

National Grid Gas plc;
all holders of a gas transporter licence;
the UNC modifications panel;
the Joint Office of Gas Transporters;
interested parties.

8 March 2018

Dear Stakeholder

Decision to direct National Grid Gas plc (NGG) to undertake specific tasks to implement aspects of Regulation (EU) 2017/460¹, the European Network Code on harmonised transmission tariff structures for gas (TAR NC)

Summary

We² consulted on directing NGG to undertake specific tasks relating to the implementation of Regulation (EU) 2017/460 ("TAR NC") in GB.³ Following this consultation our thinking has evolved in light of new evidence and stakeholder feedback. We are now publishing a decision on our direction which has changes from what we previously consulted on that reflect how our thinking has evolved. Our direction, which is shown in Annex 1, will be sent to National Grid Gas plc (NGG) today. We recognise, however, that our decision to change the gas transporter licence ("the Licence"), to allow us to direct NGG, takes effect not less than 56 days from the publication of that decision.⁴ Our direction requires NGG to use reasonable endeavours to undertake certain tasks which arise under TAR NC, and to complete them according to our directed timetable.

There are two key revisions from what we previously consulted on. The first revision provides the UNC0621 workgroup⁵ with additional time in which to develop its modification report. The second moves responsibility for undertaking the "final article 26 consultation", required under TAR NC, from NGG to Ofgem. NGG will instead be required to undertake a preliminary article 26 consultation, which shall take place at the same time as the consultation required under Uniform Network Code (UNC) modification procedures. We will undertake the "final article 26 consultation" using our draft impact assessment on the proposals and analysis included in the Final Modification Report for UNC0621.

¹ Commission Regulation (EU) 2017/460 of 16 March 2017 establishing a network code on harmonised transmission tariff structures for gas: <http://eur-lex.europa.eu/legal-content/EN/TXT/PDF/?uri=CELEX:32017R0460&from=EN>. This is also referred to as the "EU Tariff Code".

² The terms 'the Authority', 'Ofgem' and 'we' are used interchangeably. Ofgem is the Office of the Gas and Electricity Markets Authority. We are the National Regulatory Authority (NRA) in GB.

³ We set out our proposals on our draft direction in our 4 October 2017 consultation <https://www.ofgem.gov.uk/publications-and-updates/consultation-proposals-implement-aspects-regulation-eu-2017460-european-network-code-harmonised-transmission-tariff-structures-gas-tar-nc>.

⁴ See s23(9) of the Gas Act (1986).

⁵ In GB, TAR NC will largely be implemented through changes to the Uniform Network Code (UNC), the contractual framework for GB's gas transmission network. Industry proposals for these changes are being developed at the UNC0621 Workgroup. The workgroup report contains an initial modification proposal, raised by NGG, and alternative proposals, raised by other parties.

Background

TAR NC was published in the Official Journal of the European Union on 16 March 2017. Its objectives are to contribute to market integration, to enhance security of supply and to promote interconnection between gas networks. Central to the requirements of TAR NC is the implementation of a transparent reference price methodology (RPM) to set a capacity price. TAR NC requires member states to implement the RPM no later than 31 May 2019 following a stakeholder consultation and National Regulatory Authority (NRA)² approval of implementation proposals. TAR NC article 26 provides details on the content and administration of the final consultation which should precede the NRA decision on proposals which seek to implement the RPM in member states.

For National Grid Gas plc (NGG), GB's gas transmission system operator (TSO), we anticipate that the requirements of TAR NC will be largely implemented through changes to the Uniform Network Code (UNC), the contractual framework for use of the GB gas network. NGG has already raised UNC modification proposal 0621 (UNC0621).⁶ Its purpose is "to amend the gas transmission charging regime in order to better meet the relevant charging objectives and customer/stakeholder provided objectives for gas transmission transportation charges and to deliver compliance with relevant EU codes (notably the EU Tariff Code)". Current timeframes indicate that UNC0621 is scheduled for industry consultation in the second quarter of 2018, ahead of being submitted to us for a decision in summer 2018.

Ofgem consultations and decisions to date

On 4 October 2017, we launched a consultation on proposals relating to the implementation of TAR NC in GB.⁷ We proposed to:

- modify the gas transporter licence ("the Licence") (to enable us to issue a direction requiring a licensee to undertake certain activities);
- issue a direction to NGG, detailing the tasks we wanted it to undertake (following the modification to the Licence). In the direction we proposed to:
 - make NGG responsible for undertaking certain tasks arising under TAR NC and to direct a timetable for their completion;
 - align and extend the scope of the consultations required under TAR NC and industry procedures (UNC).

