

TRANSCO NETWORK CODE MODIFICATION PROPOSAL No. 0523
"Recovery of Financing Costs for Operating Margins Gas"
Version 1.0

Date: 14/01/2002

Proposed Implementation Date:

Urgency: Non-Urgent

Justification

Currently, Section K of the Network Code requires Transco to procure Storage Space and fill that space with sufficient quantities of gas to satisfy Operating Margins (OM) requirements in relation to any given Storage Year. In doing so, Transco incurs financing costs for which it is not compensated.

Transco receives an operating expenditure (opex) allowance within its price control to fund the procurement of Storage Space for OM purposes. However, under existing Network Code arrangements Transco only recovers the cost of OM gas and other associated costs such as storage injection and withdrawal charges when and to the extent that OM gas is used. Financing costs are excluded from this process and as a result Transco receives no funding for the costs of financing an investment of approximately £9m in OM gas.

Previously, Section K5.4, version 2.00 (31 May 1998) of the Network Code allowed Transco to recover the financing costs it incurred in making sufficient quantities of Balancing Margins available in each Storage Year. Transco's obligations in relation to the use and procurement of gas for Balancing Margins purposes were akin to Transco's current obligations in relation to OM. Transco, therefore, believes that a precedent has already been set for the recovery of OM financing costs.

Nature of Proposal

It is proposed to amend the Network Code so that Transco may recover the financing costs that it incurs in making quantities of gas available for OM purposes.

It is proposed that for each day Transco would be entitled to recover an amount equal to:

(Weighted Average Cost of OM gas-in-storage) * (Neutrality Interest Rate)

where:

- a) Weighted Average Cost of Gas includes all costs associated with the procurement, delivery and injection of gas into Storage (excluding Storage Space charges);

- b) Neutrality Interest Rate means: the percentage rate calculated as the base rate for the time being of Barclays Bank plc divided by 365.

It is proposed that the Operating Margins Financing Cost would be included in the calculation of the Daily Margins Recovery Amount which is included within the balancing neutrality provisions of the Network Code.

Purpose of Proposal

Transco believes that this Modification Proposal would be consistent with Section 4AA(2)(b) Gas Act 1986 (as amended by the Utilities Act 2000) which requires that Transco is allowed sufficient funding to finance its activities in operating the gas transmission system.

Therefore, Transco believes that the Modification Proposal is consistent with Special Condition 3(1) of Transco's GT Licence, i.e. that Transco should secure sufficient financial facilities to enable it to carry on the Transportation business. Consistency with Special Condition 3(1) satisfies Transco's relevant objectives as defined by Standard Condition 9 of Transco's GT Licence which requires the efficient discharge of Transco's obligations under the GT Licence.

Consequence of not making this change

Unless this Modification Proposal is implemented Transco will continue to bear financing costs in complying with its Network Code OM obligations for which it is not compensated.

Area of Network Code Concerned

Section K 'Operating Margins'

Proposer's Representative

Andy Cruise (Transco)

Proposer

Tim M Davis (Transco)

Signature

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