

UNC Draft Modification Report	At what stage is this document in the process?
<h1 data-bbox="134 322 655 412">UNC 0847:</h1> <h2 data-bbox="134 450 1177 589">Introduction of a Minimum General Non-Transmission Services Charge</h2>	<div data-bbox="1209 315 1477 636"> <div data-bbox="1209 315 1477 394">01 Modification</div> <div data-bbox="1209 394 1477 472">02 Workgroup Report</div> <div data-bbox="1209 472 1477 551">03 Draft Modification Report</div> <div data-bbox="1209 551 1477 636">04 Final Modification Report</div> </div>
<p>Purpose of Modification:</p> <p>This Modification Proposal seeks to introduce a minimum General Non-Transmission Services Charge of 0.0001p/kWh into UNC TPD Section Y to provide consistency with other charges and provide certainty that negative or zero charges cannot happen.</p>	
<p>Next Steps:</p> <p>This Draft Modification Report is issued for consultation responses at the request of the Panel. All parties are invited to consider whether they wish to submit views regarding this Authority Direction Modification.</p> <p>The close-out date for responses is 11 September 2023, which should be sent to: enquiries@gasgovernance.co.uk. A response template is available at http://www.gasgovernance.co.uk/0847.</p> <p>The Panel will consider the responses and agree whether or not this Modification should be made.</p>	
<p>Impacted Parties:</p> <p>High: Shippers, National Gas Transmission</p>	
<p>Impacted Codes:</p> <p>None</p>	

Contents		?	Any
1	Summary	3	questions?
2	Governance	4	Contact: Joint Office of Gas Transporters
3	Why Change?	4	
4	Code Specific Matters	7	 enquiries@gasgovernance.co.uk
5	Solution	7	
6	Impacts & Other Considerations	7	 0121 288 2107
7	Relevant Objectives	11	Proposer: Ashley Adams National Gas Transmission
8	Implementation	12	
9	Legal Text	12	
10	Recommendations	13	 Ashley.Adams@Nationalgas.com
11	Appended Representations	13	
Timetable		 07377135875	
Modification timetable:		Transporter: Colin Williams National Gas Transmission	
Pre-Modification Discussed	02 May 2023		
Date Modification Raised	05 May 2023		
New Modification to be considered by Panel	18 May 2023	 Colin.Williams@nationalgas.com	
First Workgroup Meeting	06 June 2023		
Workgroup Report to be presented to Panel	17 August 2023		
Draft Modification Report issued for consultation	18 August 2023	 07785 451776	
Consultation Close-out for representations	11 September 2023	Systems Provider: Xoserve	
Final Modification Report available for Panel	14 September 2023		
Modification Panel recommendation	21 September 2023	 UKLink@xoserve.com	

1 Summary

What

Due to the way in which General Non-Transmission Services Charges are calculated there exists, under certain circumstances, a possibility that the methodology could produce a negative General Non-Transmission Services charge. The risk of this occurring has been very low historically as a result of more stable costs and the timing of when revenues and charges were updated (i.e. within a charging year). A minimum price is not therefore a feature of General Non-Transmission Charges; however, this does exist for Transmission Services Entry and Exit Capacity reserve prices. More recently, the likelihood of negative General Non-Transmission Charges occurring in future (specifically those applicable from 01 October 2024) for has increased.

National Gas Transmission will, with stakeholder support, develop solutions over the coming months to address the wider issues with Non-Transmission charging that have become more apparent in light of recent events. These include but are not limited to the potential for negative charges. The implementation of such measures, some of which are highlighted in the “why change” section, while not solely focused on preventing negative charges, will significantly reduce the possibility of them materialising.

This Proposal will introduce a minimum General Non-Transmission Service Charge of 0.0001p/kWh which will come into effect should the measures mentioned above not have the desired outcome. This will provide certainty to Stakeholders that negative charges are not able to materialise under any circumstances via an explicit prohibition in UNC. It also provides consistency with Transmission Services Entry and Exit Reserve prices where there already exists a minimum price.

