

Modification proposal:	<b>Uniform Network Code (UNC) 352: The introduction of an interruptible reverse flow service at Moffat interconnector (UNC352)</b>		
Decision:	The Authority <sup>1</sup> directs that this proposal be made <sup>2</sup>		
Target audience:	The Joint Office, Parties to the UNC and other interested parties		
Date of publication:	4 October 2011	Implementation Date:	4 October 2011

## Background to the modification proposal

Article 16(1) of the Third Package Gas Regulation<sup>3</sup> requires a Transmission System Operator (TSO) to make maximum capacity on its gas transmission system available to market participants<sup>4</sup>. We understand that the European Commission considers that the obligation to offer maximum capacity, combined with the obligation to provide firm and interruptible third party access services under Article 14(1)(b)<sup>5</sup> of the Third Package Gas Regulation implies that a TSO has to offer capacity in both directions at a connection with another TSO. In those cases where it is technically not possible to have physical flows in both directions it is still possible to offer capacity as a 'counter flow' on an interruptible and virtual basis.

Under present commercial arrangements, gas flows from Great Britain (GB) to Ireland, with shippers buying GB exit capacity at Moffat interconnector and Irish entry capacity. Currently there is no commercial interruptible reverse flow service available at Moffat. To allow this to happen, certain industry agreements require amendment - two of which are the Connected System Exit Point (CESP) ancillary agreement and the Connected Systems Agreement (CSA). These are both ancillary agreements to the Uniform Network Code (UNC) and can be modified via the UNC modification process.

## The modification proposal

The modification proposal seeks to amend and restate the Moffat CSEP ancillary agreement. The CSEP ancillary agreement will be amended and restated to become the Moffat Ancillary Agreement (MAA).

The CSEP ancillary agreement is an agreement between National Grid Gas (NGG) and CSEP users. It contains specific commercial terms for National Transmission System (NTS) shippers transporting to the interconnector at Moffat. It specifies rules governing the booking of capacity at exit points, energy allocations and nominations, and rules around the rates and quantities of offtake. The modification proposes that the following changes are made, among others:

<sup>1</sup> The terms 'the Authority', 'Ofgem' and 'we' are used interchangeably in this document. Ofgem is the Office of the Gas and Electricity Markets Authority.

<sup>2</sup> This document is notice of the reasons for this decision as required by section 38A of the Gas Act 1986.

<sup>3</sup> Regulation (EC) No 715/2009 of the European Parliament and of the Council of 13 July 2009 on conditions for access to the natural gas transmission networks and repealing Regulation (EC) no 1775/2005, see [www.eurlex.europa.eu](http://www.eurlex.europa.eu).

<sup>4</sup> Article 5(1) of the Second Package Gas Regulation (Regulation (EC) No 1775/2005 of the European Parliament and of the Council of 28 September 2005 on conditions for access to the natural gas transmission networks) also required a Transmission System Operator (TSO) to make maximum capacity in its gas transmission system available to market participants. The Second Package Gas Regulation was repealed by the Third Package Gas Regulation on 3 March 2011 and the Third Package Regulation applies from 3 March 2011.

<sup>5</sup> Article 4(1) of the Second Package Gas Regulation also required a TSO to provide both firm and interruptible third party access services.

- designate Moffat as a System Entry Point (SEP)
- allow users to declare whether they wish to be a CSEP user, or a SEP user, or both
- make provisions to allow SEP users to make NTS entry nominations and receive entry energy allocations at the SEP
- ensure that no physical NTS entry flow can occur, through ensuring that exit allocations are equal to or greater than entry allocations, and through ensuring SEP users only hold daily interruptible NTS entry capacity
- make provisions for the supply of Offtake Profile Notices (OPNs) - these instruct NGG how the physical gas flow from GB to Ireland will be profiled each hour
- make provisions for a virtual reverse flow allocation mechanism.

The modification proposal also seeks to amend the CSA. The CSA is an agreement between NGG and Bord Gáis Eireann (BGE) (UK) Ltd. It contains provisions for taking (or exiting) gas from the NTS at Moffat. The proposed changes to the CSA include:

- identifying Moffat as a SEP, but forbidding physical flow onto the NTS at Moffat
- changing the single end of day physical meter volume which BGE (UK) Ltd currently provides to three volumes: gross commercial exit quantities, gross commercial entry quantities and net physical quantity
- make provisions for the supply of OPNs.

The proposer thinks UNC352 will better facilitate the following UNC relevant objectives:

(b) coordinated, efficient and economic operation of (i) the combined pipeline system, and/or (ii) the pipeline system of one or more other relevant gas transporters  
 (d) securing of effective competition between: (i) relevant shippers; (ii) relevant suppliers; and/or (iii) DN operators (who have entered into transportation arrangements with other relevant gas transporters) and relevant shippers.

