

**Modification Report**  
**Annual NTS Exit (Flat) Capacity Credit Arrangements**  
**Modification Reference Number 0261**  
**Version 3.0**

This Modification Report is made pursuant to Rule 9.3.1 of the Modification Rules and follows the format required under Rule 9.4.

## **1 The Modification Proposal**

*Where capitalised words and phrases are used within this Modification Proposal, those words and phrases shall usually have the meaning given within the Uniform Network Code (unless they are otherwise defined in this Modification Proposal). Key UNC defined terms used in this Modification Proposal are highlighted by an asterisk (\*) when first used.*

This Modification Proposal\*, as with all Modification Proposals, should be read in conjunction with the prevailing Uniform Network Code\* (UNC).

### **Background**

Review Group 0221 “Review of Entry Capacity and the Appropriate Allocation of Financial Risk” was established in September 2008 to assess whether or not the current credit arrangements in place for securing long term NTS Entry Capacity\*, were sufficiently robust and provide the correct balance of risk between various Shipper Users. National Grid NTS raised Modification Proposal 0246 “Quarterly NTS Entry Capacity User Commitment” to address the issues identified by the Review Group.

Discussions at the April 2009 Transmission Workstream, considered whether a Proposal containing aspects similar to 0246 should be applied to NTS Exit Points\*. It was noted by the Transmission Workstream attendees that the Annual NTS Exit (Flat) Capacity\* regime contained key differences to that applying at entry, which would need to be considered, including:

- Demonstration Information\*, required when making an Adhoc application between 1 October and 30 June in Gas Year Y when works are required.
- The User must be in accordance with the principles in the prevailing Exit Capacity Release Methodology Statement\* i.e. that where a User has requested additional Enduring Annual NTS Exit (Flat) Capacity\* the User must meet the associated User Commitment (4 years’ worth of capacity charges) before any reductions may become effective.

National Grid NTS then provided an Exit Capacity risk analysis at the June 2009 Transmission Workstream. This analysis evaluated the level of risk to the Shipper Community from a Shipper default relating to the following categories of NTS Exit (Flat) Capacity\*:

- Existing Enduring Annual NTS Exit (Flat) Capacity (resulting from Initialisation);
- Enduring Annual NTS Exit (Flat) Capacity (Adhoc Applications);
- Enduring Annual NTS Exit (Flat) Capacity (Annual Applications); and
- Annual NTS Exit (Flat) Capacity.

The analysis indicated that the overall risk from a Shipper default is <£2m. However, the analysis reaffirmed that there is a similar risk at NTS Exit Points as identified by 0246 at Entry Points in relation to a User's ability to defer their Capacity commitments. This risk could conceivably lead to revenue expected to be recovered from a User being redistributed to the general shipper community should the original User choose to defer their commitment.

The Transmission Workstream agreed that a Proposal should be raised to address the aforementioned problem with the NTS Exit (Flat) Capacity regime.

### **Nature of the Proposal**

The ability for Users to defer capacity is described in UNC TPD Section B3.2.7. National Grid NTS proposes to remove this section of the UNC to remove the current ability for the User's Annual NTS Exit (Flat) Capacity to lapse. Full details are as follows:

Under UNC TPD Section B3.2.6 National Grid NTS assesses the sum of the User's Value at Risk\* which includes the aggregate NTS Exit (Flat) Capacity charges\* payable by the User in the following 12 months. The liability for the capacity charges associated with NTS Exit (Flat) Capacity are acquired via Annual Application Window\* or adhoc applications. If this aggregated amount exceeds 100% of the User's Code Credit Limit\*, then UNC TPD Section B3.2.7 states that National Grid NTS will notify the User. The User can either increase its Code Credit Limit by providing additional security or allow the future 12 months Annual NTS (Flat) Capacity to lapse, in effect deferring their capacity application.

