

## Explanation of the NTS SO Commodity Charges for the formula year 2013/14 – Indicative 1 February 2014

Please note that only the SO charges have changed at February 2014 and so the TO charges are unchanged with the relevant information available in the October 2013 Final document.

National Grid sets its charges to recover the price controlled allowances set by Ofgem. Ofgem has issued its Final Proposals for the RIIO-T1 price control to apply from 1 April 2013.

National Grid has used Ofgem's RIIO-T1 Price Control as the basis for calculating the charges contained in the Notice of Change to NTS Transportation Charges effective from 1 February 2014.

### Introduction

This document seeks to provide greater transparency to the processes and data used by National Grid Gas NTS ("National Grid") to set the NTS System Operation (SO) and Transportation Owner (TO) Commodity Charges.

Charges are generally set before actual costs and allowed revenues have been finalised and can be subject to significant variances and volatility throughout the year, which are amplified by the fact that Indicative and Final notices and their related costs are forecast 150<sup>1</sup> days and 2 months before actual charges are implemented and costs incurred.

National Grid has an obligation to use its best endeavours in setting its charges to ensure that, in respect of any formula year, the revenue which it derives (from  $SOR_t$  &  $TOR_t$ ) shall not exceed the maximum NTS allowed revenue ( $SOMR_t$  &  $MR_t$ ).

Therefore, as costs fluctuate throughout the year, the charging obligations on National Grid ensure that charges must fluctuate as well.

By providing greater transparency of the individual cost components and how these contribute to charges, NTS users could potentially forecast any future fluctuations and price changes.

If you would like further information on how the costs and allowed revenues are derived, please refer to System Operator incentive consultations, TO Price Control documents and charging notices for further detail regarding these matters.

### Other related information sources

This document is one of a suite of documents that describe the NTS charges levied by National Grid and the methodologies behind them. The other documents that are available are:

- Statement of the Gas Transportation Charging Methodology
- Statement of Gas Transmission Transportation Charges
- Entry & Exit Capacity Release Methodology Statements
- Transmission Connection Charging Statement

<sup>1</sup> In exceptional circumstances notices may be made in a time period less than 150 days such as a third price change

These are available on our Charging website at:  
<http://www.nationalgrid.com/uk/Gas/Charges/statements/>

### **Structure of this document**

This document is divided into three sections:

- Part A relates to the SO Commodity Charge;
- Part B relates to the TO Entry Commodity Charge;
- Part C relates to the TO Exit Capacity and TO Exit Commodity Charges;
- Part D provides details of the annual charge setting timetable and sources of further information.

### **Comments & Feedback**

As part of our commitment to customers, National Grid welcomes comments and feedback on the information contained in this notice. In particular, to ensure that information is provided and presented in a way that is of most use to customers, we would welcome specific feedback on:

- the level of numeric detail provided to explain charge changes;
- the quality of the explanation given to describe and explain charge changes;
- information that is not useful and could be omitted; and
- information that is missing that could be added.
- These should be sent to:

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## PART A: SO COMMODITY CHARGE

The SO Commodity Charge recovers the difference between the SO allowed revenue and revenues received from other SO charges.

To derive the SO Commodity Charge a number of high-level steps are required:

- Step 1:** Determine the SO allowed revenue
- Step 2:** Determine the revenue to be recovered from the SO Commodity Charge
- Step 3:** Determine the volumes that attract the SO Commodity Charge
- Step 4:** Calculate the SO Commodity Charge rate

### Step 1: Determining the SO allowed revenue

The maximum NTS SO allowed revenue in respect of formula year  $t$  ( $SOMR_t$ ) is defined in National Grid's Gas Transporter Licence for the NTS ("the Licence")<sup>2</sup>. It is calculated using the following formula:

$$SOMR_t = SOBR_t + CM_t + SOOIRC_t + TSS_t + DELINC_t - SOK_t$$

Table 1 details the individual terms contained in the equation above, which have been used to determine the charges that applied during the relevant year. Note that all the figures quoted within this note relate to the entire formula year, 2013/14.

**Table 1**

Terms used for Final notification of charges	Feb Value (£m)	Oct Value (£m)
Base Price Control SO Revenue (SOBR <sub>t</sub> )	187.4	187.4
Constraint Management revenue adjustment (CM <sub>t</sub> )	30.2	30.2
SO external incentive adjustment (SOOIRC <sub>t</sub> )	128.2	152.8
SO Transportation Support Services revenue adjustment (TSS <sub>t</sub> )	8.4	8.4
SO Legacy accelerated incremental capacity delivery incentive (DELINC <sub>t</sub> )	9.1	9.1
Revenue adjustment term for prior year (SOK <sub>t</sub> ) *	0.9	0.9
<b>Maximum NTS SO allowed revenue (SOMR<sub>t</sub>)</b>	<b>362.3</b>	<b>387.0</b>

\*SOK<sub>t</sub> is deducted in the SOMR<sub>t</sub> formula. Therefore any under recovery is shown as ().