Our proposals, set out in a draft direction, required the final consultation under TAR NC article 26 to be undertaken by NGG, to be extended to include matters listed in TAR NC article 28, and to be undertaken using the UNC0621 draft modification report (DMR). They also required that NGG should use reasonable endeavours to ensure that the DMR is presented to the March 2018 (or earlier) meeting of the UNC modification panel and that the industry consultation is launched at the same time as the extended final TAR NC article 26 consultation. In addition, our proposals required that both consultations should commence no later than 2 April 2018 and remain open for two to three months. Our proposed timetable was designed to enable various milestones to be met ahead of a RPM implementation deadline of 31 May 2019.

On 1 December 2017, and following consideration of seven consultation responses, we published decisions on three of four of our proposals.⁸ We decided to:

⁶ Further details are available at <https://www.gasgovernance.co.uk/0621/>. UNC0621 was raised subsequent to our request that industry develop UNC modification proposals to implement changes to the gas transmission charging regime and TAR NC – see <https://www.ofgem.gov.uk/publications-and-updates/gas-transmission-charging-review-confirmation-policy-view-and-next-steps> and <https://www.ofgem.gov.uk/publications-and-updates/open-letter-european-union-network-code-harmonised-transmission-tariff-structures-gas-tar-nc> for further information

⁷ <https://www.ofgem.gov.uk/publications-and-updates/consultation-proposals-implement-aspects-regulation-eu-2017460-european-network-code-harmonised-transmission-tariff-structures-gas-tar-nc>.

⁸ <https://www.ofgem.gov.uk/publications-and-updates/statutory-consultation-proposal-modify-gas-transporter-licence-following-decisions-proposals-relating-implementation-regulation-eu-2017460-tar-nc-qb>.

- launch a statutory consultation on our proposal to modify the Licence. We therefore launched our statutory consultation to change the Licence on 1 December 2017;
- make NGG responsible for undertaking certain tasks arising under TAR NC and to direct a timetable for their completion;
- align and extend the scope of the consultations required under TAR NC and industry procedures.

We said we would make our decision on the specifics of the NGG direction after our statutory consultation on the proposed Licence modifications had closed. We also summarised responses relating to our draft direction.⁹ We noted that two respondents disagreed in principle with our proposed direction to NGG and that NGG sought a completion date for tasks rather than a start date. We said in our December 2017 publication that the best way to meet the TAR NC implementation deadline is to issue a direction which timetables the start of the consultations required under the TAR NC and UNC processes. We thought that this was necessary to ensure sufficient time is available for subsequent activities to take place ahead of the TAR NC implementation deadline.

Our final decision to modify the Licence is published today.¹⁰ This letter sets out our final decision on the direction to NGG.

Recent developments and observations

Since making our decisions on three out of four proposals (that we had consulted on in October 2017) in our 1 December 2017 publication, and launching our statutory consultation, the following issues have emerged.

- Development of the UNC0621 workgroup report has been slower than anticipated. We are encouraged that eight alternative modification proposals have now been raised in addition to NGG's original modification proposal. However, we are concerned that none is supported by an assessment of its likely impact, either against the existing long run marginal cost (LRMC) based RPM, or against alternative methodologies. We also note that all of the proposals which have been raised to date are variations on NGG's capacity weighted distance (CWD) based proposal, and maintain a 50/50 entry-exit revenue recovery split. None advocate an alternative RPM or entry-exit split.

In the absence of any supporting assessments, we have been unable to form an initial view on whether any of the proposals will provide an outcome that is in the interests of consumers. Given the potentially significant distributional impact of the proposed changes, we believe it is prudent to provide the workgroup with more time in which to develop its proposals and, if deemed appropriate, to bring forward a more diverse set of proposals. We note that it is open to UNC signatories and materially affected parties to raise any modification proposals which better facilitate the relevant objectives of the UNC (which includes compliance with TAR NC) and expect industry to bring forward proposals in a timely manner.

In our October 2017 publication, we proposed that the DMR be presented to the March 2018 meeting of the UNC modification panel. In light of the issues raised above, our view is that the UNC0621 workgroup report requires additional workgroup development time. This view is shared by the majority of workgroup attendees. Additional workgroup time will enable existing modification proposals to be more fully developed ahead of submission to the UNC modification panel as the DMR. It will also enable supporting analysis to be developed for each of the proposals, and new alternatives to be raised. These new proposals should address

⁹ See the section headed "Our proposal to issue NGG with a direction requiring it to undertake certain tasks according to our timetable" in Annex 1 of our 1 December 2017 publication.⁸

¹⁰ <https://www.ofgem.gov.uk/publications-and-updates/modification-gas-transporter-licence-facilitate-implementation-regulation-eu-2017460-tar-nc-gb>.

any perceived shortcomings of the existing proposals, and take into account our views expressed above.

