

## Representation - Draft Modification Report UNC 0667

### Inclusion and Amendment of Entry Incremental Capacity Release NPV test in UNC

**Responses invited by: 5pm on 21 May 2019**

**To:** [enquiries@gasgovernance.co.uk](mailto:enquiries@gasgovernance.co.uk)

<b>Representative:</b>	Malcolm Montgomery
<b>Organisation:</b>	National Grid NTS
<b>Date of Representation:</b>	21 <sup>st</sup> May 2019
<b>Support or oppose implementation?</b>	Oppose
<b>Alternate preference:</b>	n/a
<b>Relevant Objective:</b>	<p><b>a)</b> None</p> <p><b>c)</b> Negative</p> <p><b>d)</b> Comments</p>

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

- The NPV test has no meaningful impact upon efficient operation of the pipeline, and therefore the impact upon relevant objective a) is none.
- The NPV test currently sits in the Entry Capacity Release Methodology Statement (ECR). This proposal will subject the NPV test to dual governance arrangements, which, in our view, is an unsatisfactory arrangement that creates legal and regulatory uncertainty.
- It is recognised that this modification does remove some unnecessary barriers in the current NPV test, however the overall framework this proposal introduces is, in our view, sub-optimal.
- We believe this modification proposal has an adverse impact on relative objective c).
- Our preference is for the rules proposed under the review of the Entry Capacity Methodology Statement (ECR) to be taken forward, which we believe is a more considered and optimal approach.

The above summary is supplemented by further information at the end of this response.

**Self-Governance Statement:** *Please provide your views on the self-governance statement.*

This modification should go to the Authority for approval.

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

If this modification proposal were to be approved, then before implementation we would like to see clarity brought to the regulatory framework via a Licence amendment.

There are no system considerations here that may affect the lead time.

**Impacts and Costs:** *What analysis, development and ongoing costs would you face?*

No change in ongoing costs identified.

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

Yes, though we note that both UNC modifications 667 and 678<sup>1</sup> are seeking to amend UNC TPD section Y at this time. We believe it is possible to manage this, but think it would be useful to industry if we share the following observations on 2 relevant scenarios.

Scenario 1. UNC modification proposal 667 is implemented prior to 678.

The NPV test within UNC modification proposal 667 seeks to make use of the existing LRMC methodology which as well as producing charges produces estimated project values. This works upon implementation of 667, but an issue is created by the fact that 678 is proposing to remove the LRMC methodology and replace it with a new charging methodology. The appropriate solution seems to be for UNC section Y to have both the new charging methodology and retain the existing LRMC methodology. The legal text implemented under 678 would need to be amended to reflect this.

Scenario 2. UNC modification proposal 678 is implemented prior to 667.

The LRMC methodology is proposed to be removed upon implementation of one of the 678 modifications. If UNC modification 667 is implemented then the LRMC methodology will need to be re-instated into UNC section Y. The legal text for modification 667 would need to be amended to reflect this.

It seems prudent that under both scenarios then clarification be added into Section Y to confirm that the charges being calculated under the LRMC part of the charging methodology are redundant.

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<sup>1</sup> Note that 678 is used as a shorthand for the whole suite of 678 modifications including all alternatives, and is not presuming upon which modification proposal, if any, are implemented.

**Are there any errors or omissions in this Modification Report that you think should be taken into account?** *Include details of any impacts/costs to your organisation that are directly related to this.*

Yes. There are statements in the Draft Modification Report stating that substitution user commitment rules sit in the UNC.

...the substitution user commitment which is in UNC despite the rules for substitution being prescribed in the licence and methodology statements.

And

the Substitution User Commitment test, which is in UNC Section B 1.17.7 c) ii

This is not correct, and is erroneously being used to demonstrate an existing overlap between the Licence/ECR and UNC, to try and help justify adding further overlap.

The UNC user commitment rule in TPD Section B1.17.7c) ii is only for capacity that is not subject to a NPV test. The NPV test applies to both substitution and incremental capacity, i.e. substitution user commitment is not in the UNC.

