

Modification proposal:	Uniform Network Code (UNC) 485: Introduction of long-term use-it-or-lose-it mechanism to facilitate compliance with the EU Congestion Management Procedures		
Decision:	The Authority ¹ consents ² to this modification ³		
Target audience:	The Joint Office, Parties to the UNC and other interested parties		
Date of publication:	20 August 2014	Implementation Date:	30 September 2014

Background to the modification proposal

The final report of the European Commission's (the "Commission") sector inquiry into competition in gas and electricity markets (published in January 2007)⁴ noted (amongst other things) the lack of effective competition in European markets and ineffective congestion management across Europe.

In response, a suite of legally binding European Union (EU) legislation, referred to as the Third Package⁵, on European electricity and gas markets was introduced and adopted on 13 July 2009. The Third Package was transposed into GB law on 10 November 2011⁶.

The Third Package created a new legal framework to promote cross-border trade. It requires a number of legally binding Guidelines and 'Network Codes' to be established and implemented. Taken together, these aim to promote liquidity, improve integration between Member States' gas markets and promote the efficient use of interconnectors to ensure that gas flows according to price signals, i.e. to where it is valued most.⁷

The first to be implemented is a set of legally binding 'Guidelines' aimed at tackling contractual congestion, whereby gas transportation capacity is fully booked but not fully used. This situation may occur where there is physical capacity to flow more gas, but the right to flow it is tied up and is being hoarded by a network user(s) so that others cannot gain access to it. Contractual congestion results in inefficient use of gas transportation assets and is a barrier to cross border trade.

The Guidelines require a number of Congestion Management Procedures (CMPs) to be implemented by 1 October 2013. These aim to enhance the efficient use of transportation capacity by bringing unused capacity back to the market on a firm basis, thereby making it available to market participants who wish to make use of it.

The CMPs required by the Guidelines include:

¹ References to the "Authority", "Ofgem", "we" and "our" are used interchangeably in this document. The Authority refers to GEMA, the Gas and Electricity Markets Authority. The Office of Gas and Electricity Markets (Ofgem) supports GEMA in its day to day work.

² This document is notice of the reasons for this decision as required by section 38A of the Gas Act 1986.

³ 'Change' and 'modification' are used interchangeably in this document.

⁴ <http://ec.europa.eu/competition/sectors/energy/inquiry/>

⁵ In relation to gas, the Third Package includes Directive 2009/73/EC of the European Parliament and of the Council of 13 July 2009 concerning common rules for the internal market in natural gas and repealing Directive 2003/55/EC (the "Gas Directive") and Regulation (EC) No 715/2009 of the European Parliament and of the Council of 13 July 2009 on conditions for access to the natural gas transmission networks and repealing Regulation (EC) No 1775/2005 (the "Gas Regulation").

⁶ The relevant GB legislation is the Gas and Electricity (Internal Market) Regulations 2011

⁷ See Article 8(6) of the Gas Regulation for the areas to be covered by Network Codes.

- a) Capacity increase through oversubscription and buy-back (OSBB).⁸ This is where Transmission System Operators (TSOs) offer capacity in excess of their technical capability where they expect booked capacity not to be used. Where users signal that they intend to flow more gas than the system can carry, TSOs may then buy-back some of this capacity to reduce flows on the system.
- b) Surrender of contracted capacity.⁹ This refers to a process where shippers who hold capacity (i.e. the right to flow gas) but who do not intend to use it can offer this capacity back to the TSO to be reallocated.
- c) A long-term use-it-or-lose-it (LT UIOLI) mechanism.¹⁰ Here, capacity which is deemed to be systematically under-utilised can be removed from the shipper and made available to others in future auctions.

The Guidelines entered into EU law through the Commission Decision of 24 August 2012 to amend Annex I to the Gas Regulation. They apply to interconnection points (IPs) between adjacent entry-exit systems, irrespective of whether these are physical or virtual, in so far as these points are subject to booking procedures.

The modification proposal

On 17 July 2014, the Final Modification Report (FMR) for UNC485 was published on the Joint Office website. UNC485 was raised by National Grid Gas (NGG) (the proposer) in February 2014. It builds on NGG's existing congestion management processes by introducing a number of new defined terms and processes to the UNC to facilitate compliance with the CMP Guidelines.

