

Modification Report
Reconciled SO Commodity Charges at Storage Facilities
Modification Reference Number 0547
Version 1.0

This Modification Report is made pursuant to Rule 7.3 of the Modification Rules and follows the format required under Rule 8.9.3.

1. The Modification Proposal

The PC70 proposal recommends a methodology for applying the System Operator (SO) commodity charge to be imposed on gas exiting the NTS to a storage site.

Storage facilities can be considered to provide a parking service for gas. Gas which leaves the NTS and is injected into a storage site will, at some point in time be redelivered to the NTS, normally during periods of higher than average demand. Gas which is injected into storage and is used by the storage owner (own-use gas) is not classed as parked gas and is treated differently.

There can be no debate that the costs incurred by Transco for transporting gas to storage facilities are directly related to the actual physical volumes transported and as a result a cost-reflective commodity charge must be based on the physical flows which occurred over the relevant charging period.

This proposal endeavours to design a charge, which complies with the principle of cost reflectivity and additionally, is relatively easy and economical to administer.

The proposal applies the reconciliation mechanism adopted for exit points following the recovery of actual allocated flows. It is proposed that in the first instance, on the 30th September of each gas year, aggregate net flows are calculated. This derived on the basis of the difference between the aggregate actual injections and the aggregate actual withdrawals during the relevant Gas Year. If the result is positive then a charge (which may be based on a negative rate to achieve cost reflectivity) should be applied to those shippers who, during the relevant period, were net injectors.

The total charge ("Total reconciled charge") to be applied should be equal to the net aggregate flows multiplied by the relevant SO commodity rate

On the 30th September of each gas year, net flow volumes per shipper ($\text{injections}(\text{yr } x) - \text{withdrawals}(\text{yr } x)$) are calculated.

The total reconciled charge is then allocated to the net injecting shippers on a pro-rata basis i.e. for $\text{GBP} = (\text{net flow of shipper} / \text{aggregate net flow}) * (\text{aggregate net flow} * \text{SO Commodity charge}) / 100$.

If the net aggregate flow is negative then no charge will be applied.

2. Transco's Opinion

Transco does not recommend implementation of the Modification Proposal for the following reasons:

Transco recognises the benefits to Users of the "parking service" that storage provides. Availability of gas in storage facilities may, for example, assist Users in minimising their daily imbalance. However, with the exception of peak demand days or days associated with supply or transmission failure, the value of a storage parking service to the System Operator is limited. This is due to the long durations typically associated with injection and withdrawal. If charges were to reflect the value of any parking service they would need to embody injection and withdrawal durations as basic parameters. This Proposal, however, makes no such allowance and therefore implementation would not contribute to the efficient operation of the pipeline system.

Unlike the four alternatives proposed under Modification Proposal 0532 which was simultaneously issued for consultation, this Proposal would create charging based on total gas flows over the Gas Year, rather than over each gas flow day. Transco believes that as the SO costs tend to be associated with physical flows on individual days, charging based upon net daily flows would be more cost reflective. In particular, basing charges on the net quantities aggregated over a period longer than a day would essentially lead to non-storage users subsidising storage users.

Transco did not see any benefit in separately accounting for Storage Use Gas (SUG). Over a period of time, the difference between injection and withdrawal would equal the quantity of SUG and thus would automatically be charged at the relevant commodity rate. Transco requested representations on this issue.

3. Extent to which the proposed modification would better facilitate the relevant objectives

The Proposer believes that by using a cost-reflective methodology, Transco would fulfil the Relevant Objective: the efficient and economic operation by the licensee of its pipeline system. Transco, however, as expressed above, believes the Proposal is less cost reflective than charging based on daily flows.

4. The implications for Transco of implementing the Modification Proposal , including a) implications for the operation of the System:

Transco has not identified any implications for operation of the System.

b) development and capital cost and operating cost implications:

Transco would incur costs in amending its UK-Link System. The extent of these costs has not been identified at this stage.

c) extent to which it is appropriate for Transco to recover the costs, and proposal for the most appropriate way for Transco to recover the costs:

Transco is not recommending implementation of this Modification Proposal. However, if this Proposal were implemented, any recovery of costs would be through the usual channels.

d) analysis of the consequences (if any) this proposal would have on price regulation:

Transco is not aware of any consequences this Proposal would have on price regulation.

5. The consequence of implementing the Modification Proposal on the level of contractual risk to Transco under the Network Code as modified by the Modification Proposal

Transco does not anticipate that there would be any consequences on the level of contractual risk under the Network Code, as a result of implementing this Modification Proposal.

6. The development implications and other implications for computer systems of Transco and related computer systems of Users

Transco has identified that systems development would be required by both Users and Transco.

7. The implications of implementing the Modification Proposal for Users

It is likely that Users would need to alter their systems and processes to accommodate implementation of this Modification Proposal.

8. The implications of implementing the Modification Proposal for Terminal Operators, Consumers, Connected System Operators, Suppliers, producers and, any Non-Network Code Party

Transco has identified that the introduction of additional costs may have implications on the value placed on storage services by storage users.

9. Consequences on the legislative and regulatory obligations and contractual relationships of Transco and each User and Non-Network Code Party of implementing the Modification Proposal

Transco does not anticipate any consequences on the legislative and regulatory obligations and contractual relationships of each User and non-Network Code party of implementing the Modification Proposal.

