

Representation - Draft Modification Report UNC 0751

Capping price increases for Long-Term Entry Capacity

Responses invited by: 5pm on 11 June 2021

To: enquiries@gasgovernance.co.uk

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

Representative:	Daniel Hisgett
Organisation:	National Grid Gas
Date of Representation:	11 June 2021
Support or oppose implementation?	Oppose
Relevant Objective:	<p>c) None</p> <p>d) Negative</p> <p>g) Negative</p>
Relevant Charging Methodology Objective:	<p>c) Negative</p> <p>e) Negative</p>

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

The modification proposes a price cap on Quarterly System Entry Capacity (QSEC) derived based on the Consumer Price Index (CPI). The Modification would apply this price cap to any Capacity to be used in future, post implementation, regardless of when it was booked. In the case of Capacity booked prior to the implementation of UNC0678A the CPI Uplift would be applied to the price at the time of the auction rather than the floating price. Our primary concern is that this effectively replicates the Interim Contracts previously proposed and rejected under UNC 0621.

The proposal would introduce a form of price protection to contracts struck from 06 April 2017 onwards, for use in any period post implementation. The modification proposed has two distinct pricing impacts to consider, the period between implementation of TAR on 06 April 2017 and 30 September 2020, and the period post UNC0678A implementation on 01 October 2020.

The first impact is most significant as it applies the proposed price cap to the auction prices associated with Capacity booked in the previous pricing regime, where the majority of charges were collected via the “top-up” commodity charges, and so the capacity prices were not reflective of the costs to be recovered. The price uplift, calculated based on a forecast of CPI for the periods modelled, would not necessarily trigger an increase to the auction price once rounded to four decimal places. The

resulting prices calculated are lower than the expected “floating” price to be applied to all Capacity purchased after this period.

National Grid will continue to collect the same total Revenue and so any costs not recovered from a User (or Users) due to application of this additional layer of price protection will result in higher prices being passed on to all other Users. The levels of impact on any annual period will vary due to the bookings applicable to the period, but exceed £30m per year on a number of occasions based on the analysis provided by both National Grid and the Proposer. This level of impact results in an increase to the Entry Transmission Services Rate of up to 5.9% based on previous analysis.

We already see a marked influence in the prices due to price protected contracts, known in the GB market as Existing Contracts. This modification would create further distortion, providing a small number of Users with a competitive advantage which would not be afforded to others, and so we believe the Modification negatively impacts on Relevant Objective d) and Relevant Charging Methodology Objective c).

The second relates to the application of a price cap to QSEC auctions occurring following the implementation of UNC 0678A on 01 October 2020 which introduced the floating price structure to the GB market. This portion of the modification isn't expected to have a significant impact, but any price reduction due to application of the Price Cap will be picked up by other Users, driving up the Reserve Prices, even if the materiality is low.

Implementation:

We would request that the modification, if approved, be effective from the 1st of October of any given year. The timescales provided by the ROM suggest a project stand up time of three months and a further 12-14 weeks to implement the changes, which would suggest a decision publication would be required no later than 1st April in that same year.

This should leave time to assess and account for the impact of the modification on prices prior to publication of the IP Auctions in late May.

Impacts and Costs:

An enduring solution will cost at least £115,000, but probably not more than £150,000 to implement

Legal Text:

Yes, the Legal Text satisfies the solution outlined in the Modification.

Modification Panel Members have requested that the following questions are addressed:

Q1: Provide views on whether this Modification is suitable for Self-Governance procedures.

We believe there is a material impact on Users if this modification were to be implemented and so should be considered for Authority Direction.

Quantifying the potential impacts on future prices is difficult as it is difficult to accurately predict future prices, but we do know that the impact of applying this new price cap to contracts purchased in the period between 06 April 2017 and 30 September 2020, does increase Reserve Prices, negatively impacting some Users over the next 10 years.

Q2: Provide views on whether there are any compliance issues associated with this Modification.

The introduction of a form of price protection for contracts booked during the interim period, between implementation of TAR NC on 06 April 2017 and implementation of UNC0678A on 01 Oct 2020, is similar in nature to the proposed introduction of Interim/Historical Contracts under UNC0621 (and alternatives). This Modification was previously rejected by Ofgem as it wasn't considered to be compliant under the EU Tariff Network Code, now retained in UK Law.

As a consequence of price protected Capacity which already exists in the market, we see an increase in Reserve Prices to compensate for under recovery associated with lower priced Capacity. Any extension of price protection may raise concerns that prices could rise further to compensate and be levied against a reduced User base. The small and shrinking denominator used to calculate the Reserve Prices would result in a decreased likelihood of price stability and predictability.

Are there any errors or omissions in this Modification Report that you think should be taken into account?

None.

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

Analysis mentioned above was published on the Joint Office website as part of the UNC0751 Workgroups on 02 March 2021¹ (NGG) and 02 February 2021² (WWA).

¹ <https://www.gasgovernance.co.uk/0751/020321>

² <https://www.gasgovernance.co.uk/0751/020221>