Why

Non-Transmission charges are designed to collect the majority of National Gas Transmission’s System Operator Revenue. As a result of higher costs than allowances in the Allowed Revenues and the timing of when revenues (and therefore charges) can be updated, the General Non-Transmission charge that will be applicable from 01 October 2023 is forecast to increase substantially. Based on current indicative values, without intervention, this would be followed by a large decrease in the General Non-Transmission charge applicable from 01 October 2024 which creates a potential for negative charges. This increased risk of negative charges has led National Gas Transmission to raise this Modification to provide stakeholders with certainty that they will not be able to materialise.

Introducing a minimum General Non-Transmission Services charge will also bring the General Non-Transmission Services charge in line with the primary Transmission Services charges in this respect, where there already exists minimum Entry and Exit Capacity Reserve Prices.

If negative General Non-Transmission Services Charges were allowed to materialise, they would result in National Gas Transmission paying its customers to flow gas on the NTS. This would create a perverse incentive for users to flow gas which would in turn likely drive unpredictable behavioural changes, which could have serious and far-reaching impacts for all Stakeholders.

How

This Proposal will form part of a larger strategy to address the wider issues with Non-Transmission charging and prevent negative charges materialising. The primary mitigations to the risk of negative charges are detailed in the why change section of this Proposal. However, should these methods not be approved, or have the desired effect, this Proposal will serve as a failsafe, ensuring that negative prices are not permitted to materialise under any circumstances via the insertion of a minimum General Non-Transmission Services charge of 0.0001p/kWh into UNC.

2 Governance

Justification for Authority Direction

This Proposal seeks to insert a minimum General Non-Transmission Services charge into UNC which would, if used, intentionally increase the charge to a number greater than the negative value produced via the methodology. This would create an overcollection of revenue during a given Formula Year (01 April to 31 March inclusive). Although this overcollection would be passed back to users via the normal processes and a reduction in the charge for the following year, it could materially alter the costs that are passed on to consumers in any given year. The Proposer is therefore of the view that there is sufficient materiality to require a decision from the Authority.

Requested Next Steps

This Modification should be considered a material change and not subject to Self-Governance.

Workgroup's Assessment

Workgroup Participants did not disagree.

3 Why Change?

The principal objectives of this Proposal are to provide certainty that General Non-Transmission Services charges cannot be negative or zero and to provide consistency by bringing the principal Non-Transmission Services charge in line with the two principal Transmission Services charges where there are existing minimum Capacity Reserve Prices for Entry and Exit Capacity. This is in keeping with the principle that National Gas Transmission provides a service to its customers via the transportation of gas through the NTS and that there is a charge for using this service. Negative charges, if they were to materialise, would result in National Gas Transmission paying Users for the injection or offtake of gas from the NTS creating a perverse incentive for Users to flow. This incentive would likely drive behavioural changes and associated impacts that would be both difficult to predict and have the potential to cause considerable further issues.

Drivers of Negative Charges

Negative charges are driven by volatility in the System Operator Allowed Revenues that National Gas Transmission collects in accordance with its Gas Transporter Licence and the processes and methodologies that dictate what inputs feed into the Allowed Revenues and when, and how these are used to determine charges. There are therefore a number of factors which, in combination, have led to the increased likelihood of negative General Non-Transmission Services charges. These include:

Volatility in the wholesale gas price

National Gas Transmission is required to procure Shrinkage gas. This is gas which is used in connection with the operation of the NTS or which is unaccounted for as offtaken from the NTS. The volatility in the wholesale gas price over the past 18 months and the generally increased prices that the market has experienced during that period has resulted in a significant increase to the Shrinkage costs incurred by National Gas Transmission. As National Gas Transmission is cash neutral to Shrinkage costs, these additional costs are passed through to customers via increased Allowed Revenues and subsequently higher General Non-Transmission Services charges. Volatility in the wholesale gas price therefore has a significant impact on the volatility of the General Non-Transmission Services charge.

