

Representation – Modification UNC 0748 (Urgent)

Prospective Removal of Entry Capacity Revenue from Capacity Neutrality Arrangements

Responses invited by: 5pm on 11 December 2020

To: enquiries@gasgovernance.co.uk

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

Representative:	Colin Williams
Organisation:	National Grid NTS
Date of Representation:	11 December 2020
Support or oppose implementation?	Support
Relevant Objective:	<p>c) Positive</p> <p>d) Positive</p> <p>g) Positive</p>
Relevant Charging Methodology Objective:	<p>a) Positive</p> <p>b) Positive</p> <p>c) Positive</p>

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

As the proposer, National Grid NTS supports the implementation of this Modification Proposal.

Since the implementation of UNC Modification 0678A on 1st Oct 2020 the entry Capacity Neutrality mechanism has returned circa £0.5m per day to capacity holders which has contributed significantly to the need for National Grid to levy Transmission Services Revenue Recovery Charges (TSRRCs) from 1st February 2021. The return of such a materially high proportion of Entry capacity revenue to Users disproportionately benefits certain Users, particularly those who do not pay directly to National Grid for their Entry capacity, who receive a proportion of the capacity neutrality redistribution payment and are also not charged the TSRRC.

With the high value of the overall Capacity Neutrality revenue, driven by the increased revenues associated to within day and daily interruptible capacity, National Grid believe the inclusion of these revenues within the Capacity Neutrality process is not fit for

purpose. With these revenues effectively returned under the current regime, this drives an under recovery which requires the use of the TSRRCs to enable National Grid NTS to recover its Allowed Revenue.

The key principal of the charging methodology introduced from 1st October 2020 as a result of UNC Modification 0678A – Amendments to Gas Transmission charging regime is to set reserve prices for *all* capacity at such levels that best facilitate recovery of National Grid NTS' Allowed Revenue. Therefore, return of a material portion of this capacity revenue to Users runs contrary to this principal. The distributional impact will vary across Users depending on how they have booked their capacity. Two examples we highlighted in the Modification, which has been evident in October 2020's data illustrate the varied impacts across Users:

- A User not having Capacity secured by auction (i.e. by trading the capacity in where the liability remains with the original holder) and therefore not paying any Capacity Charges directly to National Grid NTS and receiving a proportion of the Capacity Neutrality redistribution;
- A User procuring a significant proportion of their capacity from Interruptible Capacity whereby the Interruptible Capacity is paid for direct to National Grid however the Interruptible capacity receives no proportion of the Capacity Neutrality revenue as the redistribution is based on each individual User's percentage of firm capacity on a daily basis.

A TSRRC can adjust these positions depending on the applicability to each User. For Entry, the Transmission Services Revenue Recovery Charge (TSRRC) is applied to the aggregate amount of NTS Entry Capacity that a User holds at an Entry Point on a given day "Fully-Adjusted Available Capacity" minus the "Existing Available Holdings", which are defined as User's Available NTS Entry Capacity for such Entry Point and Day as at the Tariff Regulation Effective Date (06 April 2017). Therefore, the impacts will vary across Users, however the Entry TSRRC rate is significantly influenced by the high levels of Existing Available Holdings that do not attract the TSRRC.

The proposal to temporarily permit a reduced notice period for signalling amendments to relevant charges is beneficial to make such changes in the earliest possible timeframe post decision. Further detail is provided in our response to Question 3 at the end of this response.

On this basis, we believe implementation would better facilitate the identified Relevant Objectives and Relevant Charging Methodology Charging Objectives for the reasons we set out in the Proposal.

Implementation:

As set out in the Proposal, implementation should take effect as soon as practicable noting that this should be the first calendar day of a month.

There is a clear need to rapidly address the issues caused by Capacity Neutrality given the materiality of the issue (i.e. the revenue returned to Users that needs to be consequently recovered via the TSRRC) increases incrementally (circa £0.5m per day) for as long as the issue remains unresolved. On this basis, timely implementation will

facilitate a consequential reduction in the TSRRC rate as soon as possible following an implementation decision.

