



Shippers, Transco and Other
Interested Parties

*Bringing choice
and value to
customers*

Our Ref: net/cod/mod/0617
Direct Dial: 020 7901 7437
Email: mark.feather@ofgem.gov.uk

Dear Colleague,

Modification Proposal 0617 'Revision to the Standard Year for purposes of acquiring and holding Long Term System Entry Capacity'

British Gas Trading (BGT) raised modification proposal 0617 '*Revision to the Standard Year for purposes of acquiring and holding Long-Term System Entry Capacity*' on 19 February 2003.

Ofgem has carefully considered the issues raised in this proposal and has decided to direct Transco to implement this proposal because we consider that the modification will better facilitate Transco's achievement of the relevant objectives of its network code, as set under amended standard condition 9 of Transco's Gas Transporter (GT) licence.

In making this decision Ofgem has taken into account the obligations set out in Transco's GT licence, our wider statutory duties and all relevant facts.

We have set out below the reasons for our decision to direct Transco to implement modification proposal 0617.

Ofgem has also today published its decision on modification proposals 0616 '*Revision to the standard year for purposes of acquiring and holding monthly system entry capacity*' and modification proposal 0625, '*Short term six month auctions*'. Ofgem has directed Transco to implement modification proposal 0616, but has rejected modification proposal 0625. The reasons for these decisions are set out in separate letters.

Background to the proposal

System Entry Capacity Auctions

Transco has allocated monthly system entry capacity (MSEC) rights to access the national transmission system (NTS) via six monthly entry capacity auctions since September 1999. The most recent MSEC auctions were held in February 2003 and covered a period from 1 April 2003 to 30 September 2003. Transco also releases firm and interruptible capacity on a daily basis where there is additional capacity available. In addition, in the event that expected flows exceed both the capability of the system at an entry point and the amount of capacity held by shippers at that terminal, Transco is able to scale back interruptible capacity and to the extent necessary buy back firm entry rights at market determined prices.

Following Ofgem's approval of modification 0500, '*Long-Term Capacity Allocation*', Transco also makes available quarterly system entry capacity (QSEC) rights to access the NTS up to 15 years ahead of use. The first long-term auction for the sale of QSEC from 2004 to 2017 was held in January 2003.

Following the implementation of modification 0500, Transco has an obligation to issue annual invitations for MSEC and QSEC auctions not earlier than 1 August and not later than 31 August in each gas year¹.

The next series of long-term auctions is currently scheduled to occur in August 2003 for the period October 2005 to September 2018. The first annual monthly system entry capacity (AMSEC) auction is scheduled for August 2003 for the period October 2003 to September 2005. Both the AMSEC and the long-term auctions are currently operated on the basis of capacity years which are aligned with the traditional gas year and defined as the period from 1 October in any year until and including 30 September in the following year.

As such, the arrangements are not aligned with Transco's price control formula year which is the period from 1 April in any year until and including 31 March in the following year.

Related modification proposals

¹ The first long-term auction was held in January 2003 for the purposes of allowing shippers time to prepare to bid in the auctions, following the final implementation of modification 0500 in September 2002.

Separate to this proposal BGT has also raised modification proposal 0616, '*Revision to the Standard Year for purposes of acquiring and holding Annual Monthly System Entry Capacity*'. This proposal provides that the AMSEC auctions are held in February of each year from 2004. During these auctions Transco would offer capacity for the period April (Y) to March (Y+1). The proposal also contains interim arrangements whereby a further six monthly MSEC auction would occur in August 2003 in order to offer capacity for the period October 2003 to March 2004.

In addition, Shell Gas Direct has raised modification proposal 0625, '*Short term six month auctions*' which provides that the AMSEC auctions are held every six months, namely in February for April to September capacity and in August for October to March capacity with long-term auctions held in September each year.

The proposal

BGT has proposed a revision to the timing of the LTSEC allocation process with these auctions occurring in September of each year. Under the proposal the auctions would offer capacity for the period April (Y+2) to March (Y+16) thereby aligning the capacity year with the Transco price control year.