The timing of when costs can be included into Allowed Revenues and charges

Prior to a recent Licence change, which allows for a later submission of the PCFM (Price Control Financial Model), the PCFM could be republished at the latest in January of any given year. The PCFM forms the basis on which revenues are set for the following Formula Year (01 April to the following 31 March inclusive), and on which charges are subsequently set for the following Gas Year (01 October to the following 30 September inclusive). PCFM republication in January meant that many of the cost inputs that feed into the process used values from towards the end of the prior calendar year. Charges applicable from any given October were therefore formed using data and forecasts that were 10-12 months old by the time that these charges were to come into effect. This allowed for significant changes in costs and forecasts between the time that they were produced and the time when their outputs came into effect.

The result of this has been to exacerbate the volatility in Allowed Revenues. As costs and cost forecasts increase, as they did, for example, with the outbreak of the war in Ukraine in February 2022, there was no facility to incorporate these into Allowed Revenues until the following April. This resulted in a period where the costs incurred by National Gas Transmission were much higher than what it could collect through the Allowed Revenues and therefore cost inputs being stored up for the following year. Allowed Revenue forecasts for the following Formula Year (01 April 2023 to 31 March 2024 inclusive) increased significantly to include both the increased costs expected to be incurred during that year and also the reconciliation of the additional costs that were unable to be recovered in the prior year. Indicative Allowed Revenues and charges applicable from April 2023 and October 2023 respectively therefore increase significantly in comparison to the prior years.

The Licence change which came into effect on 10 April 2023 moves the PCFM resubmission backstop date back from January to May. Although this recent change will bring significant improvements to the process going forwards, it does not have any effect on previous years which have contributed to the issues.

Revenues set for a Formula Year and charges set for a Gas Year

National Gas Transmission is entitled to recover a specified Allowed Revenue over a Formula Year (01 April to the following 31 March inclusive). However, charges are set for a Gas Year (01 October to the following 30 September inclusive). One of the effects of this offset (and the method of Gas Year Allowed Revenue determination described below) is that if a spike in costs, and therefore revenues, is experienced in one year and followed by a decrease the following year, high charges can remain in place for a period of six months after Allowed Revenues have decreased. For example, if Allowed Revenues for the Formula Year that begins in April of year Y are higher, due to the requirement to collect additional costs incurred by National Gas Transmission, the charges applicable for the Gas Year that begins in October of year Y will be higher (all else being equal). If the Allowed Revenues for the following Formula Year, beginning in April of year Y+1 decrease, charges will not decrease until the October of year Y+1. This leaves a six month period where higher charges are in place but revenue values are lower.

Method of Gas Year Allowed Revenue Determination –

The existing mechanism for determination of Allowed Revenue due to be collected over the course of the Gas Year (as set out in the NTS Transportation Charging Methodology) only takes into account the Allowed Revenue for the Formula Year which ends in the relevant Gas Year, without taking account of the Allowed Revenue for the following Formula Year (the first half of which coincides with the latter half of the relevant Gas Year). There is therefore a requirement when setting charges to calculate the Allowed Revenue for any given Gas Year from the two-part formula years that fall within it.

Part of the methodology used to determine the Allowed Revenue for the Gas Year subtracts what has been collected in the first six months of the Formula Year away from the total to be collected for that Formula Year to establish what is left to be collected. If the charges for the Gas Year beginning October of Year Y are very high and if the Allowed Revenues for the Formula Year beginning Y+1 reduce significantly, the revenue collected

within the first six months for the Formula Year beginning April of year Y+1 could be greater than the Allowed Revenue for the entirety of that year. This would result in a negative target revenue for the Gas Year beginning October Y+1 and thus the methodology would provide a negative price.

