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Dear Thomas

RE: NTS GCD11 - Optional Commodity Charge Change

Whilst intuitively, updating the costs of constructing a pipeline to reflect current levels for the purpose of the Optional Commodity Charge (OCC) calculation feels correct, it is important that the full impact of this change is understood. Since the input costs have not been updated for a significant amount of time, the effect of this proposal will be to introduce significant and unavoidable additional costs for Shipper and End Users. Our own analysis, based on NGG's revised calculation suggests that that the charging "benefits" associated with the OCC would be reduced by over 50% in some cases. For end users, such as gas-fired generators, who are already competing in difficult market conditions, this change could be sufficient to lead plant to mothball or close prematurely; thereby potentially impacting GB security of supply. For this reason, E.ON UK is unable to support these proposals at this stage, but does recognise that some minor adjustments may be required to ensure the OCC remains cost-reflective. Our strong preference is for NGG to limit the changes to a simple uplift by RPI.

We believe this discussion paper also highlights the need for more robust governance around NGG's charging methodology and associated inputs. We believe, therefore, that the whole OCC calculation and associated inputs should be codified under the UNC.

E.ON UK would like to offer the following comments in response to the questions posed in your discussion paper:

Question 1: Do respondents prefer Option One or Option Two as the most reasonable approach, and most consistent with facilitating the relevant objectives, to update the underlying costs of the formula in an effort to bring the NTS Optional Commodity charge formula more up to date?

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We are not able to express a preference at this stage, as we find both Options proposed unsatisfactory. In our view, the changes proposed here by NGG have the effect of altering the calculation in such a significant manner that it cannot be simply updated, as proposed. It is not clear why a simple RPI indexation has been rejected and no justification is provided for increasing charges above RPI. This seems particularly relevant since for most of the period from 1998, National Grid was subject to RPI–X regulation.

Furthermore, given that this is not a UNC proposal, it is not appropriate to justify the changes in this discussion paper in the context of the UNC's "relevant objectives". We consider this to in effect be a change in methodology so should be subject to full governance under the UNC, where a full and proper evaluation against all the relevant objectives can be undertaken.

Question 2: Do you agree with the proposal to delay reviewing the methodology / access and flexibility of the NTS Optional Commodity charge until EU TAR / GTCR is more certain?

Yes, although we consider that the changes proposed here are significant enough to warrant a delay by NGG in making a final decision, in order to fully understand the impact; particularly on the wholesale gas market. As noted above, we consider this would be best carried out under established UNC governance procedures.

In addition, the future interaction between the European Tariffs (TAR) Code and the OCC are, as yet, unknown; but likely to be significant given the focus in the TAR Code on cost recovery via capacity charges, rather than commodity charges. Therefore delay is also warranted to consider this impact more fully.

Question 3: Do respondents agree with our proposed approach on timescales for notifying a change to NTS Optional Commodity charges, following the same notice periods as for other NTS charges? If not what do you believe these should be?

Yes, the notification periods are consistent with other NTS charges. However, if NGG chooses to pursue Options One or Two, it should explore the option of "staggering" the impact of the charges over a number of years, rather than introducing a full update to the input costs, as proposed.

For example, for an individual Shipper the impact of these proposals may be similar (or even greater) than a large, unexpected NTS metering error. There have been proposals put forward in these instances to limit the impact of such sudden changes, by spreading the costs over the same period of time over which the metering error took place. NGG may wish to consider such an approach if it continues to pursue Option One or Two following this discussion paper, in order to avoid such a sudden “shock” to Shippers and End Users.

Question 4: Do respondents believe 1 April 2016 is an appropriate implementation date? If not what do you believe the implementation date should be and why?

No. It is our strongly held view that any change to the OCC calculation should be introduced at the start of a gas year to coincide with contractual changes within the gas market. As such, we would only wish to see any change taking effect from October rather than April.

Question 5: Are there any elements that you feel we should take into consideration, or that you believe we have missed and should take into account, in the two options being considered for reviewing the NTS Optional Commodity Charge?

We consider that RPI is the most cost-reflective inflation measure to use and future work on the OCC methodology should be focused on this.

In addition, as this is a NGG discussion paper, it (perhaps not unreasonably) does not consider in sufficient detail, the impact on market participants and focusing primarily on revenue recovery principles. For example, there is no consideration on the impact on market efficiency, or the potential consequences for electricity security of supply, if the economic viability of marginal CCGTs currently on the shorthaul tariff is affected, which may lead to mothballing or closure decisions being brought forward.

There also needs to be a clearer proposal on future updates to the OCC calculation, as publishing a discussion paper at random time intervals does not provide certainty for market participants. For example, NGG could commit to reviewing the calculation and its inputs every five years. However this obligation would be best discharged via a UNC Modification Proposal and through the associated governance process.

Yours sincerely

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