Modification proposal:	**Uniform Network Code (UNC) 268: Change to the Provisions Determining the Earliest Reading Date Applicable within the AQ Review (UNC268)**		
Decision:	The Authority[1] directs that this proposal be made[2]		
Target audience:	The Joint Office, Parties to the UNC and other interested parties		
Date of publication:	15 February 2010	Implementation Date:	To be confirmed by the Joint Office

Background to the modification proposal

Annual Quantity (AQ) represents the expected volume of gas to be used at a particular Supply Point in a year. It is an input to capacity planning, energy balancing, charging and reconciliation. The accuracy of AQs are therefore important to Consumers, Shippers and the Gas Transporters (GTs). AQs are reviewed annually and revised on 1 October each year. This revision involves the adjustment of historical consumption to a seasonal normal value:

- Historical consumption is calculated using a starting meter read and an ending meter read. Currently, the earliest possible date of a starting meter read that can be utilised to derive an AQ is 1 October 2002. This date is known as the AQ backstop date.

- The seasonal normal adjustment factor is based on a set of parameters derived from demand models using the latest view of seasonal normal weather. This view of average weather is updated every five years on the basis of new weather experience, as part of the Seasonal Normal (SN) review.

This year, the seasonal normal adjustment factor parameters to be used as part of the 2010 AQ review will be the revised parameters based on the updated view of average weather as determined by the 2010 SN review. However, as a result of timing, volume of analysis and time taken to re-run the models, the parameters only pertaining to the period post 1 October 2006 can be derived using current demand models.

Consideration is therefore being given to replacing the current static AQ backstop date with a rolling AQ backstop date, given that:

- in order to calculate AQs of supply points which use a historical consumption period prior to 2006, a manual method of calculating the seasonal normal adjustment factor would be required; and

- using data back to 2002 is not seen as representative of recent consumption.

[1] The terms 'the Authority', 'Ofgem' and 'we' are used interchangeably in this document. Ofgem is the Office of the Gas and Electricity Markets Authority.
[2] This document is notice of the reasons for this decision as required by section 38A of the Gas Act 1986.

The modification proposal

UNC268 proposes to replace the fixed backstop date with a rolling backstop date. The proposed backstop date would be 1 October in the year that is four years prior to the start of the Gas Year in which an SN review becomes effective. The new backstop date would then become effective from 1 February of the preceding Gas Year. For example:

- For an SN review which becomes effective from 1 October 2010, from 1 February 2010 the backstop date will be 1 October 2006.

- For an SN review which becomes effective from 1 October 2015, from 1 February 2015 the backstop date will be 1 October 2011.

To enable this change, an amendment is required to Section H3.2.4 of the UNC which currently specifies 1 October 2002 as the earliest reading date.

The proposed modification will negate the issues around re-running the models to create the seasonal normal adjustment factor back to 2002 and will allow a wider measurable period than was used in the 2005 SN review from which the AQ can be calculated (3 years 4 months at its shortest point and 8 years 4 months at its longest). It is believed that restricting the AQ backstop date to a rolling period will result in less non-calculations[3] and ensure that AQs are calculated using the latest SN information.

For these reasons, the Proposer considers that UNC268 is likely to further relevant objective (d) as set out in Standard Special Condition A11 (1) of the Gas Transporters Licence[4].

UNC Panel[5] recommendation

At the UNC Panel (the 'Panel') meeting on 21 January 2010, of the nine Voting Members present, capable of casting ten votes, ten votes were cast in favour of implementing the proposal. Therefore, the Panel recommended implementation of the proposal.

The Authority's decision

The Authority has considered the issues raised by the modification proposal and the Final Modification Report (FMR) dated 21 January 2010. The Authority has considered and taken into account the responses to the Joint Office's consultation on the modification proposal which are attached to the FMR[6]. The Authority has concluded that:

1. implementation of the modification proposal will better facilitate the achievement of the relevant objectives of the UNC[7]; and
2. directing that the modification be made is consistent with the Authority's principal objective and statutory duties[8].

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[3] The number of supply meter point AQs that may not be calculated due to the 'starting' meter reading falling prior to the earliest date able to be utilised.
[4] For detailed views from the Proposer and Respondents, see: www.gasgovernance.com
[5] The UNC Panel is established and constituted from time to time pursuant to and in accordance with the UNC Modification Rules.
[6] UNC modification proposals, modification reports and representations can be viewed on the Joint Office of Gas Transporters website at www.gasgovernance.com
[7] As set out in Standard Special Condition A11(1) of the Gas Transporters Licence, see: http://epr.ofgem.gov.uk/document_fetch.php?documentid=6547
[8] The Authority's statutory duties are wider than matters which the Panel must take into consideration and

Reasons for the Authority's decision

There were seven responses to the Joint Office's consultation. Of these, six respondents fully supported implementation of the proposal and one offered qualified support on the basis that it had not fully evaluated the work necessary to change its systems by the proposed implementation date. The views of the Proposer and those expressed by respondents are considered below.

The Authority considers that this proposal will better facilitate relevant objective (b), (d) and (f) of Standard Special Condition A11 of the Gas Transporter Licence and is neutral in relation to the remaining objectives.

