Representation - Modification UNC 0790 (Urgent)

Introduction of a Transmission Services Entry Flow Charge

Responses invited by: 5pm on 06 December 2021

To: enquiries@gasgovernance.co.uk

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

Representative:	Colin Williams
Organisation:	National Grid NTS
Date of Representation:	01 December 2021
Support or oppose implementation?	Support
Relevant Objective:	**d)** Positive
Relevant Charging Methodology Objective:	**aa)** Positive **c)** Positive

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

We see benefits of this proposal on competition grounds and linked to this, it can ultimately benefit end consumers by reducing the overall pricing disparity Users pay for Transmission Services Entry charges.

One of the challenges faced under the current regime is the price payable for Transmission Services Entry Capacity given the availability and use of Existing Contracts. The use of these at the expense of new capacity is high, greater than forecasted ahead of October 2020, when the updated postalised regime was implemented. Existing Contracts have fixed capacity charges from when they were allocated.

Their influence has been visible through the high Transmission Services Entry Capacity reserve prices across Gas Years 2020 and 2021, prompting National Grid to take remediating measures to defer £45m[1] of Entry revenue to reduce some of this impact and lower the level of the Entry Reserve Prices from what they would have been. We recognise that change was needed to manage this to some levels for the benefit of Users and Consumers.

This prompted National Grid to issue its open letter[2] in May 2021 that highlighted a number of issues notable a need to address the pricing differential on Transmission

[1] https://www.nationalgrid.com/uk/gas-transmission/document/135731/download
[2] https://www.nationalgrid.com/uk/gas-transmission/document/135746/download

Services Entry charges between access and use of Existing Contracts and that of new capacity (i.e. capacity bought on or after 6 April 2017).

There are two key positive changes this proposal delivers on against the noted relevant objectives, related to competition:

- Adjusting the reference / reserve price calculation to make the reference prices more stable, less susceptible to large changes due to small changes in capacity or revenue inputs in the Entry reference/reserve price calculations. This results in Transmission Services prices that will be lower than they would otherwise be in the current methodology, especially while levels of Existing Contracts remain high;
- Introducing a new Transmission Services Entry Flow Based charge that will only exist whilst Existing Contracts are also present. The charge will reduce in line with the levels of Existing Contracts and will be zero when there are no Existing Contracts remaining. The Entry flow based charge, noting the exemptions for Interconnection Points and Storage, produces a charge that is more equitable across Entry Users and applies across all flows providing a larger base than that used for the purposes of setting Transmission Services Entry Reference / Reserve Prices. Like the adjustments to the calculation of Transmission Services Entry reference prices, the method of calculating this is less susceptible to large changes when there are small changes to calculation inputs than if the additional charge were capacity based, for example.

On the grounds of competition we believe this furthers Relevant Objective d and Charging Relevant Objectives aa and c:

We believe that existing arrangements which effectively target the recovery of most of the Transmission Services Revenues on holders of new Entry Capacity is not appropriate. This is largely driven by the impact of the levels of Existing Contracts and their use at the expense of new Entry Capacity. The Transmission Services Entry revenue shortfall borne by new capacity (created by the pricing of Existing Contract (EC) Capacity being fixed) is not appropriate and has been shown to be greater than anticipated post implementation of new arrangements from 01 October 2020.

In our view, this is detrimental to competition between Users, notably between those with or access to Existing Contracts and those without. The impact of this proposal:

- Reduces the price disparity for Capacity prices. This is achieved by changing the denominator on the reference price calculation linked to the impact Existng Contracts would have.
- Reduces the reference price from what it would be without this change (i.e. Under the current method) and has the additional benefit of not being as susceptible to large changes due to small changes in capacity or revenues.
- Reduce the overall transportation charging rates that could be ultimately passed on to consumers.

Even with Users that may hold a mix of these, the impact overall is that any ‘new’ capacity currently bears the brunt of Transmission Services Entry revenue recovery.

The Modification proposes a more equitable approach to socialise such costs across all gas flowed at Entry Points (save for the noted exemptions to Storage and Interconnection Points and providing for the relevant discount to Entry Eligible Quantities). The extension of the conditional capacity discount to eligible quantities maintains the integrity of the inefficient bypass product keeping any discount on flow based charges linked to any actual discount applied to eligible quantities. Overall, this we believe will positively increase the competition between Users of the network.

