TRANSCO NETWORK CODE MODIFICATION PROPOSAL No. 0508

"A method of Long Term Capacity Allocation"
Version 2.0

Date: 17/12/2001

Proposed Implementation Date:

Urgency: Non-Urgent

Justification

As part of the development of long term NTS investment signals, the RGTA workstream has been discussing and developing methodologies for the long term allocation of firm entry capacity. The purpose of this proposal is to introduce an alternative long term allocation methodology to that which has been proposed by Modification proposal 0500 ‘Long Term Capacity Allocation’ in order that this can also be considered and developed by the RGTA worksteam.

Nature of Proposal

This proposal sets out a process whereby Users are able to purchase long term entry capacity rights in the NTS to suit their portfolio and business requirements. All prices will be ring-fenced and not adjusted as a consequence of subsequent auctions or price controls. This proposal provides clear signals of future capacity requirements to Transco and underwrites any required incremental investment.

Each year Transco will sell Long Term Entry Capacity (LTEC) in quarterly segments, Quarterly System Entry Capacity (QSEC), commencing with year Y+1 (i.e. from 1st October 2002) for the period required by the Users. Upon completion of the auction process, any unsold capacity beyond Y+1 will be carried to the next annual auction.
All capacity will be offered on the basis of an end of day quantity from which is derived an equal hourly flow rate against which Users have purchased a right to flow gas. Payment, as now, will continue to be due the month after the month of potential use and will be charged on a pence per kWh basis.

As with other capacity products, Users will have the opportunity to trade their QSEC at any time. The payment liability will remain with the primary purchaser regardless of secondary market trading. However, any User liabilities associated with entry capacity management will take into account net capacity holdings and shall reflect the effect of capacity trades.

Transco will be exposed to the full cost of any buy-back liability arising out of any failure to accommodate flows of Users QSEC at any ASEP.

Overview of the capacity allocation process

Prior to the commencement of each annual LTEC allocation, Transco will issue a schedule of reserve prices by Aggregate System Entry Point (ASEP) associated with output measures to be specified in its Gas Transporter licence, together with an indicative cost schedule for the provision of capacity in excess of up to [50%] of the output measures. The reserve price will be based upon Transco's regulated revenues allocated between terminals according to long run cost. The available capacity for each quarter, which is the output measure less previously sold capacity, will also be published. All of this available capacity will be offered in the auction. Users will have a period of [2 weeks] to submit their QSEC requirements by quarter and ASEP to Transco. Upon closure of the submission period Transco will aggregate the Users QSEC demand by ASEP and publish the outcome of the round:

·if aggregate demand by ASEP in any quarter is less than or equal to the available capacity then all capacity demanded for that quarter will be offered at the reserve price;

·if aggregate demand by ASEP is greater than the available capacity for any quarter Transco will recalculate the cost of providing the additional incremental capacity demanded at each ASEP for the period(s) over which the incremental capacity is required. The cleared price for these periods will be the aggregate of the reserve price plus the cost of providing the incremental capacity spread over the volumes bid for these periods.

In addition Transco will provide details of the proposed investment programme by cost, location and timing.

A further round will take place within [7 days] during which Users will then have the opportunity to confirm their acceptance of these prices by leaving their bids unchanged, or to submit revised requirements by volume and ASEP.

This process will continue until, in response to Transco's latest demand / price schedule, either,

(i) Users make no further adjustments to their requirements or ,

(ii) The aggregate volumes and the auction clearing prices have not changed by more than [+/-X%] in any quarter at
any ASEP or,

(iii) After [6] iterations or if the process is diverging, mathematical principles are available to ensure that the process is closed out.

In conjunction with this LTEC allocation process there are other associated issues that require consideration. These issues are common to any long-term allocation process and include

· Agreement on satisfactory credit / security arrangements with Transco.
· The application of overrun to be adapted to reflect the new entry capacity regime
· Transparency of Transco's cost modeling processes and determination of prices

· Arrangements for shorter-term capacity products, which may include MSEC, DSEC, MISEC and DISEC.

However, Transco can only sell these short-term products for year Y+1 when the auction for that year is complete.

This proposal does not require any changes to entry capacity trading arrangements.

Purpose of Proposal

This Modification Proposal is intended to provide an alternative long-term allocation process for entry capacity to that proposed in modification proposal 0500. This proposal will enable Transco and Users to contract for long term firm capacity requirements, and give Users adequate time to consider and adjust their requirements in response to revised price/volume outputs from Transco.

The auction provides strong differentiated price signals to shippers, reflecting the additional costs their actions are imposing on the system; this creates strong incentives for shippers to adjust their positions so as to minimise excessive investment demands and ensures that Transco faces investment signals that are efficient.

The iterative process will provide reliable investment signals to Transco for it to use as part of its determination of the most efficient level of entry capacity needed to meet Users demands within the overall framework of Transco's Price Control. In addition Users underwrite the full cost of incremental capacity investments thus eliminating the risk of stranded assets. Furthermore the risk of revenue over recovery is minimised due to the use of cost reflective pricing in the process.

This proposal does not obligate Transco to build incremental capacity. This decision remains theirs alone. However this proposal will provide Transco with the full cost of any incremental capacity demanded by Users. Therefore, Transco will be exposed to the full cost of any buy-back liability arising out of any failure on its part to accommodate flows of Users QSEC at any ASEP.

The range of products available (including the secondary market) will provide every opportunity for new entrants to obtain their necessary capacity requirements and as such there is no need for any capacity to be held back from the LTEC process.

Consequence of not making this change

In the absence of the changes envisaged by this allocation proposal it will be difficult for Users to signal their capacity requirements and to commit with certainty to these long-term arrangements. Transco would in turn be denied appropriate signals to invest both efficiently and in a timely manner in incremental capacity.

Area of Network Code Concerned

Section B
Section L
Section S

Transition Arrangements

Proposer's Representative

Andrew Knights (TOTALFINAELF Exploration UK PLC)

Proposer

Peter Nicholls (Total Gas Marketing Ltd)

Signature

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