

Review Group Report
Review Proposal Reference Number 0329
Review of Industry Charging and Contractual Arrangements – DM Supply Point
Offtake Rates (shqs) and DM Supply Point Capacity (soqs)
Version 1

This Review Group Report is presented for the UNC Modification Panel's consideration. Scotia Gas Networks indicated to the Review Group that it is their view that the Review Group Report should detail any changes required to the Supply Point capacity regime in relation to DN DM sites to ensure SPORs are representative of Shipper / End User requirements. The Review Group considers that Modifications provide the appropriate mechanism for taking the issues forward.

1 Review Proposal

Scotia Gas Networks raised Review Proposal 0329, Review of Industry Charging and Contractual Arrangements – DM Supply Point Offtake Rates (shqs) and DM Supply Point Capacity (soqs), (available at: www.gasgovernance.co.uk/0329). The agreed Terms of Reference for the Review are attached below as Annex 1.

2 Review Process

In accordance with the Modification Rules, at its meeting on 19 August 2010, the Modification Panel determined a Review Group should be formed to consider this Proposal. A workplan was agreed at the initial meeting, and the Review Group met on seven occasions. All papers in support of the meetings are available at: www.gasgovernance.co.uk/0329. This Review Group Report was compiled by the Joint Office and approved by Review Group attendees.

3 Areas Reviewed

A summary of the discussions is:

- *The group undertook consideration of the impacts associated with too high / low SHQs – potential for sterilising system capacity, unnecessary reinforcement and increased cost or a risk to security of supply;*
- *The group concluded that the current NDM regime is robust and still works and whilst not the complete solution, value could be found in focusing on SHQs;*
- *The group acknowledged that where sites exceed their contracted (SHQ) levels planning and operational issues can arise – in extremis, sites may be cut-off;*
- *The group considered that a high actual SHQ (where a site has a low contracted SHQ) is a potential safety issue where network planning is based on contractual values.*
- *The group recognised that SHQ accuracy is sought to provide accurate notification of system utilisation, and not as a mechanism to remove capacity;*
- *In considering load factors the group concluded that size and geographical location have a bearing, especially for the larger NDM sites;*
- *The DNs remain confident that their algorithms for the 'domestic' NDMs are appropriate, as any variation in load has little impact on network planning;*

- *Opinions remained divided as to whether customers need to be treated differently based on size, with some believing that understanding the type of customer is more important;*
- *National Grid provided network referrals related supporting evidence to explain the 16x rule;*
- *DNs confirmed that they utilise telemetry flow rates (at VLDMC sites) for operational purposes;*
- *It was acknowledged that whilst SHQs drive cost, these are not incorporated into the Transportation charges passed to Shippers as these are mainly SOQ based;*
- *In summary SHQs are utilised for planning whereas SOQs are utilised for pricing;*
- *Examples of instances where a change in SHQs had led to a potential network investment saving were provided;*
- *Scotia Gas Networks provided a presentation on the current UNC DM supply point requirements, whilst summarising UNC0275 implications for allowing capacity reduction(s);*
- *Current Code rules ensure that SOQ / SHQ changes >16x result in an automatic referral to the network for consideration;*
- *Daily capacity patterns are taken into account for network planning purposes;*
- *The impact of pressure surveys on SHQs (where a site is offtaking more gas than its SHQ) which could potentially result in an exaggerated statement of demand and subsequent over-investment was discussed;*
- *It was considered that should meter capacities be used as the ultimate system constraint this could incentivise the networks to invest based on the size of the meters which is likely to be a costly solution;*
- *Inappropriate setting of SHQs could lead to sites paying charges below the cost reflective level;*
- *Transporters remain keen to see a reduction in SHQs due to improved accuracy, which could prevent unnecessary investment and ultimately leading to a reduction in customer costs – not a unanimously shared view due to concerns about capacity being removed when end users do not wish to relinquish it since usage may change in future;*
- *DNs examined a charging framework based around individual site ratios between SHQ & SOQ with a scaling factor utilised to ‘adjust’ charges;*
- *It was acknowledged that there might be merit in any ratios being accepted from 1 to 24, although ratios that have drifted outside 1:4 could ‘trigger’ Transporters to investigate. It was acknowledged that any ratio may be appropriate where customers wish to hold, and be exposed to, the costs of providing that capacity;*
- *The group acknowledged that further consideration of the SHQ / SOQ ratio would be required along with accurate determination of the costs imposed on networks, due in part, to the impact of peaky load profiles;*
- *Transporters agreed to provide a report highlighting sites with (SHQ / SOQ ratio) discrepancies / differences >20%;*