National Grid NTS considers that the risk of a User deferring their capacity commitment is higher when the User only has capacity at a single NTS Exit Point. This is because Users with multiple NTS Exit Points are less likely to defer as in such a situation their capacity will lapse at all of their NTS Exit Points and not just at the NTS Exit Point at which the incremental capacity commitment was made.

National Grid NTS proposes to remove UNC TPD Section B3.2.7 to remove the current ability for the User's Annual NTS Exit (Flat) Capacity to lapse and therefore Users will be required to meet their capacity commitments as and when they become due and payable.

As Section B3.2.7 is being removed there is no reason to retain Section B3.2.6 and National Grid NTS also proposes to remove UNC TPD Section B3.2.6.

As a consequence of the above National Grid NTS also proposes to remove the similar provisions contained in paragraphs 3.7 and 3.8 of Section B Annex B-1. In addition, we will need to amend Section V3.3.4 to remove the references to Section B3.2.6 and paragraph 3.6 in Section B Annex B-1.

It is anticipated that these changes will enhance current incentives for Users to submit the required security. For clarity, the result of these changes is as follows:

- If the User's Value at Risk exceeds 100% of the User's Code Credit Limit, due to the User's Enduring Annual and Annual NTS Exit (Flat) Capacity for the twelve months commencing from the first day of the next calendar month, being included, then the Transporter will notify the User of such an

event, giving such User 2 Business Days to provide the additional surety or security.

- If a User does not increase its Code Credit Limit by providing additional security, then the User will be subject to the associated sanctions detailed within Section V3.3.2. These sanctions will continue to apply until the security is provided, as the User will no longer have the option to allow their capacity to lapse.
- Should the User choose not to put sufficient security in place and the charges become payable, then current provisions within UNC TPD Section V 3.0 Code Credit Limits and Section 4.0 Discontinuing Users and Termination will apply.

## **2 User Pays**

### **a) Classification of the Proposal as User Pays or not and justification for classification**

No classification required as no additional costs anticipated.

### **b) Identification of Users, proposed split of the recovery between Gas Transporters and Users for User Pays costs and justification**

None, no costs anticipated.

### **c) Proposed charge(s) for application of Users Pays charges to Shippers**

None.

### **d) Proposed charge for inclusion in ACS – to be completed upon receipt of cost estimate from xoserve**

Not applicable.

## **3 Extent to which implementation of the proposed modification would better facilitate the relevant objectives**

*Standard Special Condition A11.1 (a): the efficient and economic operation of the pipe-line system to which this licence relates;*

EDFE considered that implementation would force NGG to deliver capacity, even if a User fails to lodge security. This could therefore result in NGG undertaking investment to support capacity that was not required, whilst under the current arrangements this would be avoided. This does not appear to be economic or efficient, and so implementation of this proposal could be seen to detract from this Licence Condition

*Standard Special Condition A11.1 (b): so far as is consistent with subparagraph (a), the 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;*

Implementation would not be expected to better facilitate achievement of this relevant objective.

***Standard Special Condition A11.1 (c): so far as is consistent with subparagraphs (a) and (b), the efficient discharge of the licensee's obligations under this licence;***

NGNTS commented that the removal of a User's ability to defer its capacity holdings may prevent Users submitting speculative capacity applications (thereby triggering unnecessary investment under the licence), if the User knows it will not be able to defer its capacity holdings and will be tied in to its financial liabilities. Reducing the risk of unnecessary investment would therefore be consistent with the achievement of this relevant objective.

However, EDFE suggested that this Proposal has been amended so that if a User fails to lodge security, nothing happens other than they receive a notice from NGG. The User Default will not be enacted until the NTS Exit capacity is delivered and the Shipper fails to pay the bill. This could result in National Grid NTS undertaking significant investment to deliver enduring exit capacity that is not required, which would ultimately result in increased costs to Shippers and consumers.

***Standard Special Condition A11.1 (d): so far as is consistent with subparagraphs (a) to (c) the 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;***

Implementation would mitigate the community risk from a User signalling and being allocated Enduring Annual NTS Exit (Flat) Capacity and then subsequently, through not providing sufficient security, that User's capacity lapsing.

