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Date: 20 February 2014

Dear Richard

### **Gas Transmission Charging Review**

Thank you for your letter<sup>1</sup> of 20 January 2014 to Ian Marlee about the Gas Transmission Charging Review (GTCR). We welcome your initiative of establishing a dedicated forum to discuss charging arrangements in Great Britain alongside our Review.

It might be helpful if I re-state the reasons why we feel a Review of charging is called for, and why we think now is a good time to do so.

#### **GB charging methodology needs to be fit for purpose**

Our principal duty is to protect the interests of present and future consumers. This includes ensuring that existing regulatory arrangements remain fit for purpose. In our Call for Evidence<sup>2</sup> we mentioned concerns expressed to us over aspects of the charging regime, notably the volatility and magnitude of the commodity charge. Responses confirmed that these concerns are widely shared. We note your comment that that the current regime is 'not beyond improvement'.

GB gas transmission charging has not changed significantly in recent years and we have evidence that it could work better: a 2010 industry proposal showed that commodity and entry capacity charges may not be as cost reflective as they should be (GCM 19<sup>3</sup>). The proposal also showed that it would be useful to review how capacity and commodity charges together collect allowed revenue. When we revisited the price responsiveness of gas interconnectors in 2012, these concerns remained. Our joint analysis<sup>4</sup> with Dutch and Belgian regulators indicated that the commodity charge might cause a distortion to cross-border flows. Therefore it is time to consider whether the current regime is still fit for purpose.

#### **EU Network Codes affect interconnection and domestic points**

You rightly point out significant interdependencies between Capacity Allocation Mechanisms, Tariff Framework Guidelines and domestic charging. The European Network of Transmission System Operators for Gas (ENTSOG) is drafting the Tariff Network Code

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<sup>1</sup> Gas Forum Transmission Charging Sub Group, Gas Forum, EnergyUK (not supported by Centrica), Major Energy Users Council (MEUC). Letter published on Gas Forum website, [www.gasforum.co.uk](http://www.gasforum.co.uk).

<sup>2</sup> Call for Evidence, 24 June 2013: <https://www.ofgem.gov.uk/ofgem-publications/75513/gas-trans-charging-review-call-evidence.pdf>.

<sup>3</sup> The proposal aimed to meet charging methodology objectives whilst maximising the proportion of TO entry revenue recovered via capacity charges. We rejected the proposal mainly because it presented insufficient evidence on how it would better meet charging methodology objectives. GCM 19 "Removal of NTS Daily Entry Capacity Reserve Price Discounts" <https://www.ofgem.gov.uk/ofgem-publications/53309/qcm019decisionsigned.pdf>.

<sup>4</sup> <https://www.ofgem.gov.uk/publications-and-updates/further-analysis-and-next-steps-review-gas-interconnectors-between-great-britain-and-belgian-and-dutch-markets>.

based on the Framework Guidelines. I attach ENTSOG's table which shows the scope of each chapter. Some chapters of the Framework Guidelines apply only to interconnection points (IPs), but some directly apply to all points including domestic points. So the Tariff Network Code, when finalised, will affect all GB market participants to some degree. Reviewing GB charges now therefore has potentially significant benefits, including:

- influencing development of the detail of the Tariff Network Code, including the approach to implementation. Evidence emerging from the GTCR can inform Ofgem, National Grid and DECC in European discussions. We will be better positioned to take a view on specific issues, and to explain that view to other regulators, TSOs, ACER, the European Commission and governments;
- identifying any changes to the GB regime, outside the scope of the Tariff Network Code, which will improve the working of the whole GB system once Code is implemented. If changes are needed to promote or preserve consumer interests, then it would be better for these to be made as close in time as possible to Tariff Network Code implementation. By contrast, if we do not review the wider GB regime until after Network Code implementation, we risk losing consumer benefits over the period before GB changes can be made. Reviewing the GB charging methodology now gives market participants the opportunity to consider it in the context of CAM implementation, and will help to avoid considering these issues from a European perspective today and reopening them from a national perspective later on. NTS users and user organisations welcomed this opportunity at the DECC-Ofgem stakeholder forum on 7 February 2014.<sup>5</sup>

We note your concerns about the time and effort the GTCR and the Third Package will require. We would welcome your input on the most constructive and efficient way to engage with market participants on current charging developments. We value our stakeholders' time and have been using two fora to engage with you on European Network Codes and the GTCR: the DECC-Ofgem stakeholder group and the Gas Transmission Charging Review stakeholder forum.<sup>6</sup> We would also like to offer to attend meetings of the Gas Forum's Transmission Charging Sub Group when you think that would be helpful. A member of the GTCR team could attend as an observer, on a flexible basis, to ensure that your ideas and concerns are included in our considerations.

### **Next steps**

As you know, National Grid Gas is leading GB industry involvement in ENTSOG NC drafting. As part of that work we understand they will prepare a note for stakeholders. It will outline potential changes in relation to IPs and domestic points to comply with the Network Code. NGG intends to share this note ahead of the Transmission Working Group on 6 March 2014.