10. Analysis of any advantages or disadvantages of implementation of the Modification Proposal

Advantages:

The Proposer argues that it seeks to minimise cross-subsidies between System Users and the potential over-recovery of revenues from storage users.

Simple to administer

Consistent with the reconciliation process carried out for other system exit points

Disadvantages:

Not wholly consistent with the spirit of PC70 objectives

Potentially discriminatory as non-storage users could be regarded as subsidising storage users

The change of inventory and apportionment to shippers may cause a problem.

11. Summary of the Representations (to the extent that the import of those representations are not reflected elsewhere in the Modification Report)

Modification Proposals 0532, 0545 and 0547 were issued simultaneously for consultation. Some respondents requested that their general comments in response to Modification Proposal 0532 be considered alongside these representations. The following tabulates ten responses to Modification Proposal 0547:

Respondents

SSE Energy Supply Ltd (SSE)
PowerGen UK plc (PG)
British Gas Trading (BGT)
AEP Energy Services Ltd (AEP)
Shell Gas Direct (SGD)
Scottish Power (SP)
London Electricity plc (LE)
Entergy-Koch (EKTL)
Dynegy (DYN)

Responses

Against
Against
Against
Against
Against
For
Against
For
Recommends development of Modification Proposal 0546 before concluding its response.
Against

BG Group (BG)

In addition, a response was received from the Association of Electricity Producers after the consultation close-out period.

The view of SSE was that "gas injected to and withdrawn from storage by a User effectively uses the transportation system on two separate occasions, and therefore it is more appropriate that the charges should be based on net daily flows. Furthermore, Modification 0547 proposes that the charge would be reconciled annually at the end of the Gas Year,

whereas the SO commodity charge has been set to recover costs on a daily basis in the context of the price control year."

PG expressed the view that this Proposal did not provide a mechanism to fairly allocate SO charges between Storage Users. BGT also expressed its view that calculations of charges should be carried out on a daily basis. AEP confirmed that it did not believe the Proposal would better facilitate the relevant objectives.

SGD confirmed it did not support the Proposal as an annual charge would be less cost-reflective than a daily charge. SGD believed this Proposal could incur "a cross-subsidy from non-storage users to storage users, and as such would be discriminatory."

SP believed that this Proposal "complies with the main aims of PC70 and furthers the relevant objective as well as being cost reflective." SP did not believe that "there is any subsidy of storage users by non-storage users". "Alternatively, we believe that charging all storage users a commodity charge for parking their gas, or balancing effectively, is subsidising the system".

LE did not support this Proposal on the basis that "it reduces the cost of efficiency of using storage by charging a commodity charge on net injection, but does not rebate users for withdrawal."

EKTL considered this Proposal "better recognises the fact that storage sites and the NTS are constituents of an integrated system" and was "the best way to implement the charging proposal outlined in the Pricing Consultation paper PC70." EKTL believed that the application of the SO charge on a more onerous basis i.e. on a daily basis, would be detrimental to the system, as storage use would become less attractive.

Whilst DYN recommended the development of Modification Proposal 0546 before concluding its response, it expressed support for this Proposal. "The modification recognises the importance of ensuring a charge is allocated to the net position of users, thus ensuring to minimise cross-subsidies between system users and the potential over-recovery of revenues from storage users."

Whilst BG has expressed opposition to the introduction of this element of PC70, it acknowledged that this Proposal had some merits; taking a view over the year and levying the charge over that period. Additionally, BGT supported Entergy-Koch's suggestion that separate rules would be required for Own Use Gas.

The Association of Electricity Producers did not support the Proposal.

Transco's Opinion

Transco considers that it would be more cost-reflective to apply the SO Commodity Charge on the basis of daily flows in regard of storage offtakes. This would be consistent with the method of application of other transportation charges. Whilst Transco recognises the

security of supply benefits that may be provided by storage, it considers that this Proposal does not constitute an appropriate way of incentivising such provision, if such incentivisation were to be proposed. Transco is of a similar opinion to the majority of respondents that implementation of this Proposal would not be expected to further the relevant objectives.

12. The extent to which the implementation is required to enable Transco to facilitate compliance with safety or other legislation

Implementation of this Modification Proposal is not required to enable Transco to facilitate compliance with safety or other legislation.

13. The extent to which the implementation is required having regard to any proposed change in the methodology established under Standard Condition 4(5) or the statement furnished by Transco under Standard Condition 4(1) of the Licence

Implementation of a Modification Proposal is required to enable the implementation of SO Commodity Charges to all NTS loads from 2002 as set out in PC70.

14. Programme of works required as a consequence of implementing the Modification Proposal

Systems development work would be required to enable implementation of this Modification Proposal.

15. Proposed implementation timetable (including timetable for any necessary information systems changes)

In view of Transco's recommendation, no implementation timetable is proposed.

16. Recommendation concerning the implementation of the Modification Proposal

Transco does not recommend implementation of this Modification Proposal.

17. Restrictive Trade Practices Act

If implemented this proposal will constitute an amendment to the Network Code. Accordingly the proposal is subject to the Suspense Clause set out in the attached Annex.

18. Transco's Proposal

This Modification Report contains Transco's proposal not to modify the Network Code and Transco now seeks agreement from the Gas & Electricity Markets Authority in accordance with this report.

19. Text

Signed for and on behalf of Transco.

Signature:

Tim Davis
Head of Regulation NT&T

Date: