

UNC Final Modification Report		At what stage is this document in the process?
<h1>UNC 0605S:</h1> <h2>Amendments to TPD Section K - Additional Methods to Procure and Dispose of Operating Margins Gas</h2>		<div style="display: flex; flex-direction: column; gap: 5px;"> <div style="border: 1px solid #00a651; border-radius: 5px; padding: 5px; display: flex; align-items: center; gap: 5px;"> 01 Modification </div> <div style="border: 1px solid #00a651; border-radius: 5px; padding: 5px; display: flex; align-items: center; gap: 5px;"> 02 Workgroup Report </div> <div style="border: 1px solid #00a651; border-radius: 5px; padding: 5px; display: flex; align-items: center; gap: 5px;"> 03 Draft Modification Report </div> <div style="border: 1px solid #00a651; border-radius: 5px; padding: 5px; display: flex; align-items: center; gap: 5px;"> 04 Final Modification Report </div> </div>
<p>Purpose of Modification:</p> <p>This modification seeks to enable National Grid NTS to procure and dispose of Operating Margins Gas in a more efficient and economical way.</p>		
	Panel consideration is due on 20 July 2017	
	The Panel determined that this self-governance modification should not be implemented.	
	High Impact: None	
	Medium Impact: None	
	Low Impact: Shippers and National Grid NTS	

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Timetable		
Modification timetable:		
Initial consideration by Workgroup	05 January 2017	
Amended Modification considered by Workgroup	04 May 2017	
Workgroup Report presented to Panel	15 June 2017	
Draft Modification Report issued for consultation	15 June 2017	
Consultation Close-out for representations	06 July 2017	
Final Modification Report available for Panel	10 July 2017	
Modification Panel decision	20 July 2017	

1 Summary

What

The UNC currently prescribes that National Grid NTS should run annual tenders in order to purchase and dispose of Operating Margins Gas, which has not changed since the inception of Code. This modification proposes to enable National Grid NTS to use other trading mechanisms in addition to tenders.

Why

UNC TPD Section K Operating Margins was based on the prevailing market conditions when the code was created 20 years ago and no longer reflects the current climate. There have been a number of changes to the market conditions such that the number of tenders received has reduced significantly as has the use of Operating Margins Gas. The process has been to accept, tender bids/offers in price order irrespective of whether more competitive prices could be achieved by trading through other routes e.g. Over The Counter (OTC) or exchange. It is not economic or efficient to limit the way in which the Operating Margins Gas is procured or disposed of. National Grid NTS is obligated under its licence, Special Condition 8C.2, to procure its Operating Margins requirements in an efficient manner. This Modification seeks to enable National Grid NTS to procure and dispose of Operating Margins Gas in a more efficient and economical way.

How

In future National Grid NTS proposes it will look to achieve the best price for procuring and disposing of Operating Margins Gas by having the ability to utilise a range of trading mechanisms which are the Over the Counter (OTC), brokered markets and trading exchanges e.g. ICE Endex in addition to tenders. New rules will be introduced to deal with the potential for trading error by National Grid NTS. It will also provide the ability to procure and dispose of gas prior to the end of the Storage Year, as well as at the beginning of the next Storage Year. There will be amendments to conditions within UNC TPD Section K, to facilitate the change in process.

2 Governance

Justification for Urgency, Authority Direction or Self-Governance

Panel determined the modification is unlikely to have a material effect on competition in the shipping, transportation or supply of gas conveyed through pipes, or any commercial activities connected with the shipping, transportation or supply of gas conveyed, because this modification is seeking change the process that may result in a minor reduction in costs for Shippers (up to £90k per annum) and an update to the process to be more reflective of the current market.

Modification 0605S will therefore follow self-governance procedures.

Fast Track Self-Governance Criteria

This modification is not suitable for Fast Track Self-Governance as it is not properly a housekeeping modification required as a result of some error or factual change.

Requested Next Steps

This modification should:

- be subject to self-governance

- issued to consultation

Workgroup participants agreed that this modification is sufficiently developed to be issued to consultation.

