

# 0517B:

Review of the Supply Matching Merit Order in Setting Capacity Charges, Rolling Average to Reduce Volatility in Annual Charges



Proposer: Jeff Chandler SSE

Panel Date: January 15 2015

# Why change?



- Exit & Entry Capacity costs arising from the change to the Merit Order are reflected in charges in the year which they occur.
- However, the changes can be very large, up to 5,400%.
- Data provided by NG, show charges will be very volatile, up one year and down the next.

<http://www.gasgovernance.co.uk/sites/default/files/Exit%20Data.pdf>

- This makes business planning and passing through of costs on a reflective basis to customers difficult. Affects competition.
- The volatility of charges affects user commitment obligation which makes investment sign off more challenging. Affects competition.

# Options



- Change merit order and implement in the following October and March – 0517 approach
- To introduce a notice period between changing the Merit Order and changing charges to address unintended consequences - 0517A approach
- Change merit order, calculate charge, calculate average of 3 years of charges and apply the average to the current charging year – 0517B approach

# Solution



- To reduce volatility in charges it is proposed to calculate and use the rolling average of three years of charges to set charges for the current charging year.
- For clarity, the methodology introduced by mod 517 will be used to calculate the annual tariffs in this alternative.
- By way of example, to set the actual charges for 2015/16; the average of the historic charges from 2013/14 and 2014/15 and those forecast for 2015/16, as calculated by the charging methodology, will be added together and then divided by three to create an arithmetic average.
- This calculation will be carried out on a rolling average basis for future years as:

$$\text{Applicable Charge year } Y = (\text{Charge year } Y + \text{Charge year } Y-1 + \text{Charge year } Y-2) / 3$$

# Recommended Steps



- The Proposer recommends that this modification should be:
- Not subject to self-governance because it is likely to impact commercial activities connected with the shipping, transportation or supply of gas conveyed through pipes
- Sent for Workgroup assessment to develop the modification along with alternatives 517 and 517A and report to the panel once the workgroup report has been developed.