- *The group acknowledged that it is not the Transporters responsibility to determine SHQs, but could support a review of site SHQs by providing actual site usage data;*
- *It was acknowledged that there exist two diametrically opposed options – to conclude that SHQs are unimportant and stop collecting the information, relying instead on other planning approaches, or alternatively, recognise that SHQs are important and make the regime work such that accurate data is made available;*
- *Scotia Gas Networks already have provision for within day information via their existing reporting systems;*
- *A lack of hourly information for Shippers means they struggle to identify and rectify issues in a timely manner;*
- *The group felt that a process which directly incentivises the provision of correct SHQs is preferable to a ratchet type solution;*
- *Transporters are to engage with Shippers to address out of synch SHQs;*
- *Ofgem stated that they would welcome any equitable process or incentive capable of driving efficient and effective network investment. However, it remains the responsibility of the DNs to justify their charging structures in line with their licence obligations to ensure their investment is efficient and economic – to do this they will need to demonstrate inclusion of consideration of both NDM and DM loads;*
- *Scotia Gas Networks provided a presentation of analysis and potential UNC changes requirements governing the setting of Supply Point Offtake Rates and Supply Point Capacity to incentivise Users to provide actual required usage volumes;*
- *Any proposed changes which could potentially remove existing customer rights, increase costs or decrease security by removing flexibility (to ramp-up) would not meet with the unanimous approval of the group;*
- *In essence the group agree it boils down to the correct and fair apportionment of costs across all users;*
- *Communication between interested, impacted parties remains a concern, although any change to the current charging regime which promotes improvements in this area would be seen as beneficial;*
- *In its CAPEX re-opener deliberations the Authority had considered the impact of any proposed change in the regime on all users, regardless of size;*
- *The group felt that bi-lateral discussions would be preferable to direct charging changes;*
- *Some view recent network capacity ‘tensions’ as stemming from the Networks taking on new loads – these in turn impact upon customers;*
- *In considering the proposed changes to the charging structure, it was recognised that some parties would gain and other lose;*
- *Some parties felt that the potential to introduce additional layers into the charging regime is a concern and further justification would be required;*
- *The AQ process is seen as providing indirect information appertaining to SOQs, although this is absent in the DM sector;*

- *Under the UNC, users are obliged to provide information on any increase / decrease in their AQs;*
- *A 'bottom-stop' review is not being proposed;*
- *How to best incentivise behaviours via investment signals is being considered elsewhere;*
- *A timetable for roll-out of any potential changes would be beneficial;*
- *It was noted that as more interruptible loads 'drop-off' the system over time, more flexibility may become available;*
- *Three new SHQ charging options were presented by SGN;*
- *Options 1 & 2 attempt to adjust SOQ based charges to reflect SHQ variations;*
- *It was felt that the transparency surrounding the setting of appropriate and different percentage levels would be of paramount importance;*
- *The WWU UNC modification for DM/NDM Elective regime could possibly impact on the view of the future role of SHQs and SOQs going forward;*
- *Option 3 was not widely supported whilst option 2 might be preferred if a charging option were adopted, because it provides a basis for including the SHQ factor within charges;*
- *The group considered the rules for decreasing DM SHQ/SOQ and removal of bottom-stop restrictions;*
- *It was recognised that the ability to reduce SOQs to what was actually required was beneficial for network planning;*
- *The group accepted that Users should be able to reduce SOQs at any time, but that there should be limited opportunities in order to avoid continual within-year adjustments.*