The Workgroup agreed with the Modification Panel's determination on Self-Governance as the modifications potential reduction in costs for Shippers (up to £90k per annum) and update to the process (to be more reflective of the current market) is unlikely to have a material impact on competition.

3 Why Change?

National Grid NTS purchases Operating Margins (OM) on an annual basis in line with both UNC Section K and obligations described in the National Grid Gas Safety Case in respect of the NTS (the Safety Case). The Safety Case places an obligation on National Grid Gas to maintain OM at levels and locations determined throughout the year.

The OM service is used to maintain system pressures in the period before other system management services become effective (e.g. national or locational balancing actions). A further quantity of OM is also procured to manage the orderly run-down of the system in the event of a Network Gas Supply Emergency.

Where National Grid NTS contracts for Operating Margins Capacity at a gas storage facility, National Grid NTS must purchase gas for injection or transfer into the facility. The Operating Margins requirements at each Operating Margins Facility vary over time resulting in the need to procure additional Operating Margins Gas, dispose of surplus Operating Margins Gas or transfer Operating Margins Gas between different Operating Margins Facilities.

When Operating Margins are utilised, the result is a withdrawal of Operating Margins Gas at an Operating Margins Facility and need to refill the Operating Margins Facility, in preparation for a future Operating Margins event.

Such activities to procure, dispose and transfer Operating Margins Gas are often referred to as "reprofiling".

UNC TPD Section K Operating Margins was originally based on the prevailing market conditions when the code was created 20 years ago, and no longer reflects the current climate. There have been a number of changes to the market conditions such that the number of tenders received has reduced significantly as has the use of Operating Margins Gas. The current process within UNC TPD Section K limits the method to tenders only that can be used to procure or dispose of gas. Tender bids / offers must be accepted in price order, irrespective of whether more competitive prices could be achieved by trading through other routes e.g. via Over the Counter (OTC) or by using an exchange.

What the drivers are and which parties are impacted

This Modification seeks to enable National Grid NTS to improve the process to procure and dispose of gas in a more efficient and economical way. The drivers for changing UNC to allow National Grid NTS to use other ways of procuring or selling gas are:

- Process is limited by UNC prescribing that only tenders should be used;
- Less competitive prices offered through tenders versus other options (OTC or exchange) and a reduction in the number of tenders received;
- National Grid NTS licence directs that it operate in an efficient and economical way;
- Benefit to shippers of approximately £30k to £90k per annum which feeds through into the Closing Margins Adjustment Charge (UNC TPD Section K 4.4.5);

The Modification has no impacts on either National Grid NTS or Xoserve systems and the effects on National Grid NTS processes and procedures are negligible.

What the effects are should the change not be made

The Modification provides an improved method to manage the process for the procurement and disposal of Operating Margins Gas. Although, this Modification has a low impact it would benefit as a slightly more economical and efficient operation of the market.

4 Code Specific Matters

Reference Documents

http://www.gasgovernance.co.uk/sites/default/files/TPD%20Section%20K%20-%20Operating%20Margins_4.pdf

Knowledge/Skills

No additional skills or knowledge is required to assess this modification.

5 Solution

It is proposed that a change to Code is made to allow National Grid NTS to utilise other methods to procure and dispose of Operating Margins Gas at its own discretion, such as the OTC, brokered markets or trading exchanges. It is also proposed such procurement and disposal of Operating Margins gas be allowed prior to the end of the Storage Year (before the capacity rights reduce or expire) as well as at the beginning of the next Storage Year.

