Joint Office of Gas Transporters

Draft Modification Report

0335: Offtake Metering Error – Payment Timescales

and

0335A: Significant Offtake Metering Error – Small Shipper Payment Timescales

Consultation close out date: 02 December 2011

Respond to: enquiries@gasgovernance.co.uk

Organisation: **SGN**

Representative: Joel Martin

Date of Representation: 1st December 2011

Do you support or oppose implementation?

0335 - ~~Support/Qualified Support/Neutral~~/**Not in Support**/~~Comments*~~

0335A - **Support**~~/Qualified Support/Neutral/Not in Support/Comments*~~

If either 0335 or 0335A were to be implemented, which would be your preference?

Prefer ~~0335/~~**0335A**

Please summarise the key reason(s) for your support/opposition.

Thank you for providing SGN with the opportunity to respond to the consultation exercise relating to UNC Modifications 0335 and 0335A. As we have specified above SGN does not support the implementation of **UNC Mod 335** based on the significant retrospective element the proposal would impose on Distribution Networks, specifically Scotland Gas Networks in relation to the Aberdeen offtake metering error. We have further specified below the reasoning behind our decision including our view on the arguments put forward by the proposer of Modification Proposal 335 on the better facilitation of the licence objectives.

As the proposer of the alternative UNC Modification Proposal **MOD 335A** we would wish to provide support for its implementation; again we have provided further comments below in relation to SGN's reasoning for supporting this alternative approach.

UNC MODs 335.

The background to the original proposal stemmed from a number of significant NTS to LDZ offtake metering errors identified and notified to the industry during 2009 and 2010, namely the significant offtake meter errors at Braishfield and Aberdeen, which when combined totalled an under recording of gas flowing into the respective LDZs of approximately 4.38 terra watt hours. Modification Proposal 0335, raised by RWE Npower, would introduce into the UNC two new elements. Firstly, the Modification looks to financially incentivise Distribution Networks (DNs) to further improve the accuracy and reliability of their offtake metering equipment and associated assurance processes. It is also the Modification's intention to provide a cushion to the LDZ Shippers in relation to a cash flow impact a large metering error may create and the application of this relief in retrospect.

Offtake Metering - Financial 'Incentives'.

Implementation of MOD 0335 would require the DN to fund both the energy costs and the transportation commodity charges associated with an offtake metering error and then recover from the LDZ Shippers these costs over a period identical to the original offtake error. DN financing costs associated with funding these energy charges would be substantial. Certainly in relation to the Aberdeen offtake metering offtake error the cost to SGN of funding these energy charges would be in the region of £3M (total energy charges for Aberdeen would be in the region of £65M[1]). The proposer of Modification 0335 suggests that this financial cost (as we do not consider this to be an incentive) will drive DNs to invest in new offtake metering equipment and also improve their procedures to minimise the risk of incurring these substantial costs associated with the under recording of gas. SGN have made clear throughout the discussions on UNC MOD 0335 that it is our intention to include within our RIIO GD1 business plan capital expenditure for the installation of modern ultra sonic metering equipment at our offtakes that have significant flows. We have also, in conjunction with the other DNs, already introduced an offtake metering improvement plan which targets the previous causes of offtake errors to reduce the likely re-occurrence of these incidents and also introduces increased controls around offtake metering in general.

LDZ Shipper Cash Flow Impacts.

Following the introduction of the UNC Related Document, "Measurement Error Notification Guidelines for NTS to LDZ and LDZ to LDZ Measurement Installations", which was approved by the Uniform Network Code Committee following lengthy Shipper and Transporter development, the notification period and processes for LDZ offtake metering errors was improved. This process requires the immediate notification to the industry by the DN following the identification of an offtake metering error and regular updates relating to the progress in compiling the error report are also provided. Of the three significant metering errors which have been notified and invoiced to the industry since April 2008, the average period between first notification and final invoicing was 15 months and of the two current

[1] Approximate figure.

significant offtake meter errors which have yet to be invoiced and are unlikely to be for some time, Aberdeen was notified 14 months ago and Horndon 11 months ago.

Through this process Shippers are now afforded a considerable period of time following first notification of an error to accrue for unbilled costs associated with an under recording of gas into the LDZ. During this notification period and immediately preceding the notification period the gas Shipper and Supplier will have invoiced its customers for the charges associated with the use of gas within the LDZ. However, during both the error period and the subsequent notification period, following the incorrect recording of gas flowing into the LDZ, the LDZ Shippers will not have been invoiced the correct amounts for both gas transportation commodity and gas energy charges.

Therefore, with the invoicing of the offtake error which is correcting the initial under billing, it would be inequitable to require the Distribution Network to continue to subsidise this arrangement in line with the measures MOD 335 would introduce. We would consider that the Shippers will have been provided with sufficient notice of the pending invoice associated with the offtake error and therefore do not require further shielding from the cost of the gas they have supplied to their customers.

<u>Retrospective element of MOD 335.</u>

One of the key stated objectives of MOD 335 is to introduce incentives on DNs to improve the reliability of offtake metering following implementation of the MOD. We do not agree that implementation of the MOD would efficiently deliver this requirement and also that the existing improvements in place to facilitate this objective (along with planned improvements in the next price control period) are already providing increased confidence in offtake metering. To confirm, we do not agree the measures MOD 335 would introduce could place incentives on the DNs to improve offtake metering, they would only act as a penalty on DNs where an error was discovered.