### **UNC Panel<sup>6</sup> recommendation**

The Joint Office received five responses to its consultation on UNC352. Of these responses, all supported the modification. The UNC Panel voted on the modification on the 15 September 2011. All 11 panel members voted in support of UNC352. Therefore the UNC panel recommended implementing UNC352.

### **The Authority's decision**

**The Authority has considered the issues raised by the modification proposal and the Final Modification Report (FMR) dated 15 September 2011. The Authority has considered and taken into account the responses to the Joint Office's consultation on the modification proposal which are attached to the FMR<sup>7</sup>. The Authority has concluded that:**

- 1. implementation of the modification proposal will better facilitate the achievement of the relevant objectives of the UNC<sup>8</sup>; and**

<sup>6</sup> The UNC Panel is established and constituted from time to time pursuant to and in accordance with the UNC Modification Rules

<sup>7</sup> UNC modification proposals, modification reports and representations can be viewed on the Joint Office of Gas Transporters website at [www.gasgovernance.com](http://www.gasgovernance.com)

<sup>8</sup> As set out in Standard Special Condition A11(1) of the Gas Transporters Licence, see <http://epr.ofgem.gov.uk/index.php?pk=folder590301>

**2. directing that the modification be made is consistent with the Authority's principal objective and statutory duties<sup>9</sup>.**

**Reasons for the Authority's decision**

We consider that UNC352 will bring about enhanced liquidity and through this, improved competition. It also facilitates an economic and efficient way to trade gas between Ireland and GB. Protecting existing and future consumers is Ofgem's principal objective and facilitating a competitive market and economic solutions are key to this.

*Standard Special Condition A11(1)(a): efficient and economic operation by the licensee of its pipe-line system*

UNC352 is one step in allowing users of the interconnector access to a virtual product for reverse flow from Ireland to GB. Virtual flow is the netting off from physical forward flows, which means that actual gas flows from GB to Ireland will be more economic and efficient. The implementation of UNC352 would therefore allow existing assets to be used more efficiently and economically where demand and supply conditions suggest gas should move from Ireland to GB.

*Standard Special Condition A11(1)(b): Coordinated, efficient and economic operation of (i) the combined pipe-line system, and/ or (ii) the pipe-line system of one or more other relevant gas transporters*

The proposer indicates that UNC352 will facilitate energy nominations and allocations into the NTS, allowing greater co-ordination between the NTS and Irish pipeline systems and their users. The proposer notes that the potential for virtual flows in addition to physical flows will support user choice and efficient and economic operation of the Irish system.

Three respondents supported this view. Another respondent disagreed on the basis that it did not consider that TSOs in Ireland are 'relevant gas transporters'.

NGG's gas transporter licence defines 'relevant gas transporter' as 'a gas transporter who is a Distribution Network operator or an NTS operator'<sup>10</sup>. This definition excludes Irish transporters. However, as noted above we consider that UNC352 would support efficient and economic operation of the pipeline system, and this extends to the systems of relevant gas transporters.

*Standard Special Condition A11(1)(d): Securing of effective competition: (i) between relevant shippers; (ii) between relevant suppliers; and/or (iii) between DN operators (who have entered into transportation arrangements with other relevant gas transporters) and relevant shippers*

The proposer indicates that UNC352 would increase market liquidity by facilitating greater access to the GB market, and that implementation would provide for greater competition both through the additional supplies allowed into the GB market, and through the potential for greater nominations and allocations from the NTS into Ireland in excess of the physical exit flow.

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<sup>9</sup> The Authority's principal objective and statutory duties are wider than matters which the Panel must take into consideration and in relation to gas are detailed mainly in the Gas Act 1986.

<sup>10</sup> As set out in Standard Special Condition A3 of the Gas Transporters Licence, see <http://epr.ofgem.gov.uk/index.php?pk=folder590301>

All five respondents supported the view that the modification would better achieve effective competition. One respondent noted that it has not been possible to assess the extent to which any new interruptible reverse flow service would be utilised, and hence the extent to which these relevant objectives might be met.

We consider there is value in facilitating a virtual reverse flow service as this allows for greater potential competition for gas.

*Standard Special Condition A11(1)(f): Promotion of efficiency in the implementation and administration of the code*

One respondent noted that there may be an increased risk to existing NTS exit capacity holders who have no interest in reverse flow but who may become exposed to energy allocation errors which are not possible under prevailing arrangements.

We note the risk of managing extra data flows from the virtual reverse flow product. However, there are already default arrangements in the UNC to deal with such data errors. Furthermore, the UNC allows for shippers to appoint an agent to manage this risk.