An illustration of how these drivers combine to result in a potential negative General Non-Transmission Services charge applicable from October 2024 (should no intervention be taken) can be seen in figures 1 and 2.

How do Negative Charges Materialise?

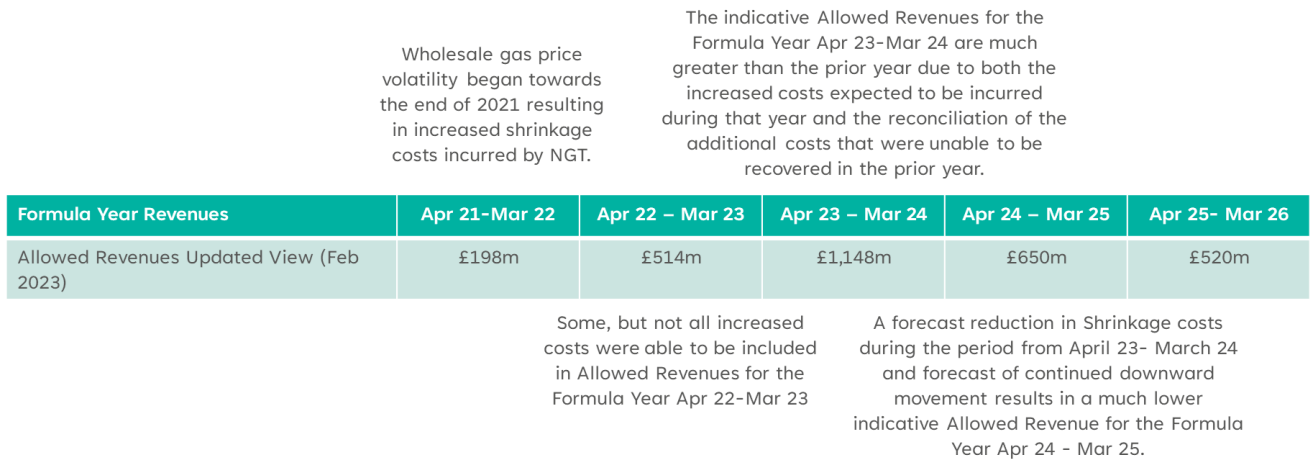


Figure 1. Indicative view of Non-Transmission Allowed Revenues using information available as of February 2023

