals are intended to address an impact identified as an aspect of the decision on UNC0678A, in particular the issue identified in para. 7.21 of the MTD letter on those proposals, the risk that bypass of the NTS would increase, with impacts on cost and efficiency. The purpose of the current proposals is to avoid or minimise that risk, thereby mitigating the impact which would otherwise occur. The effect is therefore to avoid or reduce both the extent and the breadth of an impact. We do not believe that the intent of s. 5A(1) is to require IA in cases where the proposal is to mitigate an impact. The distinction between impacts and mitigation appears for example in Ofgem’s IA decision letter of 29 July 2019 on UNC0686. The intention is that the proposed mitigation in this case would take effect at the same time as UNC0678A, thereby mitigating the impact which that change would otherwise have. In these circumstances we believe that the implementation would *not* have a significant impact, as described in s. 5A(2): rather it avoids or reduces the risk of such impact.

In Ofgem’s final decision directing that modification UNC678A be made, as it had done in the MTD, Ofgem noted that:

“preventing inefficient bypass of the NTS, in a targeted, proportionate and compliant manner is, in our view, desirable. Ofgem is committed to working with the industry and the Joint Office of Gas Transporters to facilitate the development and, depending on the assessment and approval process, timely consideration and where appropriate implementation of modification(s) that seeks to address inefficient bypass of the NTS”.

It was also noted in Ofgem’s final decision:

“that the construction or usage of alternative network infrastructure to the NTS which leads to higher costs overall would not represent an efficient outcome”

As set out in UNC728D:

“This Modification takes into account the Impact Assessment and the decision Ofgem has made regarding Modification 06781 and its Alternatives, published on 23 December 2019 and addresses the areas of compliance identified in this decision to ensure compliance with EU Tariff Code (Regulation 2017/460)2” We note that not all of the existing Users who can take advantage of the current shorthaul charge may be eligible for the product set out in the supported proposals and we note that the issue of cross subsidies and socialisation of costs has been raised in relation to the proposals. The proposals do not of themselves of course, cause any impact on those Users, UNC678A



has resulted in this impact. The Users who can take advantage of the proposals would otherwise be expected to make alternative arrangements resulting in all of the costs being met by the remaining Users.

In summary, therefore, the proposals are in fact (only) avoiding a significant impact on certain Users caused by UNC678A and 5A(1) is not engaged.

### **Reasons why an IA is not required**

In the alternative, if Ofgem considers that section 5A(1) is engaged and an IA is on the face of it required, then in these circumstances, Ofgem can and should rely on the remaining provisions of 5A(1) which state that:

*“this section does not apply if it appears to the Authority that the urgency of the matter makes it impracticable or inappropriate for the Authority to comply with the requirements of this section”.*

This provision is reflected and incorporated in paragraph 22 of Ofgem’s Impact Assessment Guidance published on 4 May 2020 (Guidance). Ofgem sets out circumstances in which, even if it considers that a proposal meets the criteria for an IA under Section 5A, it may decide that it is impractical or inappropriate to carry one out.

### *Urgency*

Ofgem has already accepted that the proposals should be granted urgent status. In its decision on this issue on 12 June 2020, Ofgem stated that:

*“In the impact assessment accompanying our final decision on UNC678 we said that under UNC678A (the modification that will be implemented in October 2020), there could be three routes additional to the status quo that may present a credible risk of bypass and this could potentially lead to additional lost transmission revenue (if these three routes choose to bypass the NTS) of £36m. In our final decision on UNC678 we said ‘that the construction or usage of alternative network infrastructure to the NTS which leads to higher costs overall would not represent an efficient outcome’. For these reasons we consider that the urgency request is justified based on the above criterion (i), namely it is linked to an imminent issue that if not urgently addressed may cause a significant commercial impact on certain users. Specifically, it is possible that higher gas transmission tariffs for some users incentivise inefficient bypass of the NTS which leads to higher costs overall.”*

Ofgem has therefore already recognised that the proposals require urgent consideration to avoid inefficient bypass. It has effectively committed to a timescale and a timetable which justifies not carrying out an IA. To determine now that an IA is still required would be inconsistent with this analysis and contrary to Ofgem’s stated intention in the decision on UNC678 that avoiding inefficient bypass is desirable. It would therefore be inappropriate in these circumstances to delay the implementation which the proposals are seeking to address.

The reasons for urgency are in our view consistent with the analysis of why s. 5A(1) is not engaged and still stands even if Ofgem considers the proposals are important.

In addition from an operational perspective, if Ofgem delays its decision on the proposals in order to carry out a further IA, for many companies it could have the same effect as the proposals being rejected. Companies affected by the imminent removal of the current shorthaul charge will need to take steps to begin implementing the construction of or reactivation of offtake bypasses or enter into commercial project arrangements to take advantage of recommissioned existing pipeline networks individually or as a cluster, as is the case in Teesside. Once these business discussions have taken place, contracts entered into and investment costs incurred, these decisions cannot simply be reversed and the impact on the NTS becomes much more significant. This demonstrates clearly that there is practically no available time for Ofgem to carry out a further IA. It also underlines that it is inappropriate for Ofgem to delay its implementation past 1 October, as this is likely to have the effect of frustrating the main purpose of avoiding inefficient bypass. In order to give effect to the purpose it needs to be implemented urgently.

As set out in proposal 0728D and above, the construction and use of such bypasses would be disadvantageous to UK customers in general and result in overall increases in Transmission and Non-Transmission Charges.

We also note paragraph 16 of the Guidance which Ofgem may consider if it accepts that s. 5A(1) is not engaged:

*“...if we consider that the industry has conducted a suitable consultation (or assessment of impacts) and that a further IA by us would not add value, we are unlikely to repeat this exercise and carry out an IA ourselves. By ‘suitable consultation’, we mean one that would take into account the same considerations as we would as part of an IA, where proportionate to the issue at hand.”*

In light of the fact that the impact is caused by UNC678 and these proposals seek to mitigate it, then we believe that Ofgem has all the relevant information that it needs to assess the current proposals. Ofgem carried out an IA in respect of UNC 0678 and its alternatives, and National Grid has carried out a separate consultation on four of the five proposals through GCD12, and that significant analysis has been provided in the proposals themselves. Therefore, Ofgem can reasonably justify not undertaking a further IA.

In summary, given the recognised urgent nature of these proposals, which has been endorsed by Ofgem’s decision to grant them urgent status, and the detailed work has already been undertaken to assess the impacts of more “extensive and universally accessible” shorthaul proposals via the UNC 0678 IA, it is clear that Ofgem can reasonably conclude that carrying out a further IA is not appropriate and will unnecessarily delay the decision making process which has been determined to be urgent.

Finally, whilst Ofgem will be aware that as a public body it is required to act rationally and reasonably and of the importance of ensuring that its decisions are evidence-based, these duties are tempered by a duty to act proportionately. It would be reasonable for Ofgem to conclude that in line with s. 5A(1) and in all of the circumstances set out above that it would not be proportionate to undertake another impact assessment. Ofgem already has the information it would need to make a decision on the proposals and a delay to carry out a IA is not proportionate given the intent to avoid inefficient bypass of the NTS.