

Modification proposal:	Uniform Network Code (UNC) 737: Transfer of NTS Entry Capacity from a Capacity Abandoned ASEP		
Decision:	The Authority ¹ has decided to reject this modification ²		
Target audience:	UNC Panel, Parties to the UNC and other interested parties		
Date of publication:	30 September 2021	Implementation date:	n/a

Background

In the Final Modification Report ("FMR"), Centrica Energy Ltd ("the Proposer") states that some Aggregated System Entry Points ("ASEPs") on the National Transmission System ("NTS") may be "abandoned" as planned upstream projects do not come to fruition, gas has been exhausted, or the ASEPs are no longer economic. In these circumstances, where users hold entry capacity at capacity "abandoned" entry points, the users will continue to pay National Grid Gas ("NGG") for capacity which will not be utilised and therefore for a service which is not required.

The Proposer states that this also restricts NGG in releasing capacity at other entry points as it is required to fulfil obligations to support existing bookings. Additionally, if a user(s) were to default against payments for these entry capacity holdings, NGG may serve Termination Notices which would result in the socialisation of unpaid costs across all users.

The modification proposal

On 17 September 2020, the Proposer raised UNC737: 'Transfer of NTS Entry Capacity from a Capacity Abandoned ASEP'³, which proposes to allow the transfer of sold NTS Entry Capacity at a "capacity abandoned" entry point to a recipient entry point where there remains unsold entry capacity. The modification would define an entry point as a "Capacity Abandoned ASEP"

¹ References to the "Authority", "Ofgem", "we" and "our" are used interchangeably in this document. The Authority refers to GEMA, the Gas and Electricity Markets Authority. The Office of Gas and Electricity Markets (Ofgem) supports GEMA in its day-to-day work. This decision is made by or on behalf of GEMA.

² This document is notice of the reasons for this decision as required by section 38A of the Gas Act 1986

³ <https://www.gasgovernance.co.uk/0737>

where all Users apply to transfer their capacity holdings to one or more alternative entry points within the same Transfer Window such that no User continues to hold capacity at the original entry point. Where the entry capacity booked at the donor entry point is classified as existing capacity the protections afforded to this entry capacity remain post-transfer, meaning the fixed entry price is preserved and Revenue Recovery Charges (“RRCs”) are not applied.

UNC Panel⁴ recommendation

At the UNC Panel meeting on 21 January 2021, eleven out of fourteen members of the UNC Panel considered that UNC737 would not better facilitate the UNC objectives and the Panel therefore did not recommend its approval. Among the panel members representing consumers, both the domestic consumer voting member and the non-domestic consumer voting member did not recommend implementation.⁵

Our decision

We have considered the issues raised by the modification proposal and the FMR dated 22 January 2021. We have considered and taken into account the responses to the industry consultation on the modification proposal which are attached to the FMR⁶. We have concluded that:

- implementation of the modification proposal will not better facilitate the achievement of the relevant objectives of the UNC.⁷
- directing that the modification be made would not be consistent with our principal objective and statutory duties.⁸

⁴ The UNC Panel is established and constituted from time to time pursuant to and in accordance with the UNC Modification Rules.

⁵ <https://www.gasgovernance.co.uk/sites/default/files/ggf/2021-01/Minutes%20and%20determinations%20Panel%20268%20v1.0.pdf>

⁶ UNC modification proposals, modification reports and representations can be viewed on the Joint Office of Gas Transporters website at www.gasgovernance.co.uk

⁷ As set out in Standard Special Condition A11(1) of the Gas Transporters Licence, see: <https://epr.ofgem.gov.uk//Content/Documents/Standard%20Special%20Condition%20-%20PART%20A%20Consolidated%20-%20Current%20Version.pdf>

⁸ The Authority’s statutory duties are wider than matters which the Panel must take into consideration and are detailed mainly in the Gas Act 1986.

Reasons for our decision

We consider this modification proposal would not better facilitate UNC Relevant Code Objective (d) and UNC Charging Methodology Relevant Objectives (“CMROs”) (c) and (a), and has a neutral impact on UNC Relevant Code Objectives (a). Given the similarities between the UNC Relevant Code Objectives and the CMROs, we assess them in tandem.

We consider that the UNC Relevant Code Objectives (b), (c), (e), (f) and (g), and CMROs (aa), (b), (d) and (e) are not relevant to the modification proposal under assessment.

CMRO (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

We consider that the proposal does not better facilitate CMRO (a).

The Proposer states: “The Modification better facilitates Charging Relevant Objective (a) as where NTS Entry Capacity is held at an ASEP where it will not be used... a User will continue to make a contribution to National Grid’s revenue where no service is required to be provided and therefore, no costs or minimal costs will be incurred by National Grid.” Panel Members agreed that implementation of this proposal would have a positive impact on CMRO (a) with no Panel Members offering a different view. We consider that Users who have Existing Registered Holdings (“Holdings”)⁹ at entry points knowingly and fairly entered into arrangements whereby they are liable to the costs associated with capacity holdings, including in the event that the Holdings are not utilised. Users who hold capacity at entry points where capacity is no longer utilised were aware of the risk of paying for unutilised capacity when they obtained the Holdings. Therefore, we think that these capacity charges due to NGG fairly reflect the expectations and obligations entered into by the relevant Users when they obtained the Holdings. On balance, we consider that the proposal does not better facilitate CMRO (a).

⁹ As defined in UNC Section Y 2.2.2 (e)

Objective (d) securing of effective competition and CMRO Objective (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.

We consider that the proposal does not better facilitate and would have a negative impact on UNC Relevant Code Objective (d) and CMRO (c).