In order to allow National Grid NTS to procure and dispose of gas outside the tender process, amendments are required to UNC TPD Section K Operating Margins conditions:

- 3.3.7 Existing paragraph removed to facilitate changes to the Operating Margins Gas process;
- 3.3.8 Renumbered as 3.3.7 and circular reference to 3.3.7 deleted;
- 3.7.2 (a) to (f) renumbered as 3.7.3 (a) to (f). The new paragraph provides the ability to procure and dispose of Operating Margins Gas by other methods and before the end of the Storage Year;
- 3.7.2 (g) and (h) removed and new 3.7.3. (g) and (h) inserted to facilitate the changes to Operating Margins Gas and allow National Grid NTS to utilise other ways to procure and dispose of Operating Margins Gas:
- 3.7.3 Renumbered as 3.7.4;
- 3.7.4 Deleted, as the new 3.7.3 (h) and the new 3.7.5 describe the process for dealing with Residual Gas Transfers;
- 3.7.5 Renumbered as 3.7.6 and amended to allow Residual Gas Transfers to be conducted other means; and
- 3.7.6. Renumbered as 3.7.7

Recognising that Operating Margins gas costs are recovered from Users, it is further proposed to include the following rules in UNC TPD Section K to address errors that may occur in the trading activities undertaken by National Grid NTS for Operating Margins purposes.

Definition

1. An “**Operating Margins Trading Error**” occurs where, in respect of a trade for Operating Margins gas procurement or disposal (executed by National Grid NTS) it is identified by National Grid NTS *ex post* that one or more of the following elements of the transaction were not consistent with intention of the National Grid NTS representative executing the trade:
 - 1.1 The trade **gas price** is different to that which the National Grid NTS representative intended to be the gas price for the applicable trade; or
 - 1.2 The trade **gas volume** is different to that which the National Grid NTS representative intended to be the gas volume for the applicable trade; or
 - 1.3 The relevant trade **date** (or **range of dates**) is different to that which the National Grid NTS representative intended to be the relevant date (or range of dates) for the applicable trade.

National Grid NTS Obligations in the Event of an Error

2. Where National Grid NTS has identified the occurrence of an Operating Margins Trading Error, as soon as reasonably practicable it will seek cancellation of the relevant trade, or revision or correction of the executed Trade Parameters, to the extent permitted under the relevant Trading System Operator terms and/or policies and/or as agreed by the trading counterparty.
3. Where the actions described in paragraph 2 are not possible, National Grid NTS will undertake trading activity to limit the value of, or rectify, the error.
4. Where further to paragraph 2 the Trading System Operator and/or trading counterparty (as appropriate) permits:
 - 4.1 cancellation of the trade, or revision of all the executed Trade Parameters equal to those intended by National Grid NTS, no Error Value Determination will be made in accordance with paragraph 5 or 6, nor any adjustment made in accordance with paragraph 8 or 9; or
 - 4.2 revision of the executed Trade Parameters, but nonetheless to values *not* equal to those intended by National Grid NTS, the revised Trade Parameters will constitute amended executed Trade Parameters.

Error Value Determination

5. Where the Operating Margins Trading Error is attributable to the circumstances identified in paragraph 1.1, the value of the error is the difference between:
 - 5.1 the intended gas price multiplied by the executed gas volume; and
 - 5.2 the executed gas price multiplied by the executed gas volume.
6. Where the Operating Margins Trading Error is attributable to the circumstances identified in paragraphs 1.2 or 1.3, the value of the error is the difference between:

- 6.1 The intended revenue/cost (determined on the basis of the intended Trade Parameters); and
- 6.2 The net revenue/cost from the trading activities (determined on the basis of the executed Trade Parameters) following any action taken in line with paragraph 3.