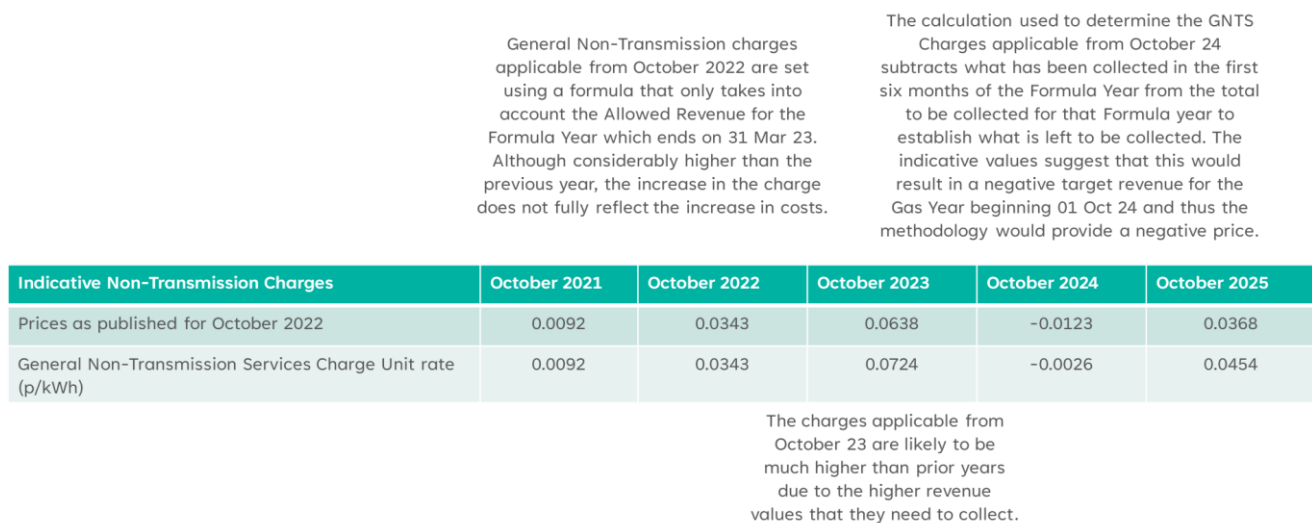


Figure 2. Indicative view of General Non-Transmission Services Charges published for October 2022 and latest view as of February 2023

Wider Strategy

This Proposal forms part of National Gas Transmission’s wider strategy to prevent zero or negative prices. It is designed to work in a complimentary way, and no way inhibit other improvements in this area which have already been developed or will be developed in future. It will ensure that the minimum allowable General Non-Transmission Services charge under any circumstance is 0.0001p/kWh, this is the minimum possible positive charge that can be levied within the system and will act as a final mitigation should the primary mitigation methods fail to prevent negative prices. These primary mitigation measures include:

- **A change to the PCFM republication backstop date from January to May¹.** This change to National Gas Transmission's Gas Transporter Licence was implemented 10 April 2023 and will allow for more timely updates to Revenues in future years. This strikes a balance between reducing the scope for costs to change materially within the time frame and providing the industry with certainty of what tariffs shall be for the following Gas year with sufficient notice ahead of those tariffs coming into effect.
- **The consideration of a deferral of a sum of revenue from the Formula Year 01 April 2023 to 31 March 2024 inclusive into the following year.** Any deferral of revenue will apply a downward pressure on the price applicable from October 23 and an upward pressure on the price applicable from October 24 (when we first foresee the risk of negative charges occurring). A decision will be made in July 2023, using the latest information available at the time on the requirement for any deferral and any sum that is to be deferred.
- **A commitment to explore and develop more enduring solutions with Stakeholders for 2024 and beyond.** A range of initial options to bring closer alignment of costs and revenues which will in turn reduce the risk of negative prices were presented to stakeholders via an industry webinar which is available to view on National Gas Transmission's website². These solutions will be explored and developed further in the coming months with a plan to implement ahead of charge setting for the Gas Year beginning 01 October 2024

4 Code Specific Matters

Reference Documents

[UNC TPD Section Y](#)

5 Solution

It is Proposed that an additional paragraph is appended to UNC TPD Section Y to mandate a minimum General Non-Transmission Services Charge of 0.0001p/kWh.

Should the methodology for the calculation of the General Non-Transmission Services charge produce a zero or negative value, the implementation of this Proposal would result in instead applying a value of 0.0001p/kWh. If, as part of applying this methodology, it would result in an over-recovery relative to the System Operator Allowed Revenue, it should be noted that this is permitted as per National Gas Transmission's Gas Transporter Licence providing explicit permission is granted by the regulator.

6 Impacts & Other Considerations

Does this Modification impact a Significant Code Review (SCR) or other significant industry change projects, if so, how?

None

¹ <https://www.ofgem.gov.uk/publications/decision-modifications-gas-transporter-licence-held-national-grid-gas-plc>

² <https://www.nationalgas.com/charging/transmission-system-charges>

Consumer Impacts

There will potentially be an impact on different consumer groups should a minimum price be required as National Gas Transmission would potentially over recover against allowed revenue within a given year. However, this would be purely for the intention of avoiding more substantial impacts that negative prices could bring and any negative impact on Consumers bills will be outweighed by the avoidance of negative charges. Additionally, any over-collection of revenues as a consequence of a charge which is increased to 0.0001p/kWh would be offset by a reduction in the charge for the following Gas Year. In practice, this change will only be required should other mitigations fail to prevent negative pricing. It will provide certainty to consumers that negative charges, and the associated impacts can not materialise.

What is the current consumer experience and what would the new consumer experience be?

Impact of the change on Consumer Benefit Areas:	
Area	Identified impact
<p>Improved safety and reliability</p> <p>No Impact</p>	None
<p>Lower bills than would otherwise be the case</p> <p>Although, if required, the minimum price would increase the General Non-Transmission Services charge for the period of a year, this Proposal would not change the Allowed Revenues for any given year. Thus, any overcollection due to a minimum price would be distributed back to Users via lower tariffs than would otherwise be the case in the following year.</p>	None
<p>Reduced environmental damage</p> <p>No Impact</p>	None
<p>Improved quality of service</p> <p>No Impact</p>	None
<p>Benefits for society as a whole</p> <p>No Impact</p>	None

Cross-Code Impacts

None identified.

EU Code Impacts

None identified.

Central Systems Impacts

No system changes are foreseen to be required.

A Workgroup Participant identified that avoidance of negative charges may in fact remove the need for system changes and without this Modification being implemented there may be a need for system changes.

Performance Assurance Considerations

None identified by the Workgroup.

Initial Representations.

None Received.

Panel Questions

None raised.

Workgroup Impact Assessment

A Workgroup Participant, whilst welcoming this Proposal, observed that this is a ‘fix’ which does not address the more fundamental problems that can lead to volatility of prices. In addition, the discretionary nature of some of the other mechanisms for dealing with volatility, such as NGT proposing to defer revenue recovery, leads to greater uncertainty for customers.

A Workgroup Participant, whilst welcoming this proposal, asked whether NGT is still anticipating the possibility of negative charges in 2024. The Proposer confirmed that by the time this Proposal concludes its Workgroup assessment NGT will have published the July 2023 Pricing information so parties will have a clearer view.

At the August meeting NGT pointed out that it has proposed to defer a portion of revenue and that this has a mitigating action for 2024. However, the Proposal is still valid as it is made to provide certainty that GNTS charges cannot become negative under any circumstances.

A Workgroup Participant asked whether an over-recovery of allowed revenues would occur if the collar price is applied as that would appear to breach the Licence. The Proposer acknowledged that in such circumstances, it could occur, but that explicit Authority consent would be required and that any monies so collected would be ‘ring-fenced’ against the System Operator and would be considered in setting the prices for the following year.

A Workgroup Participant observed that if Ofgem approves this Proposal then it appears to create an obligation for it to also grant the Licence derogation if the collar acts to cause a potential over-recovery. Another Workgroup Participant asked what would happen should Ofgem refuse to permit the over-recovery that this modification appears to enable. The Proposer responded that in this unlikely event, NGT would have to seek an urgent Code modification to avoid the breach of its Licence.

NGT provided the following illustrations to show the effect of the Proposal on future prices noting that all figures used are indicative only. The tables show the half-year periods (as requested by Workgroup Participants) illustrating the overlap effects of Gas Year and Formula Year periods.

Example based on current methodology

Current Methodology	Apr 23-Sep 23	Oct 23-Mar 24	Apr 24-Sep 24	Oct 24-Mar 25	Apr 25-Sep 25	Oct 25-Mar 26	Apr 26-Sep 26
GNTS Charge (p/kWh)	0.0343	0.0536		-0.0024		0.0483	
Entry and Exit Commodity Revenue	291,814,259	565,645,414	431,979,637	-24,307,418	-18,566,935	475,834,878	371,355,322
Non-Obligated	8,495,867	8,495,867	8,495,867	8,495,867	8,495,867	8,495,867	8,495,867
St Fergus	32,663,848	42,731,367	32,663,848	42,731,367	32,663,848	42,731,367	32,663,848
Total Recovered Revenue (6 months)	£332,973,973	£616,872,648	£473,139,351	£26,919,816	£22,592,779	£527,062,112	£412,515,037
Recovered Revenue (FY)	£949,846,621		£500,059,167		£549,654,891		

Figures for Oct 24 based on the current methodology suggest a negative price would be required to collect the target revenue for the overlapping formula year.