National Grid NTS, in its proposal, also included a transitional arrangement following a positive decision to implement that would allow a temporary and time limited reduction in the notice period for signalling changes to any charges subject to the two months' notice period given in TPD Section B1.8.2(a) that is referenced in TPD Section Y. The proposal and legal text allow this to be less than two months and no shorter than 5 Business Days until the rate becomes effective. In practice National Grid NTS will seek to offer the longest possible notice period following a decision to implement. If this proposal is implemented, for example from January 2021 (i.e. a decision to implement is made in December 2020) then the change to Capacity Neutrality would be effective from 1st January 2021 and National Grid NTS would look to amend the already published TSRRC effective from 1st February 2021.

Impacts and Costs:

As stated in the Proposal, there will be impacts on Gemini and UK Link invoicing systems. The costs of implementation are currently being assessed but are expected to be minor when compared to the benefits of implementation.

If this Proposal is not implemented the current Capacity Neutrality arrangements will continue and the published TSRRC notified on 30th November 2020 will be applied. As mentioned, Capacity Neutrality has resulted in around £0.5m per day being returned to Users and implementation will enable, as highlighted above, a reduction to the TSRRC from February 2021 subject to the timing of a decision.

As mentioned above, the distributional effects of Capacity Neutrality highlighted by scenarios in the Modification proposal have become evident upon further analysis of the October Data and will likely continue without intervention.

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

We are satisfied that the legal text delivers the intent of the solution identified in this Proposal.

Ofgem have requested that parties give due consideration to the following questions:

Q1: Do you agree that the treatment of interruptible and within day firm entry capacities feeding into capacity neutrality is inappropriate?

Yes

Please explain your rationale:

Inclusion of Within Day NTS Entry Capacity and Daily Interruptible NTS Entry Capacity revenues in Capacity Neutrality was predicated on the charging methodology and structure in place at that time for a specific purpose i.e. to ensure that National Grid NTS was neutral to any cash flows related to any Constraint Management costs and relevant

revenues and that these revenues offset such costs for those parties subject to Capacity Neutrality.

The introduction of a new charging methodology which materially differs in structure from that previously in place merits consideration as to whether these arrangements remain fit for purpose. Due to the move to a model whereby the purpose is to recover Allowed Revenue for Transmission Services entirely from capacity based charges, around two-thirds of Entry Capacity Revenue collected in October 2020 was returned to Users via Capacity Neutrality and is therefore not in line with the intentions of the reforms implemented under UNC Modification 0678A.

With the high value of the overall Capacity Neutrality revenue, driven by the increased revenues associated to within day and daily interruptible Entry capacity, National Grid NTS believe the inclusion of these revenues within the Capacity Neutrality process is not fit for purpose. Prior to 1st October 2020 the revenue returned via Capacity Neutrality was typically circa £100k per month. On average, across October and November this is approximately £15m per month.

Q2: Do you agree that these revenues should be removed from capacity neutrality?

Yes

Please explain your rationale:

Based on the rationale stated in response to Q1, we believe the revenues from the identified Entry Capacity products should be removed from Capacity Neutrality arrangements.

Q3: Do you support that National Grid should be granted a one-off relaxation of its obligation to provide two months' notice of pricing changes?

Yes (See the 'Solution' section of the modification)

Please explain your rationale:

As identified above, the materiality of the issue (i.e. the revenue returned to Users that needs to be consequently recovered via the TSRRC) increases incrementally (circa £0.5m per day) for as long as the issue remains unresolved. A TSRRC has been notified to the industry to take effect from 1st February 2021, should this modification be implemented then the Revenue to be recovered will cease escalation.

We recognise the need to maintain price/market stability and confidence which forms the basis of the rationale for the current notice period. Without this proposed reduced timeframe it would mean, for example Entry TSRRCs, could not be updated until at least two months post any decision. Therefore, we are proposing that this notice waiver is only available for a limited period of time (2 months) subsequent to the date of Ofgem's decision.

The proposal allows this to be less than two months and no shorter than 5 Business Days until the rate becomes effective. In practice National Grid NTS will seek to offer the longest possible notice period following a decision to implement. If this proposal is implemented, for example from January 2021 (i.e. a decision to implement is made in December 2020) then the change to Capacity Neutrality would be effective from 1st

January and National Grid NTS would look to amend the already published TSRRRC effective from 1st February 2021 to reflect the change.

Are there any errors or omissions in this Modification Report that you think should be taken into account?

We have not identified any such error or omissions.

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

N/A