For further details of the SO allowed revenue, refer to Special Condition 2A "NTS System Operation activity revenue restriction".

### *Typical variations in SOMR<sub>t</sub>*

The values in Table 1 are subject to uncertainty, particularly those that are linked to externalities such as gas costs. It is anticipated that separate reporting of the SO external incentive performance will allow shippers to better predict future price movements. However, shippers may wish to note that the new Licence makes allowances for many of the cost terms and so it is the variation from the allowance that is added on to the base revenue that makes up the maximum allowed revenue (SOMR<sub>t</sub>).

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<sup>2</sup> Draft Licence

## Step 2: Determining the target revenue for the SO Commodity Charge

The maximum NTS SO allowed revenue is collected through a number of charges in addition to the standard SO Commodity Charge. The revenue from these other charges must first be forecasted so that the residual target revenue to be collected through the SO Commodity Charge can be calculated. The SO Commodity charge is set such that the target actual SO Revenue equals the maximum NTS allowed revenue. The actual NTS SO revenue (SOR<sub>t</sub>) is calculated using the following formula:

$$SOR_t = SOREntC_t + SOROC_t + SORExC_t + RCOM_t$$

**Other SO Charges:** Tables 2 to 4 show the build up of other SO charges.

### *Associated SO charges*

Forecasted revenue resulting from associated SO charges levied by National Grid is deducted from the maximum NTS SO allowed revenue total.

Table 2

Terms used for Final notification of charges	Feb Value (£m)	Oct Value (£m)
Balancing Neutrality Charge	6.0	6.0
Capacity Neutrality Components (revenues)	A	A
<b>Adjustment for Neutrality (SOROC<sub>t</sub>)</b>	<b>6.0+A</b>	<b>6.0+A</b>

Please refer to our Charging Methodology Statement for further information regarding any terms mentioned within this section of the document.

### *Adjustments for the sale of legacy incremental capacity*

Revenue from the sale of **legacy** incremental entry and exit capacity is deducted as this is recovered through the relevant capacity charges. For entry the amount equates to revenue resulting from any incremental capacity allocated through the Entry Capacity auctions held ahead of the gas day and this capacity may either be obligated or non-obligated. The revenue is effectively used to net off the incremental SO allowed costs included in SOMR<sub>t</sub>. For exit the adjustment is equal to the forecasted revenue collected in the formula year in relation to Exit Charges for firm exit capacity above the baseline. An adjustment is also made for sales of SO non-obligated exit capacity.

Table 3

Terms used for Final notification of charges	Feb Value (£m)	Oct Value (£m)
Sales of Non-Obligated Exit	1.20	1.1
Legacy Entry Capacity Investment Revenue	15.0	15.0
Legacy Exit Capacity Investment Revenue	7.3	7.4
<b>Adjustment for the sale of incremental capacity</b>	<b>23.5</b>	<b>23.6</b>

### *Adjustments for other Charges*

A proportion of the SO costs are recovered through the St Fergus Compression Charge, Shorthaul Commodity Charge and Capacity Neutrality Buyback revenue. The St Fergus Compression Charge recovers the compression costs associated with the St. Fergus TOM sub-terminal directly from those shippers at that terminal due to local pressure tier arrangements. The optional Shorthaul Commodity Charge is offered as a replacement to the TO and SO Commodity Charges. In all cases, the forecast revenue recovered from these charges is deducted from SOMR<sub>t</sub>.

Table 4

Terms used for Final notification of charges	Feb Value (£m)	Oct Value (£m)
St Fergus Compression Revenue	16.8	18.5
Shorthaul Revenue	15.6	15.7
Capacity Neutrality Buyback Costs recovered through Capacity Neutrality	2.3	3.0
Capacity Neutrality Components (revenues credited via capacity neutrality)*	-A*	-A*
<b>Adjustment for other Commodity Charges</b>	<b>34.7-A</b>	<b>37.2-A</b>

\*This cancels out the figure in Table 2 and therefore has no impact on the SO Commodity charge

The target revenue to be recovered through the SO Commodity Charge is as follows:

Table 5

Terms used for Final notification of charges	Feb Value (£m)	Oct Value (£m)
Maximum Allowed NTS SO revenue (SOMRt)	362.3	387.0
...less associated SO charges	6.0	6.0
...less sales of incremental capacity	23.5	23.6
...less other charges	34.7	37.2
<b>Remainder of RCOM i.e. revenue to be collected through SO Commodity Charge</b>	<b>298.1</b>	<b>320.3</b>

The figure changes as National Grid's view of the above costs and revenue change. Table 6 details how the target revenue to be collected through the SO Commodity Charge has varied during the formula year.