Please note the following caveats:

- These tables are for illustrative purposes only.
- The General Non-Transmission Services Charge applicable for Gas Year 23/24 will be published towards the end of July 23
- The underlying data behind these numbers are subject to change (forecasts for 23/24 are to be updated before price setting in July)

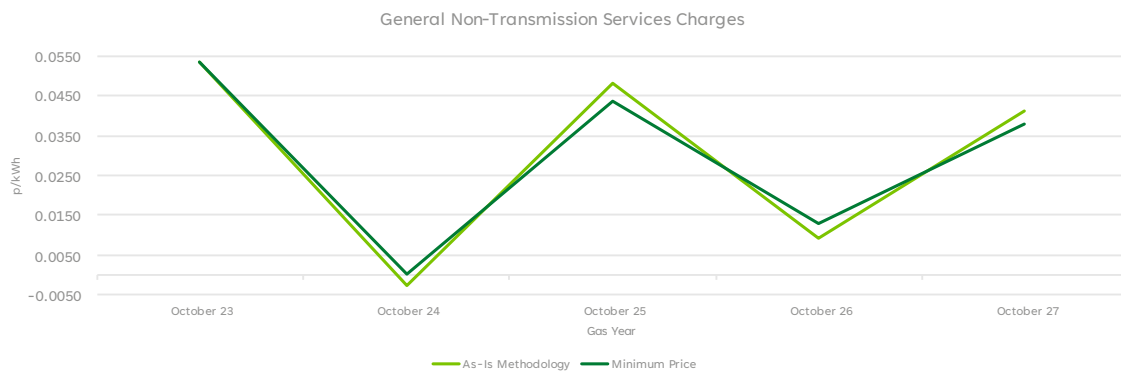
Example rates calculated under a minimum price methodology

Minimum Price	Apr 23-Sep 23	Oct 23-Mar 24	Apr 24-Sep 24	Oct 24-Mar 25	Apr 25-Sep 25	Oct 25-Mar 26	Apr 26-Sep 26
GNTS Charge (p/kWh)	0.0343	0.0536		0.0001		0.0438	
Entry and Exit Commodity Revenue	291,814,259	565,645,414	431,979,637	1,012,809	773,622	431,502,436	336,757,000
Non-Obligated	8,495,867	8,495,867	8,495,867	8,495,867	8,495,867	8,495,867	8,495,867
St Fergus	32,663,848	42,731,367	32,663,848	42,731,367	32,663,848	42,731,367	32,663,848
Total Recovered Revenue (6 months)	£332,973,973	£616,872,648	£473,139,351	£52,240,043	£41,933,337	£482,729,670	£377,916,715
Recovered Revenue (FY)	£949,846,621		£525,379,394		£524,663,006		

In this scenario, application of a minimum price of 0.0001p/kWh for Oct-24 results in an over-collection of approx. £25m, an additional 5% compared with expected revenues.

This over collection is ringfenced and returned to Users via the GNTS charges in the following year. In this illustration the charge for GY 25 is 0.0438p/kWh as opposed to 0.0483p/kWh under the original methodology.

Examples Rates calculated under minimum price methodology



Overall, the application of the minimum price has a slight smoothing effect on the rates across future years. Any over collection of Revenue, when setting prices, requires Ofgem permission as part A of Special Condition 2.1 (Transportation owner revenue restriction) of National Gas' Licence. This does not preclude any additional actions from being taken prior to Oe23 price setting.