On the Price Differential between Existing Contracts and Non-Existing Contracts we believe these changes further Relevant Objective d and Charging Relevant Objectives aa and c:

The price protection afforded to Existing Contract Capacity results in a significant price differential between the unit cost of Existing Contract Capacity and new Entry Capacity, with Users allocated the latter paying on average 23 times the unit price paid for the equivalent product under an Existing Contract as demonstrated within the Modification.

A flow-based charge distributed across all flows (save for the noted exemptions to Storage and Interconnection Points and providing for the relevant discount to Entry Eligible Quantities) has the benefit of being applied over a larger base. The charge is paid by all flows whether they are Existing Contract Capacity or other Entry Capacity booked.

The Modification is expected reduce the material differentiation in Users' Transportation Charges for the equivalent Transportation service which is apparent under the current arrangements. The Proposal is seeking to reduce the differential in question (representing an improvement when compared to the current arrangements) but does not seek to or fully eradicate this differential.

Volatility and sensitivity from Year on Year:

We believe these changes on introducing the Charging Relevant Objective aa

A flow-based charge distributed across all flows (save for the noted exemptions to Storage and Interconnection Points and providing for the relevant discount to Entry Eligible Quantities) has the benefit of being applied over a larger base. This helps with the stability of any such charge given any movement in the numerator (i.e. flows) is spread across a larger base than any prevailing capacity charge would be applicable to.

Using flows also provides for greater stability in the denominator as flow forecasting by National Grid has historically been relatively accurate, more so than capacity forecasting to actuals. This would also have the benefit of a reduction in the level of year-on-year volatility in Entry Capacity Reserve Price rates.

If implemented this Modification is expected to provide a more stable and predictable Reference Price for Entry Capacity leading to Users having a greater level of confidence in their forecasts of prospective use of network costs and therefore set their own service costs more accurately (potentially with a lower risk margin), thereby enhancing effective competition.

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

As set out in the Proposal, implementation should take effect in time to be reflected in the Transportation Charges which will apply from 01 October 2022 or the next 01 October following the Authority direction to implement.

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

The ROM estimate provided by Xoserve indicates that an enduring solution will cost at least £210,000 but probably not more than £280,000.

This change would need to be prioritised through the DSC Change Management Committee alongside other changes within Xoserve's planned Gemini programme. The high-level estimate to develop and deliver this change is approximately 14 to 21 weeks for Analysis through to Post Implementation Support.

Please note a lead time of 3 months for startup/sanction/mobilisation should be considered though there is the potential for this to be shortened subject to the delivery mechanism and availability of resources.

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

We are satisfied that the legal text delivers the intent of the solution identified in this Proposal.

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

We have not identified any such error or omissions.

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

We note that Frontier Economics produced a further assessment of the potential impacts of this modification to introduce a Transmission Services Entry Flow Based charge. This was updated following feedback on the initial version and the updated note and material we believe provides clarity on the assessment and its application for Stakeholders to comment on both now and as part of any further assessment from Ofgem.

This assessment goes beyond the typical level of assessment performed at this stage in the modification process. The purpose to this assessment is to provide more views on the potential impacts beyond those typically presented. It's aim is to consider broader market assessments can help inform representations at this stage and support, as much as possible, any assessment Ofgem may carry out on the back of this modification proposal prior to any decision.

Whilst there is substantial detail in the assessment, we support the aggregation taken in the assessments when considering the overall impact. This ensures a level that cannot reasonably account for Shipper specific decision making which will produce some variances against the assessment that can be brought out in any response to a broader impact assessment.

To comment on one aspect related to consumer impact, we feel that whilst there is a likely range when it comes to consumer benefits (taking into account that some shipper behaviours may be different to those assumed but not reasonable to assess when considering broader, aggregated impacts) there are a few points that is worth taking account of:

- We believe competition will benefit from this change that, when looking at the Transmission Services Entry Reserve Prices compared to Existing Contracts and when brining in the new Entry flow-based charge. This reduces, not removes, price disparity that is significant in the current regime and its reduction should better facilitate competition by providing a more level playing field than now.
- Whilst it is reasonable to consider a range for consumer benefits, we believe there is a consumer benefit from these change proposals. Consumer benefit will not be negatively impacted and should deliver a benefit in overall lower, more stable total prices for Entry Transportation charges than they would be without this change.