- We have reviewed the timelines for other tasks which need to take place ahead of the TAR NC RPM implementation deadline of 31 May 2019. NGG has informed us that allocations from the Quarterly System Entry Capacity (QSEC) auction which takes place in March 2019 can be concluded ahead of this deadline. This means the auction can take place using reference prices generated by the existing RPM. Consequently, we are able to delay our decision until nearer the RPM implementation deadline, freeing up time in the near-term which can be used for UNC0621 workgroup development. NGG have advised, however, that they require an Authority decision ahead of March 2019 in order to generate and publish reference prices for the next NTS exit capacity allocation window and capacity allocation mechanism (CAM) auctions which take place in July 2019.
- When we published our decisions on 1 December 2017, we omitted one consultation response from RWE Supply and Trading GmbH/RWE Generation UK plc ("RWE"). We acknowledge receipt of this response elsewhere.¹¹ In its response, RWE seeks that established practice is followed whereby following a UNC panel recommendation on a modification proposal, Ofgem undertakes an impact assessment based on the relevant objectives and our principal objective. RWE considers this is more consistent with TAR NC and UNC consultations. Furthermore, RWE suggest that the final TAR NC article 26 consultation should not be the UNC consultation. RWE consider the final TAR NC article 26 consultation should be the Ofgem impact assessment and that this should be considered by ACER and the NRAs of directly connected member states. RWE also seek clarification on areas of TAR NC requesting NRA justification (citing the use of multipliers and approach to revenue reconciliation).

We have given these views on the final TAR NC article 26 consultation some consideration and have discussed them with ACER. Our view is that, whilst the DMR could be used as the final TAR NC article 26 consultation document (as we proposed), our draft impact assessment, inclusive of the UNC0621 final modification report (FMR) and responses to the earlier consultations undertaken by NGG, would more closely align with TAR NC expectations since it will include our assessment of the proposals as appropriate.

Revised proposals and Authority direction

In light of the observations made above, our thinking has evolved and we have decided to revise the timelines and responsibilities for undertaking tasks arising under TAR NC. These revisions are reflected in our direction to NGG given in Annex 1 to this letter.

Our revised direction will have the following effect.

- We are now directing that NGG shall use reasonable endeavours to ensure that the UNC0621 DMR is submitted to the UNC modification panel in sufficient time for consideration at its 17 May 2018 (or earlier) meeting. This will provide the UNC0621 Workgroup with up to an additional two months in which to develop its modification report ahead of submission to the UNC modification panel.
- NGG will no longer be required to undertake the final TAR NC article 26 consultation. Instead, NGG will be required to undertake a preliminary consultation, pursuant to TAR NC article 26. This consultation shall take place at the same time as the industry consultation required under UNC modification procedures, as originally proposed. The maximum duration for both consultation has been shortened from three months to two. NGG shall use reasonable endeavours to ensure that these consultations shall commence no later than 18 May 2018.

¹¹ <https://www.ofgem.gov.uk/publications-and-updates/rwe-s-response-our-consultation-proposals-implement-aspects-regulation-eu-2017460-european-network-code-harmonised-transmission-tariff-structures-gas-tar-nc>

- We are continuing to direct NGG to forward the consultation documents on to ACER. As noted in our 1 December 2017 publication, we consider it appropriate to seek ACER's views on industry proposals ahead of us undertaking and consulting on an impact assessment of those same proposals.

Our revised timetable will provide additional time to NGG and the proposers of alternative modification proposals in which to fully develop their proposals. We expect proposals to be fully supported by their own detailed and robust analysis against alternative solutions. This should result in us receiving a carefully considered and diverse set of modification proposals. Whilst we have directed a back-stop date of DMR submission to the 17 May 2018 UNC modification panel meeting, we encourage earlier submission if possible.

We will take responsibility for undertaking the final TAR NC article 26 consultation. We will undertake this consultation using our draft impact assessment of the UNC0621 FMR which will be inclusive of stakeholder responses to the industry consultation outlined above. Our draft impact assessment will build on the assessments undertaken by proposers of modifications to the UNC and contained within the UNC0621 FMR. It will also include our assessment of those matters which TAR NC requires us to assess. We will forward the consultation documents to ACER as required under TAR NC article 27 and to NRAs of directly connected member states under TAR NC article 28. We will publish the consultation responses received and their summary as required under TAR NC article 26.