7 Relevant Objectives

Impact of the Modification on the Transporters' Relevant Charging Methodology Objectives:

Relevant Objective	Identified impact
a) Save in so far as paragraphs (aa) or (d) apply, that compliance with the charging methodology results in charges which reflect the costs incurred by the licensee in its transportation business;	None
aa) That, in so far as prices in respect of transportation arrangements are established by auction, either: <ul style="list-style-type: none"> (i) no reserve price is applied, or (ii) that reserve price is set at a level - <ul style="list-style-type: none"> (I) best calculated to promote efficiency and avoid undue preference in the supply of transportation services; and (II) best calculated to promote competition between gas suppliers and between gas shippers; 	None
b) That, so far as is consistent with sub-paragraph (a), the charging methodology properly takes account of developments in the transportation business;	Positive
c) That, so far as is consistent with sub-paragraphs (a) and (b), compliance with the charging methodology facilitates effective competition between gas shippers and between gas suppliers; and	None
d) That the charging methodology reflects any alternative arrangements put in place in accordance with a determination made by the Secretary of State under paragraph 2A(a) of Standard Special Condition A27 (Disposal of Assets).	None
e) Compliance with the Regulation and any relevant legally binding decisions of the European Commission and/or the Agency for the Co-operation of Energy Regulators.	None

b) That, so far as is consistent with sub-paragraph (a), the charging methodology properly takes account of developments in the transportation business;

Historically a negative General Non-Transmission Charge was not something that was deemed to be possible and there was therefore no requirement for a minimum charge to be inserted into UNC. However, due to the unprecedented changes that have occurred in the gas market in recent times, there is now material potential for negative charges to materialise if no intervention is taken. The changes proposed within this Modification are expected to provide certainty that negative charges will not occur thus ensuring that the charging methodology properly takes account of recent developments in the transportation business.

Workgroup Assessment of Relevant Objectives

Workgroup Participants did not disagree with this justification.

A Workgroup Participant observed that whilst not identified above, this Proposal may act to avoid costs for system changes (if these were to be required to cope with negative charges) and thus may satisfy Relevant Objective c) Efficient discharge of the licensee's obligations.

8 Implementation

No implementation timescales are proposed. However, in order to maximise the potential of this Proposal implementation is required in advance of setting the General Non-Transmission Services charges applicable from 01 October 2024. These charges are set in July 2024. A decision would therefore be required before the end of June 2024 to facilitate implementation ahead of the July deadline.

If a decision to implement is not received in time for the Non-Transmission charge setting for the Gas Year beginning 01 October 2024, implementation could be 21 days after any decision to implement but the benefit for the Gas Year beginning 01 October 2024 would not be realised.

At the August meeting Workgroup Participants noted that the proposed deferral of revenue by NGT has mitigated the risk however NGT maintain that it would be helpful to see implementation of this Modification prior to the charge setting for October 2024.

9 Legal Text

Legal Text has been provided by National Gas Transmission and is reproduced below.

Workgroup Assessment

The Workgroup has considered the Legal Text and is satisfied that it meets the intent of the Solution.

Text Commentary

This Modification seeks to introduce a minimum General Non-Transmission Services Charge of 0.0001p/kWh/day into UNC.

This is achieved with the changes to UNC TPD Section Y paragraph 4.7.3 outlined below. Stating that the General Non-Transmission Services Charge will be the greater of NANTSR_y / FANQ (the current methodology) and 0.0001 ensures that if the current methodology produces a charge that is below 0.0001 then the value of 0.0001 will be used instead.

Text

4.7.3 The General Non-Transmission Services Charge for a Gas Year (GNTSC_y, to be expressed in p/kWh) ~~will be determined as follows~~ **will be the greater of:**

GNTSC_y=

- (i) NANTSR_y / FANQ_y; **and**
- (ii) **0.0001**

where, for Gas Year y:

NANTSR_y is Net Allowed Non-Transmission Services Revenue;

FANQ_y is Forecast Aggregate NTS Quantity

10 Recommendations

Panel's Recommendation to Interested Parties

The Panel have recommended that this report is issued to consultation and all parties should consider whether they wish to submit views regarding this Self-Governance Modification.

11 Appended Representations

Initial Representation – None