Adjustment Mechanism

7. Where the value of the error determined in accordance with paragraph 5 or 6 is less than £50,000 (per occurrence), no adjustments (described in paragraphs 8 and 9) will be made.
8. In respect of Operating Margins gas procurement, for the purposes of the determination of Operating Margins WACOG (as defined in UNC TPD K4.2.1) the intended Trade Parameters will be applied (subject to an absolute cost cap in respect of each Storage Year of £1,000,000).
9. In respect of Operating Margins gas disposal, where
 - 9.1 the value determined in accordance with paragraph 5.1 exceeds the value determined in accordance with paragraph 5.2, or the value determined in accordance with paragraph 6.1 exceeds the value determined in accordance with paragraph 6.2, the Closing Margins Adjustment Charge (calculated as per UNC TPD K4.4.5) shall be decreased by the aggregate value of any such errors occurring within the Storage Year;
 - 9.2 the value determined in accordance with paragraph 5.1 is less than the value determined in accordance with paragraph 5.2, or the value determined in accordance with paragraph 6.1 is less than the value determined in accordance with paragraph 6.2, the Closing Margins Adjustment Charge (calculated as per UNC TPD K4.4.5) shall be increased by the aggregate value of any such errors occurring within the Storage Year; and
10. Adjustments to the Closing Margins Adjustments Charge in any Storage Year will be subject to a cap of £1,000,000 (in terms of absolute costs, i.e. regardless of whether the value increases or decreases the Closing Margins Adjustment Charge).

Reporting

11. National Grid NTS will detail any Operating Margins Trading Errors (that are identified within the Formula Year) within its annual Procurement Guidelines Report (published in accordance with Special Condition 8A of the National Grid NTS Gas Transporter Licence).
12. In respect of each Operating Margins Trading Error detailed in accordance with paragraph 11, the following information will be provided:
 - 12.1 Trading System;
 - 12.2 Trade Execution Time and Date;
 - 12.3 Operating Margins Trading Error Identification Date;

- 12.4 Executed Trade Parameters;
- 12.5 Intended Trade Parameters (i.e. those Trade Parameters expected or intended by the National Grid NTS representative when executing the trade);
- 12.6 Details of any actions taken in accordance with paragraph 2 or 3;
- 12.7 Value of the error determined in accordance with paragraph 5 or 6; and
- 12.8 Details of any adjustments made in accordance with paragraph 8 or 9.

Definitions

- 13. ‘executed’ means (in the context of Trade Parameters or cost/revenue) the values (confirmed by the Trading System Operator) at which the trade was conducted
- 14. ‘intended’ means (in the context of Trade Parameters or cost/revenue) the values at which the National Grid NTS representative intended to strike a trade;
- 15. ‘Trade Parameters’ means the trade price, trade volume and the delivery date (or range of delivery dates) for the relevant gas trade.

6 Impacts & Other Considerations

Does this modification impact a Significant Code Review (SCR) or other significant industry change projects, if so, how?

None identified.

Consumer Impacts

Consumer Impact Assessment	
Criteria	Extent of Impact
Which Consumer groups are affected?	None - the Workgroup agrees with the proposer’s view, as the small potential benefit to Shippers of approximately £30k to £90k per annum (0.15% to 0.45% of Operating Margins annual costs), suggests this modification is only going to lead to a negligible benefit to consumers.
What costs or benefits will pass through to them?	n/a
When will these costs/benefits impact upon consumers?	n/a
Are there any other Consumer Impacts?	None identified.

Cross Code Impacts

None.

EU Code Impacts

None.

Central Systems Impacts

The systems required for the tender process and sale of gas are already in place via the exchange or OTC. Therefore, there are no systems changes required only minor amendments to the process for reprofiling and SMPS by National Grid NTS.

Workgroup Impact Assessment

The Workgroup sought clarification of several matters closely associated with this change. These can be summarised below:

Operating Margins related trading

The Workgroup asked what trading platforms can be used and what licence restrictions/ limitations might apply to this activity. National Grid NTS clarified that the trading platforms available are brokered markets, Over the Counter (OTC) and trading exchanges such as ICE Endex.

The Workgroup also asked what the publishing requirements were with regards to NTS trades (current/proposed). National Grid NTS clarified that no changes were proposed. Currently Operating Margins Gas tenders and results are published and Operating Margins gas data trading is published in the annual Procurement Guidelines Report.

Operating Margins related incentives and trading error

The Workgroup asked for details of any related incentives and clarity on which party (ies) bears the costs in the event of a trading error made by National Grid NTS. National Grid NTS clarified that there are no incentives for Operating Margins gas and any Trading errors would be borne by Shippers but it is a low probability that a mistake could occur for a trade (or a tender for that matter). The work group requested National Grid NTS to clarify if any shrinkage manifest trading errors have been apparent.

