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cc.:

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13 December 2021

Dear Wanda

## **UNC 0687: Creation of new charge to recover Last Resort Supply Payments**

We are writing to you ahead of the extraordinary UNC Panel meeting on 14 December 2021 to express our concerns about the process being followed for UNC 0687 and the impacts that the uncertainty and timeline for implementation are having on all customers, both domestic and non-domestic.

We previously wrote to Ofgem on 6 December highlighting several issues of concern with the progression of this Modification and its sudden reprioritisation. Ofgem has on 7 December issued a decision letter sending the Modification back to UNC Panel. The letter indicates that Panel will be asked to review and revise the Legal Text of the Modification and resubmit the Final Modification Report to Ofgem with Panel's recommendation. In Ofgem's view this process will "allow a full review of the legal text, in accordance with UNC processes." Ofgem stated that the solution proposed "might not bring the benefits it is expected to",<sup>1</sup> consistent with comments Ofgem made to UNC Panel in 2020 that a different solution would be preferable.<sup>2</sup>

A variation request has subsequently been raised by the original proposer of the Modification on 8 December, which adjusts the calculation formula for the new LRSP charge and makes minor textual changes, including to the calculation examples provided in 2019. Accompanying Legal Text was published on 9 December, including an implementation date of April 2022. It is this revised solution Legal Text that Panel will be asked to review and incorporate in an FMR with recommendation to Ofgem.

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<sup>1</sup> [Ofgem Send Back Letter 0687](#).

<sup>2</sup> Ofgem suggested that different solutions should be reviewed in order to find "a faster, more efficient and more targeted way to recover SoLR customer charges" ([UNC Modification Panel Minutes of Meeting 262 held on Thursday 20 August 2020](#), 262.8 b, p. 9). A solution delivered via the REC was also under consideration ([UNC Modification Panel Minutes of Meeting 265 held on Thursday 19 November 2020](#), 265.9 c, p. 11).

## **Process and materiality**

In Centrica's view for Panel to take a view on the Modification in this manner would not conform to correct UNC process and would set a poor precedent for Code governance. Both the proposal and the circumstances surrounding the issue it seeks to address have changed significantly since the original proposal was submitted. Ofgem delayed its decision for two years since the workgroup developed and analysed the original solution under UNC 0687 in 2019. The material changes in market circumstances due to multiple SoLR events and delayed decision are grounds for the Modification to be subject to wider consultation prior to Panel review of a FMR. The minor changes made to the analysis examples in the variation request text are inadequate given the actual supplier failures that have recently taken place. Analysis in the context of the current situation must be conducted to ensure the Modification solution is robust. The change is clearly material: £877m estimated levy costs are to be recovered from gas consumers via network charges, so the inclusion of a worked example for £5m in the modification report fails to highlight to market participants the impact of the change.

Further analysis and industry consultation is required on the Modification and this is consistent with principles of good governance. Modifications should be subject to industry scrutiny prior to Panel recommendation, to ensure Panel has adequate analysis to inform its discussion and decision; it is not Panel's role to develop modifications nor conduct analysis.

## **Legal Text**

The Legal Text provided makes reference to the conditions of 0687V applying to claims received in accordance with Standard Special Condition A48 of the Transporter Licence.<sup>3</sup> This licence condition requires claims to be submitted prior to 31 October for recovery of funds by the transporter in the following regulatory year (i.e. from April 2022). In its letter of 1 December Ofgem made clear that in the current exceptional market circumstances, it would be in the consumers' interest for GDNs to process claims made after 31 October and they will not be subject to enforcement action in this case.<sup>4</sup> However, 0687V does not permit GDNs to recover these December 2021 processed claims via their charges until 2023/24. If the intention is for sums to be charged from April 2022, this is counter to the Transporter Licence.

This issue is clearly material and representative of the benefit of further analysis and review of this Modification in the current exceptional situation.

We also note that the revised modification now includes an April 2022 implementation date as part of the revised legal text. Whilst we understand the proposer's desire is to have the change implemented in April 2022, it is neither necessary to include the date to deliver the stated reason for the variation, nor is it appropriate for the legal text to seek to remove the Authority's discretion on implementation timings.

