

UNC Panel Chair, the Joint Office,
relevant Gas Transporters, Gas
Shippers, and other interested
parties

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Date: 8 December 2020

UNC748: Prospective Removal of Entry Capacity Revenue from Capacity Neutrality Arrangements

On 8 December 2020 the Joint Office of Gas Transporters ("Joint Office") received a request from National Grid Gas Transmission ("NGGT", the proposer) that Uniform Network Code ("UNC") modification UNC748 'Prospective Removal of Entry Capacity Revenue from Capacity Neutrality'¹ should be treated as 'urgent' and proceed under a timetable approved by Ofgem². After considering the justification provided for this request, we have decided to grant urgent status for UNC748. We set out our reasons below.

Background

On 5 November 2020, NGGT advised the UNC Transmission Workgroup³ of a significant under-recovery of its allowed revenue based on October 2020 data. NGGT attributed this mainly to lower than forecast capacity bookings and the operation of the capacity neutrality⁴ arrangements.

NGGT indicated that it proposed to address the under-recovery, in part, by raising a UNC modification with respect to capacity neutrality to remove certain entry capacity cash flows from the capacity neutrality arrangements.

UNC748 seeks to remove the charges paid by Users for interruptible and within day firm entry capacity from capacity neutrality on a prospective basis. NGGT has said that the current application of capacity neutrality redistributes these cash flows back to Users with the effect that these charges do not contribute to NGGT's allowed revenue stream. The current treatment of these charges under capacity neutrality has contributed to the size of the revenue recovery charges published by NGGT on 30 November 2020, effective from 1 February 2021. UNC748 includes a proposal that, if implemented, allows NGGT to issue a pricing notification at short notice to reduce these revenue recovery charges.

¹ <https://www.gasgovernance.co.uk/0748>

² Ofgem is the Office of the Gas and Electricity Markets Authority. The terms 'Ofgem', 'the Authority', 'we', 'our' and 'us' are used interchangeably in this letter.

³ <https://www.gasgovernance.co.uk/tx/051120>

⁴ UNC748 explains the operation of these arrangements as follows: "The Capacity Neutrality arrangements redistribute specific costs and revenues across Entry Users".

Our decision on urgency

We have considered the Proposer’s justification for urgency. We have assessed the request against the urgency criteria set out in Ofgem’s published guidance⁵. The guidance sets out the factors the Authority will consider in reaching a decision on urgency in the context of industry code modification proposals – it is intended to be illustrative and not exhaustive. Each request for urgency will be considered on its merits on a case by case basis by reference to our guidance, and in circumstances where we depart from it, we will explain the reasons why. Ordinarily we take the view that an urgent modification should be linked to an imminent issue⁶ or a current issue that if not urgently addressed may cause:

- i. A significant commercial impact on parties, consumers or other stakeholder(s); or
- ii. A significant impact on the safety and security of the electricity and/or gas systems, or;
- iii. A party to be in breach of any relevant legal requirements.

In their request for urgency, NGGT says that the current situation, which involves cash flows associated with interruptible and within day entry capacity feeding into capacity neutrality combined with the effects of the revenue recovery charges to be applied between February – June 2021, will “have a material effect on commercial activities relating to the shipping, transportation and supply of gas”. This is consistent with industry views expressed, including at the 7 December 2020 National Transmission System Charging Methodology Forum⁷. NGGT says that UNC748 will reduce the impacts seen in October 2020 of significant under-recovery of revenues, and would allow lower revenue recovery charges than would otherwise be the case to be set.

NGGT also point to the distributional effects between Users that the current operation of the Capacity Neutrality arrangements is having. The cost of short-term capacity is paid for by Users holding Relevant Entry Capacity, however this revenue is returned to all Users who hold Firm (Fully Adjusted) Entry Capacity via Capacity Neutrality. This gives rise to distributional impacts on Users as the method by which Capacity Neutrality payments are returned to Users differs to the way they are recovered via the revenue recovery charge.

We consider that the urgency request is justified based on the above criterion (i), namely it is linked to an imminent issue that if not urgently addressed may cause a significant commercial impact on certain users. Specifically, the current operation of the Capacity Neutrality arrangements has contributed significantly to NGGT’s under-recovery of revenues which in turn has led to NGGT raising a significant revenue recovery charge from 1 February 2021. This would have a significant commercial impact on parties, consumers or other stakeholders, in part via the distributional impacts set out above. We note that NGGT did not refer to criteria (iii) and while it has alluded to criteria (ii), we have not assessed that in the time available given that this modification meets urgency criteria (i).

While we have accepted the timeline as recommended by the proposer, we expect to see evidence in the FMR as to how Users and market participants are affected by this modification, and the Joint Office to ensure those parties impacted by the proposal are suitably consulted. The timeline is as follows:

Process	Date
Ofgem approval of Urgent status	8 December 2020
Modification Proposal issued for consultation	8 December 2020
Consultation Close-out for representations	11 December 2020
Final Modification Report available for Panel	15 December 2020
Modification Panel recommendation	17 December 2020
Final Modification Report issued to Ofgem	17 December 2020

⁵ Ofgem Guidance on Code Modification Urgency Criteria: <https://www.ofgem.gov.uk/publications-and-updates/ofgem-guidance-code-modification-urgency-criteria-0>

⁶ The imminent issue may be date related.

⁷ <https://www.gasgovernance.co.uk/ntscmf/071220>

For the avoidance of doubt, in reaching our decision on urgency we have made no assessment of the substance of the proposed modification, including the recommended implementation date, and nothing in this letter in any way fetters the discretion of the Authority.

Next steps

To facilitate consideration of this modification we want the Joint Office to include the questions in the Annex to this letter within the consultation response template, and expect parties to give this due consideration.

We have encouraged NGGT to consider, and where it considers it might be appropriate, to bring forward further remedies for the issues that it has identified with revenue recovery separately.

David O'Neill

Head of Gas Markets and Systems

Signed on behalf of the Authority and authorised for that purpose

Annex

Prospective Capacity Neutrality Modification Proposal (UNC748)

Consultation Questions

1.	Do you agree that the treatment of interruptible and within day firm entry capacities feeding into capacity neutrality is inappropriate? (Yes / No)
	Please explain your rationale.

2.	Do you agree that these revenues should be removed from capacity neutrality? (Yes / No)
	Please explain your rationale.

3.	Do you support that National Grid should be a granted a one-off relaxation of its obligation to provide two months notice of pricing changes? (Yes / No). (See the 'Solution' section of the modification.)
	Please explain your rationale.