Gas Transmission

St Fergus:

Cost Recovery

3rd May 2022

nationalgrid

Draft Discussion Matrix

St Fergus Discussion Matrix

		Full Socialisation	Degrees of Targeting	Targeting
		None	To be discussed	NSMP Entry
Scope of Charges	Which works are included in the charges and scope of Targeting			
Allowances	Identifying allowances associated with the works			
Cost Recovery	Options for how charges could be recovered, and which users will be responsible			
Under/Over Recovery Process	Reconciliation of recovered charges against costs			
Timescales	Timing of charging/recovery			

Consultation - We asked:

Cost targeting

4. Do you support targeted charging where there is demonstrable localised benefits that should be borne by a targeted group of parties / customers?

   a. Please give your reasoning for your answer

Consultation - You told us (summary):

- Respondents views:
  - Of the ten responses to this question three were against targeted charging and one felt there were pros and cons of targeted charging suggesting that moving away from socialised costs represented a high hurdle to overcome.
  - Four respondents were supportive and one was broadly supportive but suggested that a charge should be based on a market rate for compression and one was concerned about the wider market impacts which required further analysis.
  - In addition, although not directly responding to the question, one respondent felt that NSMP were in the best position to decide on the level of investment required.

Consultation - We asked:

Cost targeting

5. If you believe the charge should be targeted, to what degree should this targeting take place i.e. users at entry, users at exit, users at NSMP sub-terminal or some distance-related charge?

Consultation - You told us (summary):

- Respondents views:
  - The three respondents who were against targeted charging confirmed that they felt there should be no degree of targeting. In addition one respondent felt that the transmission system, including compression, benefits both entry and exit network users and there is no case from departing from the generally applied split, currently 50:50. A similar comment was received from another respondent who felt that the transmission system benefited both entry and exit users and did not support a distance related charge.
  - Of those who supported the targeted charge they all felt that this should be targeted at those benefiting from the service i.e. users at the NSMP sub-terminal.

You told us:

Of those that weren't supportive of targeted charging, the following reasons were given:

- It would cut across the single pricing methodology currently in force
- It would result in distortions in the market with unpredictable long-term consequences
- No demonstrable benefits
- Impinges on NG licence
- Less gas and lower security of supply
- Consumers ultimately bear the cost
- The entry point could become uncompetitive to others e.g. Easington
- Barrier to new investment in new fields
- Upgrades should be paid by all consumers and daily operations costs should be paid by NSMP shippers

Of those that were supportive of targeted charging, the following reasons were given:

- If charges are recovered from a wider set of users then there would be a cross-subsidy because National Grid Gas does not provide this service at other sub-terminals which would also be discriminatory
- It would be more cost-reflective
- It provides the right market signals
- It is aligned with the existing St Fergus compression charge
- The existing St Fergus compression charge creates a precedent
- Socialising costs creates an unlevel playing field
- Without cost targeting the NSMP sub-terminal would enjoy competitive advantage over the other sub-terminals
- Principles of user commitment should apply
- The Tariff code as now applicable in the UK via retained EU law provides for this at Article 4.4(b). This also provides for Ofgem assessing whether the service provided benefits all network users

Consultation - We said:

- NGG Response:
  - Of those that expressed a view opposing cost targeting they were by and large upstream parties. Those that were in favour of targeted charging were two upstream parties that do not use the compression services at St Fergus users of the network or their representatives.
  - The comments against targeted charging are largely centred on concerns that targeted charging will make the NSMP sub-terminal less competitive resulting in distortions in the market, a barrier to investment in new gas fields and lower security of supply. We are conscious of these concerns and will address them as part of the study on wider market impacts. There were also comments that targeted charging will cut across a single pricing methodology and it could impinge on our licence obligations. As part of discussions going forward we will explore these points further either with the respondent on a one to one basis or in the industry forums.
  - In terms of those that were in favour of targeted charging the reasoning centred around cost-reflectivity, alignment with existing St Fergus charging and providing the right market signals and without targeting then there is potentially a competitive advantage for the NSMP terminal, an unlevel playing field and a cross-subsidy where NGG does not provide this service. We are also cognisant of the comments on user commitment and compliance with the EU tariff code and would like to discuss all of these points further in industry forums.

- NGG Response:
  - Not surprisingly the responses to this question reflected those in Q4 whereby those not in favour of targeted charging did not think there should be a departure from the split between entry and exit charges of 50:50. We note that those in favour of targeting should be at the NSMP sub-terminal level. The intention is that this will be taken forward for further discussion in industry forums.

Possible Methods of recovery:

Capacity Based charge	Commodity based charge	Standing Charge

Possible Methods to demonstrate long term Cost vs. Benefit

User Commitment Style (Capacity)

Capacity is booked up front at floating prices.

Fixed volume, Fixed period

Ensures costs will be more-or-less recovered over the agreed period dependant on changes in Capacity Prices

User Commitment Style (Financial)

A Rate is calculated

A "Commitment" is made to total future usage

Rate x Commitment = Commitment Value

Charges incurred are matched off against Commitment Value until fully paid off

Questions around how Under Recovery is resolved

Economic Test

A one off auction is held for periods to the expected lifetime of new compressors.

The estimated value of all Capacity booked is assessed against project costs and the scale of the project adjusted to match demand or a new charge is calculated to address the gap between the value of bookings and project cost.

Implications and considerations

- Any of these options may require the ASEP to be split to enable booking at a specific terminal rather than the whole.
  - Modifications to split the ASEP into compression or non-compression terminal areas for capacity booking.
  - Obligated baselines at St Fergus would need to be forecast to change
  - Lessons to be drawn from the Bacton Split
  - Complexity of baseline calculated with/without compression, timing, capability of system depending on supplied pressure, potential requirements to modify connection
- A PARCA derived NPV Test/cost of allocation would likely be significantly higher than project cost
- A variation on the PARCA process or any new process design could be complex and involve significant consultation.
- The PARCA principles of a financial commitment from a customer based on an NPV test against an estimated project value, could provide a firm driver for NTS investment and lower risks of the cost of stranded assets to consumers.

PARCA Process - High Level Summary

Phase 0	• Bi-lateral discussions and PARCA Application process
Phase 1 (up to 6 months)	• Fixed fee (£120k) but costs reconciled • Initial Optioneering – identification of options to progress • Hold PARCA Window / Ad-hoc QSEC / Ad-hoc Exit Reduction Window • Agree capacity delivery date & tolerances • 'Phase 1 Output' & 'Need Case' reports
Phase 2 (up to 60 months)	• Capacity reserved exclusively for signatory • Develop Projects up to planning permission or agreed commercial solution • Credit required based on 1 year of average capacity charges stepping up over 4 years (25% per year)
PARCA Phase 2 Expiration	• PARCA ends when capacity is allocated to the NTS User (Shipper) – must pass NPV Test • Funding through FIOC Uncertainty Mechanism met through general transportation charges • Customer may be invoiced for a termination fee if capacity is not allocated • Can be terminated by the customer at any time.
Phase 3 (up to 24 months)	• Network reinforcement where required • Time between capacity allocation and the capacity registration date