We acknowledge the view of one respondent that the proposal would better facilitate the achievement of relevant objective (a) "the efficient and economic operation of the pipe-line system to which this licence relates". However, we consider that the proposal is more likely to impact all Gas Transporters (GTs) and not just National Grid Gas (NGG) National Transmission System (NTS). We have therefore considered this respondent's view in the context of relevant objective (b), below.

Standard Special Condition A11.1 (b): so far as is consistent with sub-paragraph (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;

As noted above, one respondent considered that this proposal would better facilitate relevant objective (a) by allowing the adjustment of AQs to the most up to date seasonal information[9]. In terms of the day-to-day physical operation of the pipeline system, we believe that more accurate AQ values may afford Shippers an opportunity to better understand demand fundamentals, thus creating an opportunity for more informed purchasing decisions. This in turn may reduce the need for NGG to undertake residual balancing actions in its role as the System Operator thereby better facilitating the economic and efficient operation of the NTS.

In addition, we understand that AQs, via their input into demand modelling, help to form the basis of many of the GTs' planning and system security activities. Improvements in the accuracy of AQs may therefore provide GTs with a clearer view of the energy needed to be transported through the pipe-line network, thereby allowing them to operate the system in a more economic and efficient manner. However, we recognise that AQs are only one of a significant number of other parameters which need to be taken into account in demand modelling and hence system planning. Therefore, we consider that the calculation of more accurate AQs may provide a limited contribution to the achievement of relevant objective (b) in this area.

Two respondents raised concerns in respect of the implementation date believing it to be too short. One respondent, who supported implementation of the proposal, suggested that a six month lead-in time would be necessary in order to manage system changes. This respondent considered that implementation within the next six months could have a material impact on its systems as the current backstop date is hard-wired into their day-to-day business systems. In turn, this could lead to them incurring increases in

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are detailed mainly in the Gas Act 1986.

[9] We note that this respondent did not explain its view beyond making this point.

development and capital costs. That said, we note that this respondent was unable to determine the materiality of these costs[10].

The other respondent who offered qualified support felt that the short notice period would require Shippers to implement manual processes to augment their automated AQ calculation methods and thus incur potentially significant costs. However, again we note that this respondent had not fully evaluated the work necessary to change its systems. We note that no other respondent raised any concerns with the implementation date.

In order to better facilitate relevant objective (b) the GTs (through the Joint Office), whose responsibility it is to determine the implementation date, will consider all the relevant factors when reaching a decision such that any implementation costs are kept to a minimum.

We therefore consider that the implementation of UNC268 may, at least marginally, better facilitate the achievement of relevant objective (b), the coordinated, efficient and economic operation of the combined pipeline system.

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;

The Proposer considered that implementation of UNC268 would lead to more accurate AQs and in turn, more accurate energy allocation, therefore impacting the amount of energy passed for reconciliation. It also considered that the resultant timely and correct allocation of energy would reduce the risk of misallocation of charges occurring between Shippers, improving cost reflectivity and therefore better facilitating effective competition between relevant Shippers and Suppliers.

One respondent agreed with the Proposer that implementation of this proposal would better facilitate relevant objective (d) by ensuring that AQs were only calculated using meter readings that relate to the updated seasonal normal adjustment factors. Having more accurate AQs would facilitate the allocation of energy and in turn, cost targeting, and therefore assist in securing effective competition between relevant Shippers and Suppliers.

In our view, it is crucial that costs are appropriately targeted to prevent distortion of competition between the relevant Shippers and Suppliers. In relation to the calculation of AQs, it is clearly important that the expected volume of gas to be used at a particular Supply Point over the year is calculated as accurately as possible to ensure that Shippers and Suppliers are not exposed to any extra or undue costs. For example, to the extent that Shippers will have better information about NDM Supply Point demand, we would expect them to be in a better position to manage their portfolios, thereby avoiding undue exposure to imbalance prices. In addition, the correct classification of a Supply Point based on its AQ should also ensure that transportation charges are appropriately targeted on to Shippers, thereby preventing the distortion of costs.

[10] While this respondent hoped that the costs would be small, it noted that it could not be confident that they would not be large.

For the reasons outline above, we consider that implementation of this proposal has the potential to better facilitate relevant objective (d), the achievement of effective competition between Shippers and Suppliers.

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;

Two respondents felt that, allowing the AQ backstop date to roll forward on a rolling five year programme would reduce the volume of analysis and time taken to re-run the models to create the seasonal normal adjustment factors prior to the rolling period. Implementing the modification proposal would remove this administrative burden and may therefore better facilitate the achievement of relevant objective (f).

We agree that implementation of this proposal will remove the administrative burden for xoserve, the industry and Ofgem to review the backstop date every five years in line with the five-yearly SN review. By ensuring the appropriate arrangements are now in place to facilitate a more efficient process going forward, we consider that the proposal better facilitates the achievement of relevant objective (f), the promotion of efficiency in the implementation and administration of the UNC.

Decision notice

In accordance with Standard Special Condition A11 of the Gas Transporters Licence, the Authority, hereby directs that modification proposal UNC268: 'Change to the Provisions Determining the Earliest Reading Date Applicable within the AQ Review' be made.

Ian Marlee
Partner, Trading Arrangements

Signed on behalf of the Authority and authorised for that purpose.