

Modification proposal:	Uniform Network Code (UNC) 120V: Introduction of an SO Commodity Charge for NTS Storage Exit Flows		
Decision:	The Authority¹ has decided to reject this proposal		
Target audience:	The Joint Office, Parties to the UNC and other interested parties		
Date of publication:	31 January 2007	Implementation Date:	N/A

Background to the modification proposal

On 22 December 2006 the Final Modification Report (FMR) for Uniform Network Code (UNC) Modification 120V was submitted to Ofgem for a decision. On 20 December 2006 NGG NTS submitted pricing proposal NTS GCM03 "Introduction of an SO Commodity Charge for NTS Storage Facilities" which proposes the implementation of a reduced SO commodity charge rate on storage entry and exit flows compared to other entry and exit flows. These two proposals deal with associated issues, but each proposal has been considered against the relevant objectives as set out in the Licence.

In order to provide some background, the UNC currently provides for the application of an SO commodity charge in respect of storage entry flows (withdrawals from storage) and Storage Use Gas i.e. gas that is deemed to exit the NTS at a storage point for purposes such as "boil off". However, no such provision exists in respect of storage exit flows (injection into storage). NGG NTS therefore raised this UNC modification (120V) in order to levy a charge on storage exit flows.

On 18 January 2002, Ofgem decided not to veto Pricing Consultation (PC) 70, 'NTS System Operation Transportation Charges'. PC 70 replaced the National Transmission System (NTS) standard commodity charge with a SO commodity charge, which had applied since 1 April 2002. PC 70 provided that the SO commodity charge should be applied to NTS flows into gas storage sites. However, the basis on which the SO commodity charge is to apply to gas storage sites was the subject of a number of Network Code modification proposals (532,544,547)² which were rejected by Ofgem.

Ofgem's main concern in relation to the proposed code modifications was that the proposed charge was not cost reflective and effectively resulted in storage users being subject to double charging. A large share of the SO commodity charge consists of overheads and it would not be cost reflective to charge storage users a full SO commodity charge both on the gas flowing into storage and the gas flowing out of storage. Ofgem therefore indicated that a discounted SO commodity charge based on physical flows might be more appropriate.

The modification proposal 120V

It is intended that the proposed change to the UNC for storage exit flows, together with the existing provisions in UNC with regard to storage entry flows and storage use gas, would provide for an applicable SO commodity rate to apply to all storage flows, including

¹ The terms 'the Authority', 'Ofgem' and 'we' are used interchangeably in this document. Ofgem is the Office of the Gas and Electricity Markets Authority.

² http://www.ofgem.gov.uk/temp/ofgem/cache/cmsattach/3233_532-545-547.pdf?wtfrom=/ofgem/work/index.jsp§ion=/areasofwork/gasgovernance

storage use gas. Implementation of the proposal would enable NGG NTS to levy charges that have been proposed within NTS GCM03 in respect of storage exit flows. It is intended that National Grid NTS's Statement of the Gas Transmission Transportation Charging Methodology would describe the applicable charge rate that would apply to the respective storage quantities.

The proposer argues that implementation of this proposal would better facilitate the 'efficient discharge of the licensee's obligations under this licence'³ and its 'Obligations as Regard Charging Methodology'⁴.

UNC Panel⁵ recommendation

At the Modification Panel meeting held on 21 December 2006, of the 8 Voting Members present, capable of casting 10 votes, 4 votes were cast in favour of implementing this Modification proposal. Therefore, the Panel did not recommend implementation of this proposal.

The Authority's decision

The Authority has considered the issues raised by the modification proposal and the Final Modification Report (FMR) dated 22 December 2006. The Authority has considered and taken into account the responses to the Joint Office's consultation on the modification proposal which are attached to the FMR.

The Authority has concluded that implementation of the modification proposal will not facilitate the achievement of the relevant objectives as set out in the Licence⁶.

Reasons for the Authority's decision

Ofgem's main concern with Network Code modification proposals (532,544,547), which were rejected by Ofgem, was their lack of cost reflectivity. As Ofgem pointed out in its decision letter dated 19 February 2003, given that a large share of the SO commodity charge consists of overheads, it would not be cost reflective to charge storage users the full SO commodity charge both on the gas flowing into storage and the gas flowing out of storage. Ofgem therefore indicated that a discounted SO commodity charge based on physical flows might be more appropriate.

UNC modification proposal 120V proposes the introduction of a reduced SO commodity charge for storage based on allocated quantities (i.e. commercial flows). Ofgem has carefully considered this proposal and the responses to this proposal.

We note that the Joint Office received thirteen responses to its consultation on this modification proposal, of which one was supportive, two offered qualified support, one offered conditional support and nine were opposed.

³ Standard Special Condition A11.1(c)

⁴ Standard Special Condition A5

⁵ The UNC Panel is established and constituted from time to time pursuant to and in accordance with the UNC Modification Rules.

⁶ As set out in Standard Special Condition A11(1) of the Gas Transporters Licence, see: http://62.173.69.60/document_fetch.php?documentid=6547

Ofgem accepts the concerns raised by a large number of respondents to modification proposal 120V that a reduced SO commodity charge for storage users based on commercial flows may not be cost reflective. In particular, Ofgem understands that under this proposal it is possible that storage users would be charged in circumstances where, say 10 units are injected and 10 units withdrawn resulting in a physical flow of zero but commercial flows of 20 units. Given the nature of these costs this seems inappropriate. Ofgem is concerned that to impose a storage commodity charge in these circumstances may not be cost reflective. In particular, by linking the proposed charge to commercial flows (i.e. allocated quantities), these proposals would not result in cost reflective charges.

It has also been pointed out by a large number of respondents, that the proposal would particularly affect storage sites with large commercial flows/high cycling facilities. Given the lack of cost reflectivity previously discussed, it could be argued that the proposals are potentially discriminatory towards a certain category of storage users (i.e. those with large commercial flows/high cycling facilities) and might also potentially have a negative impact on competition between shippers.

In light of the above, the Authority does not believe that the proposal would better meet the objectives set out in Standard Special Condition A11 of the Gas Transporters' Licence, particularly the securing of effective competition between relevant shippers.

Further, the Authority does not believe that the proposal meets Standard Special Condition A11.1(c) "so far as is consistent with sub-paragraphs (a) and (b), the efficient discharge of the licensee's obligations under this licence" as argued by the proposer. The main reason being that Ofgem is not satisfied that the proposal will result in cost reflective charges.

Ofgem also notes respondents concern in relation to the lack of transparency and the lack of quantitative information which made it difficult for some respondents to assess these proposals.

Given the long time lag between previous mods in relation to this issue and this current UNC modification, Ofgem is disappointed with the proposed pricing consultation (NTS GCM03) and enabling UNC Modification 120V. Going forward, Ofgem expects to see a proposal for the introduction of a reduced SO commodity charge for storage users which is cost reflective and which is arrived at through a transparent and robust process. Ofgem continues to believe that, in principle, storage flows should not be excluded from the application of the SO commodity charge and that any particular benefits provided by storage sites to NGG NTS as system operator should not be factored into the calculation of the SO commodity charge. Going forward storage flows on the network are likely to increase and hence it is going to become increasingly important for this issue to be resolved to ensure that storage users bear some of the costs associated with system operation as do other users.

Robert Hull
Director, Transmission

Signed on behalf of the Authority and authorised for that purpose.