Table 6

Target SO Commodity Charge Revenue in relevant year (£m)				
Prices to apply from April		Prices to apply from October		Prices to apply from February 14
Indicative	Final	Indicative	Final	Indicative
376.5	338.9	339.9	320.3	298.1

### Step 3: Determining the volumes that attract the SO Commodity Charge

The volumes that attract the SO Commodity Charge are those forecast entry and exit flows excluding storage flows, net of shorthaul volumes i.e. the volumes that shippers have nominated to attract the Shorthaul Commodity Charge. Shippers can nominate to go to Shorthaul at any time throughout the year.

Table 7 shows the volumes used for the prices set for the formula year.

**Table 7**

Volumes used for setting SO Commodity Charge in relevant year (GWh)				
Prices to apply from April <i>(April to March Volumes)</i>		Prices to apply from October <i>(October to March Volumes)</i>		Prices to apply from February 14 <i>(February to March Volumes)</i>
Indicative	Final	Indicative	Final	Indicative
1,639,858	1,658,338	989,158	903,536	313,427

The flow data is updated as part of the demand forecasts published in mid-May. Therefore, shippers may observe different flow assumptions for the final notice of the October price change.

### Step 4: Calculation of the SO Commodity Charge rate

The SO Commodity Charge is collected from non-storage entry and exit flows excluding shorthaul flows, therefore to calculate the charge rate to apply from April the following formula is used:

$$\frac{\text{Forecast revenue from SO Commodity Charge (£m)}}{\text{Forecast Flows (GWh)}} \times 100$$

#### ***Mid-year updates to the SO Commodity Charge***

The commercial framework allows the SO Commodity Charge to be revised in October. Further updates are permitted in exceptional circumstances.

When making a mid-year price update, the actual revenue collected during the year to date is deducted from the revised forecast annual revenue, and the remaining flows for the year considered.

For example, to update prices in October the following formula is applied:

$$\frac{\text{Forecast revenue from SO Commodity Charge - Revenue Apr to Sep (£m)}}{\text{Forecast Flows between Oct and Mar (GWh)}} \times 100$$

#### **Forecast revenue recovery through SO Commodity Charge**

Table 8 shows the forecast monthly flows that will attract the SO Commodity Charge and the expected revenue from this charge. Data shown in red is based on actuals, other data is forecast.

Table 8

Apr-13	May-13	Jun-13	Jul-13	Aug-13	Sep-13
0.0176 p/kWh	0.0176 p/kWh	0.0176 p/kWh	0.0176 p/kWh	0.0176 p/kWh	0.0176 p/kWh
£57,339,018			£38,465,760		

Oct-13	Nov-13	Dec-13	Jan-14	Feb-14	Mar-14
105,499 GWh	140,178 GWh	167,458 GWh	176,974 GWh	154,643 GWh	158,784 GWh
0.0251 p/kWh	0.0251 p/kWh	0.0251 p/kWh	0.0251 p/kWh	0.0173 p/kWh	0.0173 p/kWh
£26,480,202	£35,184,569	£42,032,047	£44,420,492	£26,753,319	£27,469,581

Charges are always set to recover the exact amount of allowed revenue for the formula year, however, as costs and volumes are not fixed and are subject to variability, any forecast/actual difference between allowed revenue and actual revenue feeds through into the formula year in two years time (with the appropriate interest adjustments made). This is through the NTS SO revenue adjustment term  $SOK_t$  which applies in that formula year.

## **PART D: CHARGING TIMETABLE & FURTHER INFORMATION**

### **Charging timetable**

Charge changes are published by the following dates throughout the year:

<b>Date (by)</b>	<b>Notification of...</b>
3 November	Indicative charges to apply from following 1 April
31 January	Final charges to apply from following 1 April
3 May	Indicative charges to apply from following 1 October
31 July	Final charges to apply from following 1 October

Notices of the updates will be posted on National Grid's industry website and on the Joint Office's website. The updates will also be notified via the Joint Office's email notification service.

### **Further information**

If you require further details about any of the information contained within this document or have any comments on how this document might be improved please contact us at [box.transmissioncapacityandcharging@nationalgrid.com](mailto:box.transmissioncapacityandcharging@nationalgrid.com).