Implementation would remove the current consequences of capacity lapsing ie an under-recovery of NTS allowed revenue and a subsequent redistribution of this allowed revenue to remaining Users through changes in general transportation charges.

EDFE did not agree and considered that implementation would remove the ability of Users to defer the delivery of capacity by not posting credit. NGNTS, however, clarified that its current obligation to make capacity available, even if a User chose to defer its registration by twelve months, would not be affected by implementation. NGNTS also clarified that it continuously evaluates whether it is economic and efficient to continue a programme of investment and this evaluation would be unchanged by implementation.

***Standard Special Condition A11.1 (e): so far as is consistent with subparagraphs (a) to (d), the 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;*

Implementation would not be expected to better facilitate achievement of this relevant objective.

*Standard Special Condition A11.1 (f): so far as is consistent with subparagraphs (a) to (e), the promotion of efficiency in the implementation and administration of the network code and/or the uniform network code;*

Implementation would not be expected to better facilitate achievement of this relevant objective.

**4 The implications of implementing the Modification Proposal on security of supply, operation of the Total System and industry fragmentation**

No such implications have been identified.

**5 The implications for Transporters and each Transporter of implementing the Modification Proposal, including:**

**a) Implications for operation of the System:**

No such implications have been identified.

**b) Development and capital cost and operating cost implications:**

By removing the User's ability to defer its Registered Annual Exit (Flat) Capacity, implementation should ensure that any requests for Enduring Annual NTS Exit (Flat) Capacity that results in investment in the NTS is efficient and economic. Investment signals used by National Grid NTS to trigger system development would also be reinforced.

**c) Extent to which it is appropriate to recover the costs, and proposal for the most appropriate way to recover the costs:**

No recovery of costs is anticipated.

**d) Analysis of the consequences (if any) this proposal would have on price regulation:**

No such consequences are anticipated.

**6 The consequence of implementing the Modification Proposal on the level of contractual risk of each Transporter under the Code as modified by the Modification Proposal**

No such consequences are anticipated.

**7 The high level indication of the areas of the UK Link System likely to be affected, together with the development implications and other implications for the UK Link Systems and related computer systems of each Transporter and Users**

No such implications are anticipated.

**8 The implications of implementing the Modification Proposal for Users, including administrative and operational costs and level of contractual risk**

*Administrative and operational implications (including impact upon manual processes and procedures)*

For those Users applying for Enduring Annual NTS Exit (Flat) Capacity, the User will probably need to adjust its administrative arrangements to reflect that the obligation to pay Annual NTS Exit (Flat) Capacity charges remain in the event that insufficient security is in place to meet their obligations. Should the User have insufficient credit in place then ultimately the provisions within UNC TPD Section V will apply.

*Development and capital cost and operating cost implications*

Some costs associated with obtaining Security are anticipated. Also, the current ability for Users to defer costs where their physical requirement for NTS capacity is deferred would be removed.

*Consequence for the level of contractual risk of Users*

By reinforcing the obligations on Users to pay NTS capacity charges, the current risk to other Users would be reduced.

**9 The implications of implementing the Modification Proposal for Terminal Operators, Consumers, Connected System Operators, Suppliers, producers and, any Non Code Party**

No such implications have been identified.

**10 Consequences on the legislative and regulatory obligations and contractual relationships of each Transporter and each User and Non Code Party of implementing the Modification Proposal**

No such consequences have been identified.

**11 Analysis of any advantages or disadvantages of implementation of the Modification Proposal**

## Advantages

The following advantages have been identified:

- Users would continue to signal sufficiently far in advance to allow National Grid NTS to make appropriate investment decisions.
- Users would be required to pay Exit Capacity charges from the agreed release date.
- Implementation would remove the risk of, and shipper community exposure to, an event of a User deferring its NTS Capacity commitments.