Specifically, this will entail the following processes:

- NGG will monitor Users' utilisation of their Available System Capacity at IPs over two six month periods each year: 1 April to 30 September, and 1 October to 31 March;
- After each six month period, NGG will alert a User that it is at risk of withdrawal where, in accordance with the principles set out in the Guidelines, it has under-utilised capacity (an Underutilisation Notification);
- Where NGG provides two consecutive Underutilisation Notifications to a User in respect of two consecutive six month monitoring periods (at the same IP), it shall include an alert to the User that it is at risk of withdrawal and that the Authority shall require information from the User as to the reason(s) for the identified underutilisation. This justification will inform the Authority's decision as to whether any capacity withdrawal should take place.

On implementation of this Modification, NGG will be required to operate a number of new manual processes combined with existing functionality, which may result in additional

⁸ CMP Guidelines 2.2.2.

⁹ CMP Guidelines 2.2.4.

¹⁰ CMP Guidelines 2.2.5.

administrative costs. However, these processes are only to be applied at IPs and, as such, these costs are not expected to be excessive.

UNC Panel recommendation¹¹

At its meeting of 17 July 2014, the UNC Panel: (i) considered the workgroup report on the modification proposal and the two responses to the industry consultation, which both supported the proposal; and (ii) voted unanimously to recommend implementation of the modification proposal.

Our decision

We have considered the issues raised by the modification proposal and the FMR dated 17 July 2014. We have considered and taken into account the responses to the Joint Office's consultation on the modification proposal which are attached to the FMR.¹² We have concluded that:

1. implementation of the modification proposal will better facilitate the achievement of the relevant objectives of the UNC;¹³ and
2. directing that the modification be made is consistent with our principal objective and statutory duties.¹⁴

Reasons for our decision

We note that the two responses to the Joint Office's consultation were both supportive of implementing the modification proposal. We agree with the proposer, the UNC Panel and those respondents who commented that the modification proposal should be considered to better facilitate achievement of Relevant Objective (g). We consider that the modification proposal is neutral in relation to the other Relevant Objectives.

Relevant Objective (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

As noted by the proposer, the UNC Panel and consultation respondents, UNC 485 introduces a LT UIOLI mechanism that is required by the CMP Guidelines. These Guidelines form part of the Gas Regulation and are a legally binding decision of the European Commission. We therefore agree that implementation of the modification proposal would better facilitate the Relevant Objective regarding compliance with the Gas Regulation.

Other issues

One consultation respondent expressed a preference for the provision of monthly capacity utilisation reports, rather than receiving these only every six months. The

¹¹ The UNC Panel is established and constituted from time to time pursuant to and in accordance with the UNC Modification Rules.

¹² UNC modification proposals, modification reports and representations can be viewed on the Joint Office of Gas Transporters website at www.gasgovernance.co.uk.

¹³ As set out in Standard Special Condition A11(1) of the Gas Transporters Licence, available at: <https://epr.ofgem.gov.uk/Content/Documents/Standard%20Special%20Condition%20-%20PART%20A%20Consolidated%20-%20Current%20Version.pdf>.

¹⁴ The Authority's statutory duties are wider than matters which the Panel must take into consideration and are detailed mainly in the Gas Act 1986 as amended.

respondent notes NGG's assertion that shippers can create their own monthly reports, but suggests it would be preferential to have these provided directly by NGG. However, we consider that the current proposal provides shippers with sufficient opportunity to both monitor and effectively manage their level of utilisation.

The same respondent also noted the Authority's intention to publish a guidance note, setting out how Ofgem would decide on capacity withdrawal actions. The respondent suggests this would help manage shipper expectations and provide industry with transparency. We recognise the benefits such guidance could provide, and will endeavour to make this publicly available in a timely manner. However, we note that any such guidance will not represent an exhaustive list of justifications for capacity underutilisation deemed to be proper by the Authority and that the Authority retains the ability to apply its discretion on a case-by-case basis.

Decision notice

In accordance with Standard Special Condition A11 of the Gas Transporters Licence, the Authority hereby directs that modification proposal UNC485: *'Introduction of Long-term use-it-or-lose-it mechanism to facilitate compliance with the EU Congestion Management Procedures'* be made.

Rob Mills

Interim Associate Partner, Wholesale Markets

Signed on behalf of the Authority and authorised for that purpose