## **Market expectation and customer (domestic and non-domestic) impacts**

GDNs published indicative charges on 1 November and included £877m of assumed SoLR levy cost to be recovered using the existing SoLR recovery method. Whilst all GDNs included commentary regarding the uncertainty surrounding the final level of SoLR claims, none indicated any uncertainty surrounding the method of recovery.

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<sup>3</sup> [Legal Text 0678V \(9 December 2021\)](#), ¶11.1, p.2.

<sup>4</sup> [Decision letter on supplier of last resort levy claims, 1 December 2021](#).

Usually, a methodology change creating such a significant transfer of cost from one market segment to another would be clearly signalled to the market at least 12 months or more in advance (e.g. CMP308: Removal of BSUoS Charges from Generation) to ensure that participants can properly reflect the change in commercial contracts with non-domestic customers and consumer fixed price tariff contracts.

Therefore, market participants had legitimate expectations that the methodology used for indicative charges would be used for the recovery of the final amount of SoLR levy claims and proceeded to price their contracts accordingly.

Uncertainty created by this revised modification is leading to poor outcomes for all customers, domestic and non-domestic, since we are now in a situation where a non-domestic supplier acting prudently will need to assume that the modification is not approved, whilst a domestic supplier acting prudently will need to assume that the modification is approved i.e. overall customers entering into contracts will be over paying until the final decision, regardless of what that final decision is. Further, due to non-domestic suppliers pricing on the existing methodology, should the revised modification be approved and implemented in April 2022, non-domestic suppliers will be afforded a competitive advantage over domestic suppliers as their prices will be higher than the revised charges.

These are consequences of the insufficient notice provided by the proposed implementation date of April 2022 and we would expect the Panel, and the Authority, to take these issues fully into account when assessing the merits of the modification.

### **Xoserve change solution**

We also have concerns about the Xoserve change solution proposed to implement the Modification. There is inherent risk in the Xoserve system change option proposed: firstly, it is a workaround rather than a complete solution, and secondly it was not part of the Final Modification Report<sup>5</sup> and has not been given adequate assessment. Thirdly, Xoserve itself has flagged in recent days that: *“there is a significant amount of change planned between January and April 2022. This brings inherent risk into our delivery and support of critical production services and processes”*.<sup>6</sup>

If Ofgem is minded to approve UNC 0687, a short-term workaround solution is not suitable for recovery of such a large sum. Procedurally, implementation should be delayed until a robust enduring solution can be delivered for the systems change, properly assessed by industry, and introduced at a point in time when it can be managed adequately by the provider.

### **Summary**

Changes to market conditions since UNC 0687 was originally proposed, and the updated proposals, including the Xoserve system change solution, constitute a material variation and therefore the Modification must be sent back for further analysis by work group and subject to further consultation by industry pursuant to the UNC modification process, to do otherwise would constitute a material process failing. It is imperative that a robust implementation solution is identified and implemented at a time when market participants can respond accordingly.

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<sup>5</sup> [UNC 0687 Final Modification Report](#), p. 9. Three change options are outlined and do not include the proposal to add a new charge type to a RTB invoice presented in December 2021 as option 4.

<sup>6</sup> [Post-meeting brief DSC Change Management Committee \(10 December 2021\)](#)

Panel must then review the further work group analysis and output of the consultation before issuing a new Final Modification Report for recommendation for approval by Ofgem.

Otherwise, Ofgem would be taking a decision on proposals that materially differ from what has been submitted under the current Final Modification Report, and the new proposals have not been adequately consulted upon. The new proposals without further analysis and consultation are not on their own the right solution, particularly given current market conditions, and ultimately would be contrary to Ofgem's statutory duties including the promotion of effective competition.

Ofgem must have sufficient information relating to the impact of the Modification on which to base any decision to approve, and Ofgem must review the proposals in the context of substantially different market conditions to that in play two years ago. The way in which the Modification is implemented is integral to its impact, and it would be unreasonable to expose stakeholders to indicative LRSP charges of £877 million without appropriate consultation.

Any decision to approve UNC 0687 without further analysis and further consultation would be vulnerable on appeal.

Please get in contact if you require any clarification of the issues raised.

Yours sincerely

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