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

South Hook Gas have raised a number of concerns regarding the current NPV test, and we do agree that the current test can be improved upon and currently is too onerous for PARCA applicants e.g. the current NPV test requires a capacity commitment beyond what could be considered reasonable.

This modification seeks to (i) move the NPV test, which currently sits in the Entry Capacity Release methodology statement (ECR), into the UNC, and (ii) amend the current test. Our comments are broken up into these 2 sections identified.

**i. Regarding moving the NPV test into the UNC.**

We do not support moving the test into the UNC. While historically we recognise that some capacity release rules have been placed within both UNC and ECR and that the UNC is the preference for some parties, we also recognise that this duplication can create risk and regulatory uncertainty. The existence of duplication of some rules now, does not mean it is sensible to extend this duplication, and more importantly any UNC rules should not interfere with the Licence. It has never been previously intended that rules for amending capacity release obligations, whether that be increasing a baseline or substituting a baseline, should sit within the UNC. National Grid NTS's capacity release obligation, and the associated allowed revenue implications that may entail, is a matter for the Licence. As such, any rules which may amend, substitute or increase baselines are best placed exclusively within the Licence or a document governed by the Licence (e.g. ECR).

It has been suggested that the ECR could point to the relevant section of the UNC, and while we would likely need to use such an approach to achieve a form of technical compliance in the short term, it is not a satisfactory long term solution. If it is decided that

the rules for amending capacity release quantities should be governed by the UNC, then for simplicity and transparency the Licence should reflect that.

We also note that there can be advantage to having certain rules out of code governance. Rules that are not continually open to modification have more predictability and stability as well as more controllable governance (e.g. no 11<sup>th</sup> hour alternative modification proposals). As National Grid NTS is the party with responsibility to develop the network, and has the obligation to do so in an economic and efficient manner, then we believe that we are best placed, in consultation with stakeholders, to bring forward proposals that achieve this.

Finally, while we do not support moving the NPV test into UNC, if it were to be moved into the UNC, then we would strongly recommend that it is done so in a controlled manner that does not create legal and regulatory conflict between the documents. The following steps would achieve that:

1. Insert NPV test in UNC that is 100% consistent with the NPV test in the ECR.
2. Amend Licence to recognise the NPV test within the UNC.
3. Parties propose amendments to the NPV test as they see fit.

**ii. Regarding the revised rules for the NPV test.**

We have raised concern within the workgroup regarding the comparative difference between the user commitment rules for existing capacity solutions (including substitution), compared to funded incremental solutions.

We believe there is a principle that for any capacity request, the cost of existing capacity solutions, should not exceed the cost of funded incremental solutions. It does not seem right that applicants utilising existing network capacity are subject to more onerous user commitment requirements than applicants requiring incremental capacity. We have identified credible scenarios under this modification proposal where that principle would not be upheld. Such a framework can incentivise PARCA applicants to connect to constrained parts of the network over unconstrained parts of the network. This would adversely impact upon consumers, and arguably such a framework is at odds with the obligation to develop the network in an economic and efficient manner.

We also note that no change to the way that the estimated project value is determined have been included within this proposal. Given that the project values are an integrated part of the LRMC methodology then this modification requires the retention of LRMC at the same time as the charging review is proposing to replace it. The net result, if both 667 and 678 are implemented, is a section Y that would contain 2 methods of producing charges. We believe a further modification to 667 would be needed to create an enduring solution for the estimated project cost, and removes the LRMC charging calculation from the charging methodology.

In summary we believe that the framework this modification proposes is sub-optimal, the way it achieves it is sub-optimal, and the amended rules themselves are sub-optimal.

National Grid NTS supports amending the NPV test via the proposals produced under our review of the Entry Capacity Release Methodology statement. These proposals support all outcomes of the Charging Review, including a revised method for determining the estimated project cost, and can be found on our website [here](#).