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Dear Colin,

Concerns regarding the inability to utilise transferred capacity for optional charging in recent optional charging proposals

Following the withdrawal of UNC modification 718 and its alternatives, we would like to raise our concerns on the ongoing development of optional charging proposals and more widely the implementation of UNC 678/A. If Ofgem still wishes to implement UNC 678 this year, which, for the record, given the current national emergency we do not believe to be expedient, it's vital that the charging framework is complete and includes proper consideration for storage discounts and a fully functional optional charging solution.

Specifically, it has become recently apparent the solution in UNC Mod 718 (and alternatives), did not allow transferred capacity to be utilised for optional charging due to insufficient time to implement the required systems changes by October 2020. In our view this changes the characteristics of existing capacity if it can no longer be transferred to optimise optional charging arrangements which we believe is not in scope of TAR NC.

If these proposals were to be re-raised in their current form without an additional solution for transferred capacity this would be operationally disruptive to current optional charging arrangements and lead to the sterilisation of already acquired, but ineligible entry capacity

Potential implications

Below are illustrations of how existing capacity is used in optional charging arrangements and the implications if this can no longer continue.

1. Beach/NBP swaps

These are performed between two separate counterparties in order to optimise the locational flow of gas **on a within day basis**, particularly at Bacton interconnectors, but also in relation to power station supply agreements. For example:

Worked example:

Shipper A is an upstream producer and is delivering 100,000 therms into the NTS at Bacton AND HAS purchased Bacton entry capacity in order to do so.

Shipper B is exiting 100,000 therms from Bacton IUK to deliver into the continent.

Shipper A sells to Shipper B 100,000 therms at the Bacton entry point, and transfers Bacton entry capacity to the other shipper (to facilitate the entry of gas by counterparty B).

Shipper B sells back the same volume at the NBP (so that the net balance of both Shippers remains the same). Shipper B uses the optional commodity charge on this 100,000 therms, and shares this saving with Shipper A accordingly.

If transferred capacity cannot be used for optional charging, this results in:

- A. Shipper A still holding existing capacity but does not transfer to Shipper B, and Shipper B rebooks the same volume of capacity (to take advantage of the optional capacity charge) – **this leads to double booking, sterilization of Shipper A's capacity and potential commercial congestion; OR**
- B. Neither Shipper A nor Shipper B purchase entry capacity until after the Beach/NBP swap is concluded (often within day around midnight) – **this leads to all shippers leaving entry capacity decisions until late within day, which is not without risk, unhelpful to NG NTS in its management of the network and may have impacts on flows if shippers are unable to obtain sufficient capacities.**

2. Vertically integrated companies – upstream issues

Many energy companies are vertically integrated combining both upstream and downstream entities. It's common practice for upstream entities to purchase entry capacity to signal investment or simply hedge these costs against future price movements or capacity unavailability. Often upstream volumes and the corresponding capacity is transferred from the upstream entity to the downstream entity to simplify trading, as this downstream division has the operational capability to manage exit flows and utilise optional charging for NTS connected customers or interconnection points.

If transferred capacity cannot be used for optional charging, this will disrupt the commercial operations of the corporate structure, with the one solution being for the upstream entity to build downstream capabilities which is costly and burdensome.

3. Vertically integrated companies - downstream issues

Similarly, integrated energy companies may have a supplier business to deliver gas to retail customers and large industrials. If optional charging is available, the entity holding the supply licence will satisfy this demand by purchasing volumes at the beach entry point from its parent shipper (who is an upstream producer), in a similar way to the Beach/NBP swap model above.

In this case, the ineligibility of capacity transfers for optional charging could result in unnecessarily inflated costs to customers if the full savings cannot be obtained by shippers and passed through to suppliers and customers.

Possible solutions

We believe there may be existing tool available that could provide the basis for a short term or long-term solution such as:

- **PRISMA and introducing 'Assignment' into the UNC:** introducing assignment in the UNC to allow the liability of capacity to be transferred via PRISMA so the optional charging tariff is levied on the assignee. This functionality exists for other TSOs.
- **GEMINI:** introducing temporary measures where a pre-defined code is entered in the price input for transferred capacity in Gemini. This code would then signal to national grid that the capacity transfer is associated with an optional charging arrangement.

Although we are happy to share our initial ideas and observations from neighbouring TSOs, we do not find ourselves able to propose a solution due to the highly technical nature of this issue. We propose that a review led by National Grid is launched to develop a complete solution to allow existing optional charging arrangements to continue in their current form from an operational perspective.

We have also entered the time of year where many counterparties have launched their gas and storage tenders for October 2020 without clarity on the full charging framework for the next gas year. These changes are business critical and it's important that steps are taken to avoid fragmented implementation of the new charging arrangements.

Yours sincerely,

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