Thank you also for raising discrimination and your work group's initial views on whether potential discrimination may be justified. The review and the implementation of the NCs will be looking at this issue. We look forward to other stakeholders contributing their views.

We would be happy to discuss the contents of this letter in person.

Yours sincerely,

**Andrew Burgess**  
**Associate Partner, Transmission and Distribution Policy**

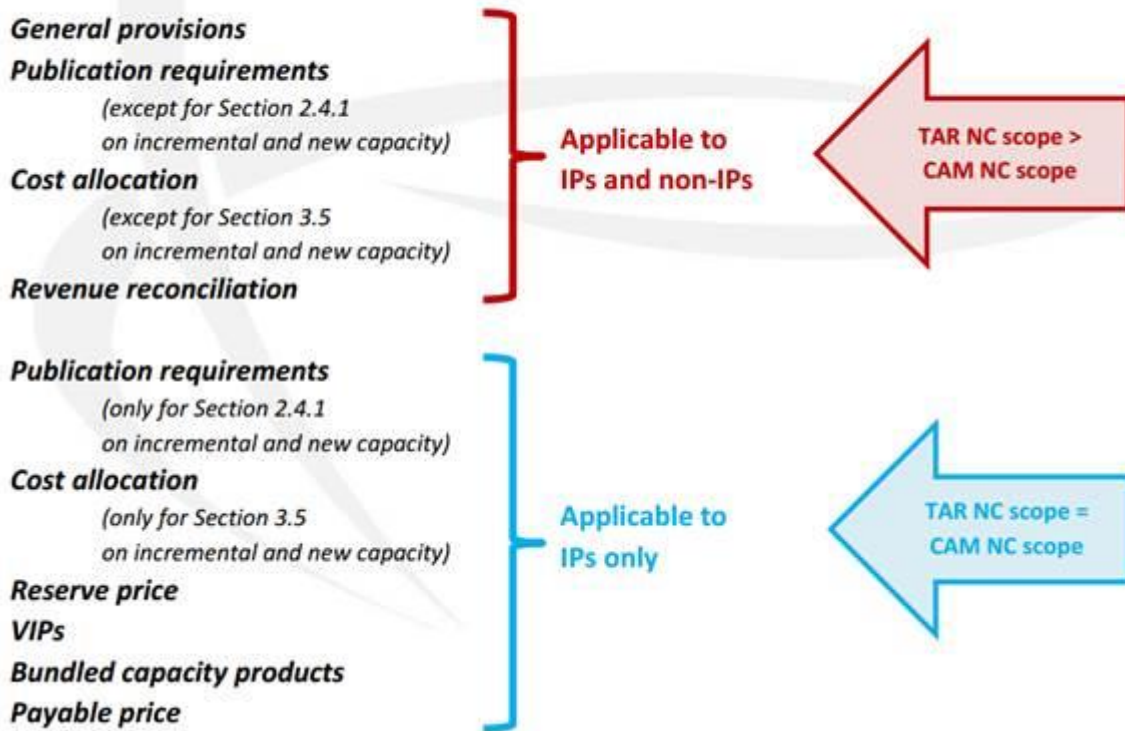
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<sup>5</sup> DECC/Ofgem Forum on our website: <https://www.ofgem.gov.uk/gas/wholesale-market/forums-seminars-and-working-groups/european-forums/decc-and-ofgem-stakeholder-group>.

<sup>6</sup> GTCR stakeholder forum on our website: <https://www.ofgem.gov.uk/publications-and-updates/gas-transmission-charging-review-december-stakeholder-event>.

Annex 1 – Application of the TARIFF FRAMEWORK GUIDELINES chapters to different points in the system, source: ENTSOG final project plan<sup>7</sup>

Figure 1. Application of the TAR FG chapters to different points on the system



**Box 1: interdependencies**

TARIFF FRAMEWORK GUIDELINES sets out how TSOs recover allowed revenue from capacity and commodity charges, and entry and exit charges. The FG determines tariffs for annual capacity products at all points on the network.

**Cost allocation methodology**

- The cost allocation methodology determines the share of the TSO’s allowed revenues that they can collect from the expected sale of transmission services at every entry or exit point.
- TARIFF NETWORK CODE aims to harmonise cost allocation at domestic and IPs
- TAR Framework Guidelines include several options, including the GB transportation model. TARIFF NETWORK CODE may change those, which could affect our transportation model

**Revenue reconciliation**

- TARIFF FRAMEWORK GUIDELINESs cover IPs and domestic points and allows domestic entry/exit points to recover allowed revenue by means other than through capacity charges (for example a commodity charge).
- We want to understand options for implementation and their meaning for current and future GB consumers

<sup>7</sup> The final Tariff NC project plan also gives more context on these areas of interdependency. It is available on ENTSOG’s website. [http://www.entsog.eu/public/uploads/files/publications/Tariffs/2013/TAR0202-14\\_140130%20Final%20Project%20Plan%20for%20Tariff%20NC.pdf](http://www.entsog.eu/public/uploads/files/publications/Tariffs/2013/TAR0202-14_140130%20Final%20Project%20Plan%20for%20Tariff%20NC.pdf).