## Disadvantages

The following disadvantage has been identified:

- Users that may have been relying on the ability to defer capacity will now have to pay NTS Annual Exit (Flat) Capacity charges even if their project is late or if the User is unable to utilise the registered capacity.

## 12 **Summary of representations received (to the extent that the import of those representations are not reflected elsewhere in the Modification Report)**

Representations were received from the following:

Association of Electricity Producers	AEP	Support
British Gas Trading Limited	BGT	Support
EDF Energy plc	EDFE	Not in Support
E.ON UK plc	EON	Support
National Grid Distribution	NGD	Support
National Grid NTS	NGNTS	Support
RWE Npower plc	RWE	Support
ScottishPower	SP	Support
Scottish and Southern Energy plc	SSE	Support
Statoil (UK) Ltd	STUK	Support
Wales & West Utilities Limited	WWU	Support

Of the eleven responses received, ten respondents were in support of implementation and one respondent was not in support of implementation.

## 13 **The extent to which the implementation is required to enable each Transporter to facilitate compliance with safety or other legislation**

Implementation is not required to enable each Transporter to facilitate compliance with safety or other legislation.

**14 The extent to which the implementation is required having regard to any proposed change in the methodology established under paragraph 5 of Condition A4 or the statement furnished by each Transporter under paragraph 1 of Condition 4 of the Transporter's Licence**

Implementation is not required having regard to any proposed change in the methodology established under paragraph 5 of Condition A4 or the statement furnished by each Transporter under paragraph 1 of Condition 4 of the Transporter's Licence.

**15 Programme for works required as a consequence of implementing the Modification Proposal**

No programme for works would be required as a consequence of implementing the Modification Proposal.

**16 Proposed implementation timetable (including timetable for any necessary information systems changes and detailing any potentially retrospective impacts)**

This Proposal could be implemented with immediate effect following direction from Ofgem.

**17 Implications of implementing this Modification Proposal upon existing Code Standards of Service**

No implications of implementing this Modification Proposal upon existing Code Standards of Service have been identified.

**18 Recommendation regarding implementation of this Modification Proposal and the number of votes of the Modification Panel**

At the Modification Panel meeting held on 17 September 2009, of the 8 Voting Members present, capable of casting 9 votes, 7 votes were cast in favour of implementing this Modification Proposal. Therefore the Panel recommended implementation of this Proposal.

**19 Transporter's Proposal**

This Modification Report contains the Transporter's proposal to modify the Code and the Transporter now seeks direction from the Gas and Electricity Markets Authority in accordance with this report.



20 Text

**UNIFORM NETWORK CODE – TRANSPORTATION PRINCIPAL  
DOCUMENT**

**SECTION B - SYSTEM USE AND CAPACITY**

*Delete paragraphs 3.2.6 and 3.2.7 and replace with “Not Used.”*

*Amend paragraph 3.3.7 to read as follows:*

“3.3.7 ~~Without prejudice to paragraphs 3.2.6 and 3.2.7, w~~Where the User ... under this paragraph 3.3.”

**UNIFORM NETWORK CODE – TRANSPORTATION PRINCIPAL  
DOCUMENT**

**SECTION B - SYSTEM USE AND CAPACITY**

**ANNEX B-1 - NTS EXIT CAPACITY  
INVITATION, APPLICATION AND ALLOCATION**

*Delete paragraphs 3.7 and 3.8 and replace with “Not Used.”*

**UNIFORM NETWORK CODE – TRANSPORTATION PRINCIPAL  
DOCUMENT**

**SECTION V - GENERAL**

*Amend paragraph 3.3.4 to read as follows:*

“3.3.4 For the purposes of paragraph 3.3.2(c)(i) and (iii) and the application of Section ~~B3.2.6 and 3.3.3(f) and paragraph 3.6 of Section B Annex B-1,~~ a User’s Value at Risk shall be treated ...is to be determined.”

For and on behalf of the Relevant Gas Transporters:

**Tim Davis**

**Chief Executive, Joint Office of Gas Transporters**