4 Recommendation

The Review Group agreed that two modifications should be raised to take forward the identified issues:

1. Introduce a requirement for transporters to provide Shippers with details of sites for which the actual SHQ appears to differ from booked, and for Shippers to confirm whether those SHQs are required or should be adjusted (*raised by Southern Gas Networks as Modification 0390*); and
2. Relax the rules for decreasing DM SHQ/SOQ and removal of bottom-stop restrictions, such that one reduction can be made in any 12 month period (*a modification is being prepared by Wales & West Utilities*).

The Panel is invited to accept this Report.

Annex 1: Terms of Reference

Background

In March 2010 Ofgem published their decision letter detailing the outcome of Scotland Gas Networks' (ScGN) application to re-open the current Gas Distribution Price Control. In light of an additional capital expenditure requirement to facilitate network re-enforcement projects resulting from UNC Modification Proposal 090, 'Interruption Reform', the Ofgem decision letter provided an approval to an adjustment of the interruption incentive allowance to take into consideration specific re-enforcement projects.

Although ScGN were permitted additional capital allowances Ofgem detailed within their decision letter certain concerns relating to the current incentives placed upon Shipper Users to provide Supply Point Offtake Rate (SPOR) values (more commonly referred to as supply hourly quantity or shq) to the Transporters which are representative of their usage. The decision letter also specified that Gas Distribution Network Operators (GDNs) should instigate a Review Process to consider if changes should be made to incentivise customers to consider their SPOR usage levels. In addition Ofgem suggested that current customer capacity charges were broadly independent of their contracted SPOR even where the contracted SPOR may require GDNS to incur additional cost in meeting these requirements.

To meet the objectives detailed in Ofgem's decision letter ScGN have raised this UNC Review Proposal to consider the issues raised and ultimately to determine whether any modifications are required to the UNC to rectify any disincentives in this area. To ensure all gas industry participants' views are included in this process ScGN would encourage the active involvement of not only Shipper Users and Transporters but also End User consumer representatives.

Nature of Proposal

It is ScGN's intention that this Review Proposal considers the UNC arrangements for the provision of Supply Point Capacity and Supply Point Offtake Rates by Shipper Users to DNs for all Daily Metered Supply Points. For clarity it is not envisaged this Review Proposal will cover arrangements for Supply Points connected to the National Transmission System although this would not rule out an analysis of current NTS arrangements in relation to DN connected DM sites. In addition to the comments made within the Ofgem decision letter regarding the incentives on Shippers to provide reflective SPORs, ScGN also consider that it would be appropriate to include and focus on the enduring arrangements associated with the setting of minimum and maximum off take rates, specifically with reference to the reduction of and increase of such rates. Following the implementation of UNC Modification Proposal 0275 in December 2009, which provided a temporary mechanism to allow flexibility in capacity booking for DM sites, Ofgem specified any enduring solution would require further analysis and comprehensive review. As any arrangements associated with extending such a regime would impact on a Supply Point's SPOR and SPC, ScGN consider it would be appropriate to include these elements in this UNC Review.

Review Group Terms of Reference

It is proposed that the UNC Review group considers the following areas within its remit:

- Impact on DN investment decisions resulting from the current and any future SPOR/SPC nomination process for the whole GDN GB market, including CSEPS.
- Potential changes to UNC rules governing the setting of Supply Point Offtake Rates and Supply Point Capacity to incentivise Users to provide actual required usage volumes (to include a review of the Supply Point Ratchet regime)