The following information was provided:

5 shrinkage trading errors have occurred in the past ~10 years

In each case, National Grid NTS could rectify the errors either at cost or with a marginal (~£50) gain / loss due to market movement

~500 shrinkage trades are typically conducted per year

Frequency and materiality of shrinkage trading errors has therefore historically been low

Such errors have been unwound with minimal cost or at no cost at all

The workgroup agreed that based on this information the probability of OM trading error was low, although some workgroup participants considered that National Grid NTS should bear financial risk in this event. National Grid NTS accepted that in principle this was appropriate and amended the Modification to deal with this issue, subject to certain materiality thresholds.

7 Relevant Objectives

Impact of the modification on the relevant objectives:

Relevant Objective	Identified impact
a) Efficient and economic operation of the pipe-line system.	None
b) Coordinated, efficient and economic operation of (i) the combined pipe-line system, and/ or (ii) the pipe-line system of one or more other relevant gas transporters.	None
c) Efficient discharge of the licensee's obligations.	Positive
d) Securing of effective competition: (i) between relevant shippers; (ii) between relevant suppliers; and/or (iii) between DN operators (who have entered into transportation arrangements with other relevant gas transporters) and relevant shippers.	None
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.	None
f) Promotion of efficiency in the implementation and administration of the Code.	None
g) Compliance with the Regulation and any relevant legally binding decisions of the European Commission and/or the Agency for the Co-operation of Energy Regulators.	None

This modification would further relevant objective (c) Efficient discharge of the licensee's obligations, because it will enable National Grid NTS to deliver an efficient and economical solution for reprofiling Operating Margins Gas in storage as per its licence condition.

8 Implementation

As self-governance procedures are proposed, implementation could be sixteen business days after a Modification Panel decision to implement, subject to no Appeal being raised.

9 Legal Text

Legal Text has been provided by National Grid NTS and is published alongside this Report.

The Workgroup has considered the Legal Text and is satisfied that it meets the intent of the Solution.

10 Consultation

Panel invited representations from interested parties on 15 June 2017. The summaries in the following table are provided for reference on a reasonable endeavours basis only. We recommend that all representations are read in full when considering this Report. Representations are published alongside this Final Modification Report.

Implementation was unanimously supported in the 3 representations received.

Representations were received from the following parties:

Organisation	Response	Relevant Objectives	Key Points
British Gas Trading	Support	c - positive	<ul style="list-style-type: none"> • There should be shipper, and hence consumer, benefits in allowing National Grid more options for the efficient procurement and disposal of operating margins gas. Concerns over liabilities for any trading errors made by National Grid have been addressed and although the solution for this is not entirely ideal, on balance there is merit in implementing this modification. • Support self-governance.
National Grid NTS	Support	c - positive	<ul style="list-style-type: none"> • Allows access to a wider range of Operating Margins gas procurement and disposal mechanisms. • Will allow a greater ability to achieve more competitive prices than may otherwise be possible under current arrangements. • Support self-governance. • This mechanism is used for shrinkage purposes, therefore there would be no further development, analysis or ongoing costs.
Scottish Power	Support	c - positive	<ul style="list-style-type: none"> • Agrees the existing methods used in respect of the procurement or disposal of Operating Margins Gas are unduly restrictive and as a result do not allow them access to more flexible and potentially cost effective options. • Supports this proposal, including the incorporation of the additional rules to address any trading activity errors. • Support self-governance.

Please note that late submitted representations will not be included or referred to in this Final Modification Report. However, all representations received in response to this consultation (including late submissions) are published in full alongside this Report, and will be taken into account when the UNC Modification Panel makes its assessment and recommendation.

11 Panel Discussions

12 Recommendations

Panel Determination

Members agreed:

- that Modification 0605S should [not] be implemented