Respondents' views

The majority of respondents supported this proposal, although one respondent offered qualified support.

September auctions

Several respondents supported the idea of holding the auctions in September as opposed to the July and August holiday period. However, one respondent giving qualified support suggested that whilst it was in support of long-term auctions occurring in September, it would prefer that the capacity year be aligned with the gas year of October to September.

One respondent who was against the proposal suggested that it would support moving the auctions to September but did not believe it was necessary to change the start date from which capacity is made available.

Alignment of capacity year with the formula year

The majority of respondents supported the idea of aligning the capacity year with the formula year. A number of respondents considered that the proposal would place them in a better position because there would be more time between the monthly and long-term auction processes to allow shippers to assess their bidding strategies. One respondent considered that this would improve the

efficiency of the auctions and would aid Transco in the overall efficient operation of the transportation system. Another respondent stated that it supported the principle of shortening the period between the long-term auction date and the actual use of the capacity product.

Some respondents stated that the proposal would provide for a baseline capacity volume consistent for each year of the MSEC process.

One respondent stated that it did not support the proposal as it would remove the alignment between capacity years and most consumer and upstream contracts. Another stated that it was not necessary to change the point from which capacity is made available from October to April as under the long-term auction regime shippers will simply buy the capacity for the quarters of capacity that they require.

Transco's views

Transco supported this proposal.

September auctions

Transco considered that although holding the auctions in September (and allocating capacity by November) would reduce the time it had to produce its Ten Year Statement, there would be very few other system implications from this modification.

Alignment of capacity year with formula year

Transco acknowledged respondents' support for this proposal. It considered that the alignment may provide shippers with more time to consider the outcome of the MSEC auctions and would remove the step change in baseline quantities, as exists under the current arrangements. Transco also acknowledged that the proposal would meet the preference expressed at industry meetings for the long-term capacity allocation to be held outside of the July and August holiday period.

Transco stated that, given its recommendation regarding the implementation of modification proposal 0616, it would be inappropriate to introduce a change in the capacity year for one auction type (ie AMSEC) while leaving the arrangements for another auction type.

Transco stated that a possible disadvantage of the proposal is that it may minimise the time period between the allocation and the production of Transco's 10 year statement.

Transco also noted that the proposal would require only minor systems changes.

Ofgem's views

Ofgem recognises the strong preference expressed by shippers that the long-term auctions be held outside of the July-August holiday window. This modification proposal addresses concerns raised by shippers about managing the auction process during the summer vacation season. To the extent that a September auction will enable shippers to better manage their participation in the long-term allocation process, this proposal should better facilitate competition.

Ofgem also agrees with respondents that a September long-term allocation will benefit auction participants by providing some additional time between the AMSEC and long-term entry capacity auctions.

Ofgem notes that the majority of respondents have not raised concerns regarding the alignment of the capacity year with the Transco price control formula year for the purposes of the long-term auctions. Ofgem considers that there are few implications associated with aligning the capacity and price control years for the long-term entry capacity auctions and therefore considers that when taken as a whole, the proposal better facilitates competition between shippers.

Ofgem's decision

Ofgem has carefully considered the issues raised by this modification proposal. Ofgem considers that by improving shippers' ability to determine their bidding strategies in both the long and short-term auctions this modification should better facilitate competition between relevant shippers and suppliers.

Accordingly, Ofgem has directed Transco to implement modification proposal 0617 as we consider that the proposal will better facilitate the achievement of the relevant objectives as outlined in amended standard condition 9 of Transco's GT licence. In particular the proposal will better facilitate the securing of effective competition between relevant shippers and between relevant suppliers.

If you require any further information in relation to this modification please feel free to contact me on the above number or Tolani Azeez on telephone 0207 901 7043.

Yours sincerely

A handwritten signature in black ink, appearing to be 'M. Khan' or similar, written in a cursive style.

Mark Feather
Head of Gas Trading Arrangements