The Proposer states: "Relevant Objective (d) is better facilitated as Users holding capacity at abandoned entry points are not encumbered with costs for a service they are unable to use." Panel Members were divided in their consideration of these relevant objectives. As we detailed in our assessment of CMRO (a), we consider that these costs fairly reflect the expectations and obligations entered into by the relevant Users when they obtained the Holdings.

Furthermore, we consider that UNC737 could lead to capacity displacement through fewer bookings of new capacity and more utilisation of existing contracts. This would be to the detriment of users of new capacity, as any revenue shortfall caused by capacity displacement would lead to an increase in the price for new capacity. Following the implementation of UNC678A¹⁰, existing contracts offer access to entry capacity for a significantly lower price than capacity which is not protected under Article 35(1) TAR NC¹¹ and is subject to a floating price. As a result, protection for existing contracts has led to a dual regime in the GB charging methodology where NTS users face significantly different costs for capacity depending on their access to existing contracts.¹² UNC737 would exacerbate the problems caused by existing contracts further, which would have a negative impact on competition. We note that some Panel Members have also expressed these views when considering the Relevant Objectives.

Additionally, the Proposer writes that "Creating a value for capacity at abandoned entry points will also enhance security of supply, by reducing the downside risk associated with the booking of capacity to support potential upstream projects. Improved supply diversity and volumes will

¹⁰ Amendments to Gas Transmission Charging Regime: Decision and Final Impact Assessment (UNC678/A/B/C/D/E/F/G/H/I/J) (28 May 2020) <https://www.ofgem.gov.uk/publications/amendments-gas-transmission-charging-regime-decision-and-final-impact-assessment-unc678abcdefghij>

¹¹ Commission Regulation (EU) 2017/460 of 16 March 2017 establishing a network code on harmonised transmission tariff structures for gas. Now incorporated in UK law by the European Union (Withdrawal) Act 2018 and the European Union (Withdrawal Agreement) Act 2020, as amended by Schedule 5 of the Gas (Security of Supply and Network Codes) (Amendment) (EU Exit) Regulations SI 2019/531.

¹² Also see UNC739: Aggregate overrun regime for Original Capacity held at the Bacton ASEPs (20 August 2021) <https://www.ofgem.gov.uk/publications/unc739-aggregate-overrun-regime-original-capacity-held-bacton-aseps>

enhance competition in the downstream market.” Some Panel Members agreed with this assessment, commenting that being able to transfer capacity will encourage more capacity to come to the UK market. However, we note that neither the Proposer nor any consultation respondents identified any impact on Relevant Objective (e) “Provision of reasonable economic incentives for relevant suppliers to secure that the domestic customer supply security standards... are satisfied as respects the availability of gas to their domestic customers”. Furthermore, no evidence has been presented by the Proposer to demonstrate any impacts on potential upstream projects nor have any material impacts on security of supply been identified.

The Proposer also sees this modification as reducing the likelihood of the socialisation of unpaid capacity on the shipper community in the event of a user termination from the UNC. In Workgroup’s assessment of the consumer impact of this modification, we see that there have been two known incidents of User Termination with non-payment of Transportation Charges in the past few years. In these instances, the charges totalled just under £1million according to NGG. It is our view that the occurrence of User Termination has been shown to be rare and the monetary impact relatively low. Furthermore, we have not received evidence that the proposal will impact any cases of User Termination.

Overall, we conclude that the proposal does not better facilitate and would have a negative impact on UNC Relevant Code Objective (d) and CMRO (c).

Objective (a) Efficient and economic operation of the pipe-line system.

We consider that the proposal will have a neutral impact on Relevant Objective (a).

The Proposer states: “Permitting the transfer of capacity bookings from an abandoned entry point to an entry point where bookings are below obligated levels, means that capacity can be “moved” to locations where it is likely to be utilised, thereby optimising the use of the NTS.” The Proposer received support from some Panel Members who also see the transfer of capacity as optimising the NTS.

However, we also note that some Panel Members disagreed with this assessment and saw this proposal as having a negative impact, given that the Modification aims to move capacity to ASEPs where capacity has not yet sold out. This suggests that there may not be an urgent

need for additional capacity at these ASEPs. This view is supported by NGG in the consultation responses. NGG also raised a concern regarding the Exchange Rate detailed in the proposal. The Exchange Rate could facilitate a transfer with a ratio of 3:1, which would result in capacity destruction on the NTS as available capacity is reduced through the transfer. We agree with these views. Overall, it is not clear whether transferring capacity will enhance or detract from the efficient and economic operation of the pipe-line system. We therefore conclude the proposal has a neutral impact on this objective.

Our principal objective and statutory duties

The Authority's principal objective is to protect the interests of existing and future consumers in relation to gas conveyed through pipes and electricity conveyed by distribution or transmission systems.

UNC737 has the potential to lead to capacity displacement and fewer sales of new capacity. The significant price differential¹³ between existing contracts and new capacity provides a strong incentive for shippers to optimise their use of existing contracts and this overall is likely to lead to fewer new capacity sales and a higher price for new capacity. For these reasons, we consider that directing that the modification be made would not be consistent with our principal objective and statutory duties.

Decision notice

In accordance with Standard Special Condition A11 of the Gas Transporters Licence, the Authority has decided that modification proposal UNC 737: *'Transfer of NTS Entry Capacity from a Capacity Abandoned ASEP'* should not be made.

David O'Neill

Head of Gas Markets and Systems

Signed on behalf of the Authority and authorised for that purpose

¹³ According to NGG estimates, in Gas Year 2021/22, the average price for existing contracts will be 96% lower than the entry capacity reserve price for new capacity, see: <https://www.gasgovernance.co.uk/sites/default/files/ggf/2021-06/NTSCMF%20July%202021%20Open%20letter%20v1.0.pdf>