However, even if we were to agree with the proposer of MOD 335 that the measures introduced by the proposal were a suitable measure to encourage DNs to improve offtake metering; we would still strongly disagree with the retrospective application of the obligations within the MOD. The business rules as drafted in the MOD require that once the final meter error report associated with the offtake error has been published the rules linked to the DN funding the energy and commodity charges would be switched on. Were Ofgem to implement MOD 335 the obligations introduced into the UNC would cover offtake metering errors identified and notified to the industry prior to (a) the MOD being implemented and (b) Modification 0335 being raised. In relation to the Aberdeen offtake metering error SGN would incur substantial costs associated with funding LDZ Shipper gas costs for an event which occurred prior to the obligations MOD 335's implementation would introduce.

Even if it was considered that MOD 335 introduced suitable drivers on DNs, we do not understand how these could be considered as an 'incentive' when applied retrospectively, covering events when the provisions the MOD would introduce were not actually in place? Within the Ofgem[2] document 'Guidance on Code Modification Urgent Criteria' there is detailed a view on the retrospective application of code modification proposals and circumstances which may justify the application of measures retrospectively. We do not consider that any of the suggested criteria detailed within the advice would justify the implementation of the retrospective elements of MOD 335 and as a result would urge Ofgem to reject the implementation of this Modification Proposal on these grounds alone.

<u>UNC MOD 335A</u>.

As the proposer of the alternative Modification Proposal 335A we would like to offer support for its implementation. Modification Proposal 0335A restricts the subsidy of Shipper gas costs to smaller Shipper organisations following the invoicing of an offtake meter error, as SGN

[2] http://www.ofgem.gov.uk/Licensing/IndCodes/Governance/Documents1/Ofgem%20Guidance%20on%20Code%20Modification%20Urgency%20Criteria.pdf

recognise that there may be an adverse impact on these specific organisations. It would appear to SGN from recent stakeholder discussions that smaller Shipper organisations, due to their limited access to credit and the disproportionate impact a meter error may have on their cash flow compared to larger organisations, that it may be appropriate to offer these Shippers some relief in relation to the period over which the incurred costs should be paid. MOD 335A also removes any retrospective application of these new obligations based on the arguments stated previously in relation to UNC MOD 335.

Are there any new or additional issues that you believe should be recorded in the Modification Report?

None.

Relevant Objectives:

How would implementation of these modifications impact the relevant objectives?

Standard Special Condition A11.1 (a)

SGN do not agree with the proposer of MOD 335 regarding the better facilitation of Standard Special Condition A11.1 (a). The proposer suggests the implementation of MOD 335 would better facilitate A11.1 (a) as it would place a cash flow incentive of DNs to invest in offtake metering which would lead to improved accuracy and reliability of offtake meter readings. Firstly SGN have already introduced improved offtake metering assurances through improved meter validation procedures and in addition we have also specified the requirement for increased capital allowances to fund new ultra sonic metering equipment at key LDZ offtakes within our RIIO GDPCR 1 business plan. We believe this is the correct mechanism to introduce improved offtake metering arrangements within our networks and not a penal measure which would only lead to increased costs to the DNs.

Standard Special Condition (d) (i) & (ii)

We do not agree with the proposer of MOD 335 that the implementation of the MOD would better facilitate Standard Special Condition A11.1 (d) (i) (between Shippers). The proposer suggests that Shippers will be able to 'manage costs more effectively' as costs will be more 'predictable' and within an expected timescale. SGN would argue that sufficient timescales are already provided with the existing UNC arrangements to provide Shippers with sufficient notice of costs associated with an under recording of gas at an offtake. We also note the proposer's argument that MOD 335 would improve competition for smaller Shippers as implementation of Mod 335 would improve their cash flow situation in the event of an offtake meter error. As the rules in MOD 335 would provide for financial relief to all Shippers' cash flow standings, including the big 6 Suppliers, we fail to understand how this would substantially benefit small shippers only to any material extent and may in fact adversely benefit larger Shippers over smaller organisations.

As the proposer of MOD 335A we support the Modification's focus on smaller Shippers and understand that there may be an issue with smaller Shippers gaining access to funds associated with the payment of large offtake meter error charges. Despite the fact all Shippers are provided with sufficient notice of these charges we understand there maybe an adverse impact on smaller Shippers which would justify financial relief for these Shippers only. This in turn would facilitate improved competition between smaller and larger Shippers and Suppliers.

Standard Special Condition (e)

We do not agree with the proposer of MOD 335 that its implementation would mitigate any risk of a Shipper being cash called following the invoicing of large meter error. Firstly all Shippers are invoiced for the gas associated with an offtake error in relation to the market share they held during the period of the error. Therefore the amounts invoiced should reflect the income Shippers have already banked from their customers but have not in effect paid for. SGN consider that the current increased notice periods associated with the invoicing of offtake meter errors already provide a sufficient basis to allow Shippers to plan for these costs.

Impacts and Costs:

What analysis, development and ongoing costs would you face if these modifications were implemented?

As we have previously stated SGN would incur substantial costs associated with the implementation of MOD 335 due to its retrospective nature.

Implementation:

What lead-time would you wish to see prior to these modifications being implemented, and why?

We believe MOD 335A could be implemented immediately after any Ofgem direction. MOD 335 could also be implemented immediately after any Authority direction as the timing of its implementation does not have any bearing on its retrospective application, this would apply regardless of an implementation date for offtake errors identified prior to the MOD's implementation where the final error report had not already been published.

Legal Text:

Are you satisfied that the legal text will deliver the intent of each modification?

Yes.

Is there anything further you wish to be taken into account?

Please provide any additional comments, supporting analysis, or other information that that you believe should be taken into account or you wish to emphasise.

No.