### **Wider statutory duties**

In making this decision, we have been mindful of our principal objective and statutory duties including our duty to promote effective competition, to secure a diverse and viable long-term energy supply and our duty to secure that all reasonable demands in GB for gas conveyed through pipes are met.

The Third Package Gas Regulation<sup>11</sup> provides that when carrying out their responsibilities, the regulatory authorities must ensure compliance with the Third Package Gas Regulation. Article 41 of Directive 2009/73/EC<sup>12</sup> provides that the regulatory authority has to comply with and implement any relevant decisions of the Agency for the Cooperation of Energy Regulators (ACER) and of the European Commission.

The general objectives of the regulatory authority under this directive<sup>13</sup> include the objectives of developing competitive and properly functioning regional markets within the Community and eliminating restrictions on trade in natural gas between Member States, including developing appropriate cross-border transmission capacities to meet demand and enhancing the integration of national markets which may facilitate natural gas flow across the Community.

In line with these objectives, we note that virtual reverse flow should support user choice and efficient and economic operation of the Irish system. In particular, nominations to counter flow are likely to occur when there are other more economic sources of gas available – such as from storage or future gas fields – or reductions in demand. Virtual reverse flows may therefore facilitate a more efficient outcome and lead to the better functioning of both the GB and Irish markets. UNC352 is a first step in better meeting our general objective under the Third Package to develop properly functioning regional markets.

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<sup>11</sup> Article 24 of the Regulation (EC) No 715/2009 of the European Parliament and of the Council of 13 July 2009 on conditions for access to the natural gas transmission networks and repealing Regulation (EC) no 1775/2005.

<sup>12</sup> Directive 2009/73/EC of the European Parliament and of the council of 13 July 2009 concerning common rules for the internal market in natural gas and repealing Directive 2003/55/EC.

<sup>13</sup> Article 40 of the Directive 2009/73/EC of the European Parliament and of the council of 13 July 2009 concerning common rules for the internal market in natural gas and repealing Directive 2003/55/EC.

Although relevant amendments to domestic legislation and to licences in furtherance of Third Package implementation have not yet been made, we are under a legal obligation to construe (as far as possible) our statutory duties in accordance with the relevant Third Package requirements<sup>14</sup>. We therefore note that we consider that UNC352 is consistent with our duties under the Third Package Gas Regulation and with our duties and general objectives under Directive 2009/73/EC.

### **Other considerations**

One respondent noted that the method for establishing overrun charges in the UNC is ineffective when applied to virtual reverse flows. Overrun charge rates, applied to overrun volumes, are determined by applying a multiplier to capacity prices. However, UNC352 involves the sale of interruptible entry capacity at a zero reserve price, and the respondent assumes that the price will never go above zero. On this basis any overrun charge will be zero, thereby weakening the incentive on shippers to book entry capacity and to flow gas only up to the level of their capacity holding.

We acknowledge that under these circumstances overrun charges will not provide an effective incentive to flow gas only up to the level of the capacity holding. However, our understanding is that the overrun charge is to ensure that the system is not compromised by physical flows higher than system capability. In the case of virtual reverse flows there will be no physical flows entering the NTS at Moffat and so compromising the system is not a significant concern. After discussion with NGG we understand that this is a more general issue, not specific to Moffat, and something NGG is proposing to raise with industry.

One respondent took the opportunity to remind NGG that implementing UNC352 should not lead to any detrimental effect on the supply of gas to the Scottish town of Stranraer (which is supplied via the Moffat interconnector). As UNC352 only enables virtual reverse flow to take place we do not consider UNC352 to be detrimental in this way.

This approval relates solely to the revisions to the two ancillary agreements (CSA and MAA). It should be noted that Ofgem's decision to approve the revisions to the CSA and MAA and the comments included in this decision letter are without prejudice to Ofgem's discretion in respect of any future decisions.

### **Decision notice**

**In accordance with Standard Special Condition A11 of the Gas Transporters Licence, the Authority hereby directs that modification proposal UNC352: 'The introduction of an interruptible reverse flow service at Moffat interconnector' be made.**

**Martin Crouch**

**Partner, European Strategy**

**Signed on behalf of the Authority and authorised for that purpose.**

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<sup>14</sup> The deadline for transposition of the relevant provisions of the Third Package Gas Regulation and of Directive 2009/73/EC into domestic legislation was 3 March 2011, and as such the Third Package Gas Regulation applies from that date. The Department of Energy and Climate Change laid before Parliament transposing regulations under section 2(2) of the European Communities Act 1972 on 18 July 2011 (the Regulations). We expect the Regulations to be in force in November 2011. You can now view the Regulations, including the proposed changes to the duties of the Authority and to UNC objectives at the following link: <http://www.legislation.gov.uk/ukdsi/2011/9780111513965/contents>