- Impact on DN Transportation charges and recovery of such charges in relation to any changes to the SPOR / SPC regime for the whole GDN GB market, including CSEPS.
- Potential changes to the current process establishing the dynamic between the Supply Point Offtake Rate and the Supply Point Capacity, including the rule specified in UNC TPD Section G 5.4.1 (SPC = between 24 x and 4 x the SPOR).
- The process and timing for reducing both the Supply Point Offtake Rate and the Supply Point Capacity including the 16x rule.
- The process and timing for increasing both the Supply Point Offtake Rate and the Supply Point Capacity rate including the 16x rule.
- Potential impact on end users of any proposed changes.
- Monitoring accuracy of SPORs and SPCs on an ongoing basis.
- Safety issues in relation to Users exceeding SPORs and incentives to minimise any such occurrence.
- Consider impacts on the new connections/siteworks process.

Suggested Aims and Outputs

It is envisaged that this Review Group will produce a report recommending any necessary changes to the UNC. It is recommended that the Review Group complete its work within a nine-month period. If necessary this could be extended by seeking agreement of the Modification Panel.

The Review Group should also look to include any draft Modification Proposals as part of the final report (this does not prevent related Modification Proposals being raised during the period of the Review Group).

Scope and Deliverables

The Review Group shall focus on changes to the UNC and Network planning processes, but also identify where improvements could also be made to areas of governance outside of the UNC.

The Review Group is to consider recommendations based on evidence provided during the topic meetings.

Limits

The Review Group will focus on developing recommendations and UNC Modification Proposals that efficiently address any issues identified in a proportionate and cost effective manner. The Review Group will consider changes required to procedures and processes within UNC, however it will not develop changes for non-code processes but will request reports from review group members who can influence changes with the appropriate industry body.

The Review Group is to be mindful of related industry obligations, processes and previous reports:

1. UNC;
2. Flow of information between UNC parties;
3. Licence and Legal obligations;
4. Industry standards and Codes of Practice.

Composition of Review Group

This review group is open to all Transporters and their agents, Code Users, Ofgem and consumer representatives.

A Review Group meeting will be quorate provided at least 2 Transporter and 2 User representatives are present.

Timetable

It is proposed that a period of nine months be allowed to conclude this review, however given the complexity of the issues this may need to be extended depending on how this review develops.

Although the frequency of meetings will be subject to review and potential change by the Review Group it is suggested that the initial frequency of the meetings be monthly.

Meetings will be administered by the Joint Office and conducted in accordance with the Chairman's Guidelines.

Review Group Workplan	
Meeting Number	Topics for Discussion
1 – 21/09/10	Introductions and review terms of reference
2 – 19/10/10	Impact of SOQ/SHQ on DN Investment decisions. To include:- <ul style="list-style-type: none"> • overview of SGN (covering DM and NDM) planning process (which data items are used and their source, why SHQs are used, overview of IGEM network planning document, why there is a 16 times rule for network referral but not below this value) • impact of SOQ / SHQ on SGN planning decisions. • impact of SOQ / SHQ on SGN physical network operation. • Link to investment, price control and charges • Other DNs confirmation of any significant differences in planning process
	Overview of current UNC rules on setting SOQ / SHQ (evidence that they create a problem, especially with respect to incentives to state an accurate SHQ)
4 – 13/12/10	Potential changes to UNC rules governing the setting of SOQs / SHQs. To include:- <ul style="list-style-type: none"> • the current SOQ / SHQ relationship (G 5.4.1). • the current SOQ Ratchet regime. • Data availability and provision to support change • Potential changes to network planning to address identified issues
5 – January 2011	Impact on DN Transportation charges and recovery of such charges in relation to any changes to the SPOR / SPC regime (including the move to 100% capacity and its implications (if any))
6 – February 2011	The process for increase and decrease of SOQ / SHQ. (Monitoring and updating of SOQ / SHQs on an ongoing basis)
7 – March 2011	The process for increase and decrease of SOQ / SHQ. (Monitoring and updating of SOQ / SHQs on an ongoing basis)
8 – April 2011	Conclude Review Group Report.