We recognise that the direction issued to NGG under paragraph 7B of Standard Special Condition A5 of the Licence will not have effect until after the proposed licence modification comes into effect - not less than 56 days from the publication of the direction to modify the Licence. However, we have decided to publish our direction to NGG alongside our direction to modify the Licence for transparency and efficiency. This will allow the UNC Panel to be better prepared for its meeting on 17 May 2018.

Next steps

If you have any queries regarding this letter, please contact Sean Hayward at sean.hayward@ofgem.gov.uk or on 0207 901 3924.

Yours faithfully

Cathryn Scott
Partner, Energy Systems, Ofgem

Signed on behalf of the Authority and authorised for that purpose

Annex 1: Direction to NGG pursuant to the gas transporter licence

To: National Grid Gas plc

Direction issued pursuant to paragraph 7B of Standard Special Condition A5 (Obligations as regard Charging Methodology) ("SSC A5") and paragraphs 9(i) and 9(j) of Standard Special Condition A11 (Network Code and Uniform Network Code) ("SSC A11") of the Gas Transporter License (the "Licence") granted under section 7 of the Gas Act 1986 (the "Act")

Whereas -

1. National Grid Gas plc (the "Licensee") holds a licence granted, or treated as granted, under section 7 of the Act and is subject to the conditions contained in the Licence.
2. Paragraph 7B of SSC A5 of the Licence provides for the Gas and Electricity Markets Authority ('the Authority') to give directions in respect of the Regulation and/or any relevant legally binding decisions of the European Commission and/or the Agency.
3. Paragraphs 9(i) and 9(j) of SSC A11 of the Licence provide for the Gas and Electricity Markets Authority ('the Authority') to give directions in respect of proposals that fall within the scope of paragraph 15CE(a) of SSC A11 of the licence.
4. Regulation (EU) 2017/460, which was published in the Official Journal of the European Union on 16 March 2017, places legally binding obligations on member states of the European Union.
5. The Licensee has made a UNC modification proposal (UNC0621) that falls within the scope of paragraph 15CE(a) of SSC A11 of the licence.
6. The Authority has consulted on a proposed direction to the Licensee in respect of the matters addressed in paragraphs 4 and 5 above.

Now therefore -

In accordance with the powers contained in paragraph 7B of SSC A5 of the Licence and paragraphs 9(i) and 9(j) of SSC A11 of the Licence, the Authority hereby directs that the Licensee undertakes the tasks set out in Appendix 1 to this direction.

This document constitutes notice of the reasons for the direction as required by section 38A of the Act.

Appendix 1 to the Authority's Direction

Tasks to be undertaken by the Licensee. All references made to TAR NC are to Regulation (EU) 2017/460

Task	Direction
1.	We direct that the Licensee shall use reasonable endeavours to ensure that the UNC0621 draft modification report is submitted to the UNC modification panel in sufficient time for consideration at its 17 May 2018 (or earlier) meeting.
2.	We direct that the Licensee shall use reasonable endeavours to ensure that the UNC0621 industry consultation is launched at the same time as the consultation referred to in Task 3. We direct that this shall commence no later than 18 May 2018 and remain open for at least one month but no more than two months.
3.	We direct that the Licensee shall undertake a consultation pursuant to TAR NC article 26 and shall use the UNC0621 draft modification report as the consultation document. We direct that this shall commence no later than 18 May 2018 and remain open for at least one month but no longer than two months.
4.	We direct that the Licensee shall perform the cost allocation assessments referred to in TAR NC article 5(1) and publish them as part of the consultation referred to in Task 3.
5.	We direct that the Licensee shall publish the matters referred to in Article 28(1) as part of the consultation referred to in Task 3.
6.	We direct that the Licensee shall publish the responses and their summary from the consultation referred to in Task 3 no later than 1 month following the end of the consultation, and forward a copy to the Authority.
7.	We direct that the Licensee shall forward the consultation document referred to in Task 3 onto ACER upon launching the consultation and request their view.
8.	We direct that the Licensee shall publish the information referred to in TAR NC article 29, relating to capacity auction reserve prices, before the annual yearly capacity auction.
9.	We direct that the Licensee shall publish the information referred to in TAR NC article 30(1), (2) and (3), relating to the technical, financial and other characteristics of the transmission system, before the tariff period as defined in TAR.