

# SLR Industry Codes Workgroup

## An example of Regulatory Enforcement of Shipper SLC 3

Paper 04/02, 17 February 2006

### St Fergus and Bacton Investigation – December 1999

#### Grounds for Investigation

During 1998, Transco undertook significant work at the St Fergus entry terminal which led to capacity shortages. The situation was made worse because the planned work was not completed on time and so available capacity on the National Transmission System (NTS) remained constrained for longer than anticipated.

At the same time as the capacity shortfalls, shippers at the St Fergus entry terminal wanted to flow (nominate) more gas on to the NTS than there was available capacity. As a consequence of the capacity shortfall and the high level of nominations, Transco was forced to take significant action to balance the nominations against available capacity. It was estimated that the direct cost to Shippers for Transco's balancing actions was approximately £23.4M and that the indirect costs were much higher.

In September 1998 the Office of Gas Supply (Ofgas) undertook an investigation into the cause of the problem and the actions of Transco and the shippers. Nb the report on the investigation was subsequently written by Ofgem.

In particular, Ofgem sought to determine whether any shipper had breached their licence by, for example, manipulating gas flow nominations to gain financial advantage whilst knowing that their course of conduct would prejudice the efficient balancing of the NTS.

#### Ofgem's Interpretation of Shipper SLC 2

Ofgas investigated Shipper compliance with an older version of the Shipper Standard Licence, ie the pre-2001 determined version. Therefore please note that SLC 2 in the old version of the Licence is now SLC 3 in the current Licence regime.

When interpreting SLC 2, Ofgem concentrated on two obligations in particular – these are contained within paragraphs 2 and 3. Paragraph 2 states that:

“Without prejudice to the generality of paragraph 1, the licensee shall not knowingly or recklessly pursue any course of conduct (either alone or with some other person) which is likely to prejudice -

- (a) the safe and efficient operation, from day to day, by a relevant transporter of its pipeline system;
- (b) the safe, economic, and efficient balancing by that transporter of its system; or
- (c) the due functioning of the arrangements provided for in its Network Code.”

Ofgem considered that the reference to a ‘course of conduct’ **implied that a series of events**, not a single action, must have occurred for a licensee to have breached this obligation. Furthermore, that the shipper should have **prejudicial intent** at the time of the conduct, not just with hindsight.

Paragraph 3 states that:

“The licensee shall not knowingly or recklessly act in a manner likely to give a false impression to a relevant transporter as to the amount of gas to be delivered by the licensee on a particular day to that transporter’s pipeline system or as to the amount of gas to be comprised in its offtakes therefrom on that day.”

Ofgem considered that in contrast to paragraph 2, paragraph 3 **prohibits single actions**, together with courses of conduct. The purpose of paragraph 3 is to oblige shippers not to mislead the transporter as to the amounts of gas to be up- and off-loaded from its system.

For further details of Ofgem’s interpretation of SLC 2 please refer to chapter 2 of the Investigation Report<sup>1</sup>.

### **Determination of Breach**

Ofgem was able to determine that some shippers had breached their Licences by **using bespoke analytical tests** on data collected by Ofgas during its investigation.

In total Ofgem used 6 tests. The tests were devised to determine whether shippers were acting in an uncharacteristic manner during the period of limited capacity compared with other historic periods of activity. Some tests did this by comparing the levels of gas the shipper **wanted** to flow onto the NTS with the levels of gas the shipper **could** flow onto or off the NTS. For example, Ofgem used actual capacity restrictions or the levels of gas available to shippers through contracts with producers as counterpoints to the levels of gas being nominated by shippers.

For further details of the tests and their results please refer to chapters 6 and 7 of the Investigation Report.

Ofgas was able to collect data on Shipper nomination activity because Shipper SLC 9 (now SLC 10) obliged licensees to provide information “to the Director General as he may reasonably require or as may be reasonably necessary for the purpose of performing functions assigned to him by or under the Gas Act.”

### **Conclusions and Action taken**

Based on its findings, Ofgem concluded that 7 shippers were in breach of Licence condition 2. However, although Ofgem had concerns about the remaining 6 shippers’ nomination activity, it was unable to conclude that they had breached their licences.

Ofgem did not take any action against those shippers it found to be in breach of their licences because:

- i) the investigation only sought to determine whether shippers were in breach of their licences, not individuals’ exposure to Transco’s balancing actions. As such Ofgem did not believe any compensation arrangements between shippers could be based on the findings of the investigation, and
- ii) Ofgem could not, at the time, impose financial penalties on licensees found in breach of their licences. Ofgem was given the power to impose financial penalties after the investigation as part of the Utilities Act 2000.

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<sup>1</sup> [http://www.ofgem.gov.uk/temp/ofgem/cache/cmsattach/1177\\_fergdec.pdf](http://www.ofgem.gov.uk/temp/ofgem/cache/cmsattach/1177_fergdec.pdf)