

Representation - Draft Modification Report UNC 0765

New retrospective debit and credit charges to reflect changes to the treatment of Entry Capacity Revenue between October and December 2020

Responses invited by: **5pm on 20 September 2021**

To: enquiries@gasgovernance.co.uk

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

Representative:	Jeff Chandler
Organisation:	SSE
Date of Representation:	16/9/21
Support or oppose implementation?	Oppose
Relevant Objective:	<p>c) Negative</p> <p>d) Negative</p> <p>g) Negative</p>
Relevant Charging Objective:	<p>a) Negative</p> <p>b) Negative</p> <p>c) Negative</p>

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

If this modification is implemented it will have damaging consequences for the GB energy market. A retrospective change to the UNC contract will undermine confidence and trust in the GB regulatory regime and may result in higher risk premiums being applied to future investments in the GB market. This increased risk premium arising from the retrospective loss of sanctity of contract would increase costs for customers or reduce investment in GB and consequent de-carbonisation efforts.

The modification fails to further the relevant objectives as claimed by the proposer. This has mainly occurred as the text from UNC 0748, a prospective modification, has been applied to a retrospective modification. Whilst SSE supported 0748 we cannot support 0765, as the relevant objectives will not be furthered because it is impossible to retrospectively unwind the market impact on wholesale prices that occurred as a result of Capacity Neutrality and varying Transmission Revenue Recovery Charges from October 2020 to 30th September 2021. Therefore, claims that competition and compliance can be improved retrospectively for events already passed are easily dismissed. Whereas,

the risk of damage to the credibility of the GB energy market from retrospective change is negative for competition.

The modification suggests that revenue was ‘inappropriately redistributed’ via the capacity neutrality arrangements. Whereas, the revenues flowed according to the rules in place at the time which for capacity neutrality had been in place for 20 years and were well understood. The magnitude of the revenue flows arose following the implementation of UNC 0678A which was approved by Ofgem following extensive consultation and impact assessment. Hence, we conclude that the revenue flows were not inappropriate, rather the market responded according to the contract rules.

Ofgem¹ agrees that past transactions should not be changed, *‘it is our view that retrospective modifications should be avoided as they undermine market confidence. It is a general principle that rules ought not to change the character of past transactions, completed on the basis of the then existing rules’*.

Certainty over the contractual rules that apply to transactions in advance is critical for market stability, with regulatory risk being a key factor in the attractiveness of a market and credibility of the regulatory regime. Ofgem provides written criteria in relation to retrospective proposals as part of its guidance on urgency criteria¹ critiqued below:

1. The issue did not arise from a fault or error in central arrangements / systems. The UNC contract was followed.

2. The Capacity Neutrality issue was foreseen; documented in the FMR² of modification 0621, which raised queries in relation to revenue flows and in the FMR³ of modification 0678 and the associated impact assessment⁴ which flagged changes in booking behaviour.

3. The possibility of retrospective action was not flagged in advance. Rather the proposal was first flagged as a possibility in mid-November but is seeking to apply from the start of October 2020. This technical inconsistency may form a basis for judicial referral of a decision to implement this modification as Ofgem will not have followed its own published guidelines.

It is therefore clear that none of the three criteria are met.

Finally, if implemented this modification is very unlikely to have any impact on a customer’s bill nor have an impact on competition as claimed by the proposer. The work group report fails to provide evidence in this regard and without this evidence it is a bold

1

<https://www.gasgovernance.co.uk/sites/default/files/ggf/Ofgem%20Guidance%20on%20Code%20Modification%20Urgency%20Criteria%2017%20February%202016.pdf>

²<https://www.gasgovernance.co.uk/sites/default/files/ggf/page/2018-07/Part%20I%20Final%20Modification%20Report%200621%200621ABCDEFHJKL%20v3.0.pdf>

³ <https://www.gasgovernance.co.uk/0678>

⁴https://www.gasgovernance.co.uk/sites/default/files/ggf/book/2020-06/unc678_-_final%20impact_assessment_%20May%202020.pdf

assumption. Any re-circulation of monies between Shippers that will occur from this modification will need to find its way to separate suppliers covering a period of three years of financial reporting. As Shippers and Supplier interests have evolved over this period it is unlikely to impact competition, for example during this period SSE has sold its upstream interests and no longer ships for its own account for upstream gas and a number of suppliers have exited the market.

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

If Ofgem was minded to approve this proposal, we expect it should carry out an impact assessment once all the data is available, to quantify and explain how reallocating money between shippers and suppliers over three financial reporting periods, given a six month I.T. implementation period, avoids introducing distortions whilst furthering competition and benefitting consumers. Essentially an impact assessment will need to demonstrate how consumer bills will be impacted.