

Impact Assessment Form

Appendix D

<p>Title: Impact Assessment and minded to decision on UNC modifications 642, 642A and 643: Unidentified Gas</p> <p>Division: Consumers and Markets</p> <p>Associated documents: UNC642, 642a and 643 Final Modification Report</p> <p>Coverage: Partial</p>	Impact Assessment (IA)
	Type of measure: Codes
	Type of IA: Not Qualified under Section 5A UA 2000
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Summary: Intervention and Options

Rationale for intervention, objectives and options

What is the problem under consideration? Why is Ofgem intervention necessary?

The current gas allocation arrangements are resulting in volumes of unidentified gas (UIG) being allocated to gas shippers each Gas Day that are greater and more volatile than many anticipated. Although these daily UIG volumes are adjusted in the subsequent 5 days as daily meters reads and other data are confirmed, before allocation is closed out, some gas shippers are finding it difficult to predict their exposure to UIG and therefore determine how much gas they should purchase in order to balance their daily positions.

Subsequent reconciliation will also take place as non-daily meter reads are entered into settlements. Therefore, whilst any error in gas allocation will be reconciled over time, there is not currently enough certainty as to when this will happen. In the meantime payment for energy, including the shipper's allocation of UIG, will become due.

Several UNC modifications proposals have been raised, looking to revise these gas allocation arrangements. As these are material proposals, the Authority must determine whether to accept or reject them, pursuant to the Gas Transporters licence.

What are the policy objectives and intended effects including the effect on Ofgem’s Strategic Outcomes

Our aim is to determine whether any of the proposals would better facilitate the relevant objectives of the UNC than the current baselined arrangements, in a way that would also be consistent with our wider statutory duties. In particular, we wish to ensure that the gas allocation arrangements facilitate effective competition between gas shippers, and in doing so ensure that there is downward pressure on the charges that they pass through to gas suppliers and ultimately consumers.

Whilst we have the option of sending the proposals back to the UNC Panel for further work, we do not consider that would be a practicable way forward on this occasion.

What are the policy options that have been considered, including any alternatives to regulation? Please justify the preferred option

As described within the main text of the impact assessment, a total of four options have been considered, which includes the three modification proposals that have been submitted to us and the final option of rejecting all three proposals in favour of retaining the current arrangements.

We consider that each of the alternatives would be a retrograde step, unwinding some of the benefits that have relatively recently been implemented as part of the Project Nexus reforms, following several years of industry development. In particular, we are of the view that none of the proposals would address the root causes of UIG, but merely apply a different weighting to its distribution amongst shippers. We consider that the proposed allocation methodologies would be less cost-reflective than the current evidence-based approach. We further consider that whilst the proposed allocation methodologies would result in more certainty for those shippers which service the relatively small number of Daily Metered supply points, this would come at the expense of greater uncertainty for the remaining majority.

Preferred option - Monetised Impacts (£m)

Business Impact Target Qualifying Provision	N/A
Business Impact Target (EANDCB)	N/A
Net Benefit to Ofgem Consumer	N/A
Wider Benefits/Costs for Society	

Explain how was the Net Benefit monetised, NPV or other

As set out in the main document, we consider that none of the modification proposals would result in a change to prevailing levels of UIG, simply reallocate it from one group of shippers to another. We therefore consider that there would, at least in the short term, be no net benefit to consumers (we recognise that there is a difference in the typical margins shippers in the DM sector apply to their energy costs as compared to the NDM sector, though we do not consider that any net impact on margin charged through to consumers as a whole could properly be attributed to these modification proposals alone).

Preferred option - Hard to Monetised Impacts

Describe any hard to monetised impacts, including mid-tem strategic and long-term sustainability factors following Ofgem IA guidance (maximum 10 lines).

We consider that the implementation of any of the proposals could have a marginally detrimental impact on sustainable development, resulting from the dilution of incentives to tackle the root causes of UIG. As the cause of that gas being lost to the system is, by definition unidentified, it is not possible to say with any certainty whether it has been consumed but not registered (e.g. though theft of poor data management) or lost in conveyance, through undetected and/or unreported leakage. The environmental impact of this lost gas would vary greatly depending on whether it has been consumed (i.e. burnt) or released into the atmosphere as natural gas. Our preference is to retain the focus of all sectors of the gas market on identifying and addressing the root causes of this gas loss and its cost to consumers. We consider that the best way to do this is to ensure the transparency and accuracy of gas settlement, allowing shippers to identify an avoidable cost.

Key Assumptions/sensitivities/risks

- The current baseline arrangements are capable of delivering lower and more predictable volumes of UIG through the provision of better quality data and analysis, in particular more regular valid meter readings submitted to the CDSP;
- The ongoing roll out of smart meters will provide more readily accessible daily data;
- That AQ remains broadly constant, both in aggregate and across each of settlement products 1 to 4 as used in our analysis;
- That the take up of products 1 and 2 will remain restricted either by the mandatory threshold in the case of product 1, or by the potential exposure of product 2 supply points to ratchet liabilities;
- That AUGÉ weighting factors will continue to reflect broadly the same proportions across settlement products and end user categories as used in our analysis.
- We acknowledge that unless and until UIG becomes more predictable for all shippers, they may seek to pass through their exposure as a risk premium;
- We are concerned that any move away from the current evidence-based and independently determined UIG weighting will set a bad precedent, which encourages the submission of further proposals which focus on the narrow interests of the proposer and/or their market sector rather than seeking to make improvements that are beneficial in the round. We note that the pre-Project Nexus settlement arrangements were exposed to gaming opportunities and other adverse effects on competition, as identified in the Competition and Markets Authority's energy market investigation final report.

Will the policy be reviewed?

Conditional on industry self-governance

If applicable, set review date: month/Year