TRANSCO NETWORK CODE MODIFICATION PROPOSAL No. 0013(0740)

"Amendment to Transco's rights to interrupt for supply / demand purposes"
Version 2.0

Date: 10/06/2005

Proposed Implementation Date: 01/10/2005

Urgency: Non-Urgent

Justification

In May 2004, Shell Gas Direct raised Modification Proposal 0699, "Amendment to Transco's interruption rights for supply / demand purposes. Following workstream discussions, Transco raised an alternative proposal, 0705, "Changing the basis for supply demand interruption". This proposal was rejected by Ofgem in December 2004.

Having considered Ofgem's decision on 0705, Shell Gas Direct continues to be of the view that amendments to Transco's rights should be made.

At present, Transco can interrupt supply points as a capacity management tool, to match supply and demand in peak conditions and for testing purposes.

The level of interruption required for transportation constraints relates to the level of investment in the network. Ofgem introduced an incentive on Transco to minimize interruption for this purpose and requires Transco to make payments to Users based on 1/15th of the relevant annual NTS Exit and LDZ capacity charges for each day of interruption at an interruptible supply point in excess of 15 days during a 12 month period.

Transco has previously suggested that there is an incentive on Shippers to wait for Transco to initiate supply and demand interruption and proposes that greater use of the market should be used to balance supply and demand. While the proposer of this modification does not necessarily accept Transco's argument, it would appropriate to ensure that Transco does not over-rely on interruption to balance supply and demand and instead is encouraged to use the market as much as possible. As Transco can interrupt when demand is above the 85% threshold, it could be argued that shippers will not make sufficient arrangements to ensure that they are in balance during peak demand.

Ofgem's cash out review document suggested a need to consider whether it is appropriate that Transco uses interruption contracts for supply-demand balancing, and if so whether these costs should feed through into the cash out price. SGD understands that this is now being discussed through the cash out review group. This proposal should not conflict with those discussions but rather provide an efficient approach to providing the correct signals to the market, including customers who may be willing to interrupt, and ensure that Transco's incentives to balance are not distorted by the option to interrupt for supply / demand at no cost. Ofgem notes the current arrangements do not prevent Transco from accessing demand side response. This proposal should incentivise Transco to fully consider all options.

This proposal will not conflict with a view that the OCM is the most efficient and economic method of fulfilling its role as residual balancer. Transco has expressed concern that there may be insufficient offers on the day. This proposal should incentivise Transco to find innovative ways of ensuring that offers for demand-side interruption are available from consumers (through shippers) in these circumstances. Contracting ahead will ensure that there will be sufficient availability that is "operationally suitable". Ofgem's decision on M705 states that Transco can use bilateral contracts via shippers to facilitate this. Ofgem has also stated separately that Transco can enter into bilateral contracts direct with consumers for "turn down" which we understand to be an energy product, not capacity and therefore not subject to Gas Act restrictions. We consider that focussing on using the OCM for supply/demand balancing with demand-side contracts will ensure that any interruption properly feeds into cash out without the necessity of complex new arrangements. However, it is for Transco to develop any arrangements it considers necessary and if proposed arrangements are not through the OCM, we would expect these to be discussed through the cash out review group.

Reducing the supposed incentive on shippers to wait for Transco to interrupt and any reliance that Transco may have on using interruptions for supply and demand purposes, should encourage shippers to enter into contracts which allow for commercial interruption in times of peak demand. These can, where appropriate, be backed up by contracts between shippers and Transco to provide this gas through the OCM.

Nature of Proposal

This Modification Proposal seeks to amend the current 85% limit to 95% from October 2005 with a further amendment to 100% from April 2006. We consider this approach to be appropriate as it would give sufficient time for consumers, shipper/suppliers and Transco to adjust to the change but recognizes that there is a risk that some may not be in a position to make changes for the forthcoming winter by the time this proposal is approved. By restricting further Transco's right to interrupt at lower demand levels, Transco will need to go to the market through the OCM or advance contracting if it believes this is necessary to ensure supply and demand balancing at the system level. By relying on the market, Transco will be properly incentivised to minimize its costs and price signals will be sent to shippers and thence to consumers about the value of their flexibility. We have kept 100% of peak demand as a prudent measure to ensure security of supply. However, this does not mean it is necessary for security of supply and we recommend that if this proposal is implemented, its performance should be reviewed after a couple of Gas Years and then consideration be given to complete removal of rights to supply/demand interruption . We understand that some may consider "95%" to be arbitrary but the same can be said of "85%"; we advocate this as being a prudent step towards more efficient operation of the pipe-line system.

Purpose of Proposal

To ensure that Transco is properly incentivised to use market mechanisms as much as possible and to provide market signals to suppliers and consumers about the value of flexibility in times of high demand. If shippers are relying on Transco to institute interruption for supply/demand purposes, this should reduce reliance. Instead, shippers would be incentivised to balance their own portfolios, reducing the requirement for Transco to take actions (including interruptions). This will promote efficiency in Transco's operation of the system. Competition between shippers will be promoted by ensuring that they compete to provide flexibility in times of high demand.

Consequence of not making this change

Under prevailing balancing regime arrangements primary Supply and Demand balancing is the responsibility of User, with Transco's role being described by some as "residual balancer". Interruption is one of the tools available to Shippers to undertake their primary role. This modification may increase the value of commercial interruption thereby incentivising consumers to enter into such arrangements removing any current distortionary effects. Ofgem has separate stated that it believes that more commercial interruption can help resolve emergencies and this modification, by encouraging commercial interruption , should therefore improve security of supply.

Area of Network Code Concerned

Section G

Proposer's Representative

Tanya Morrison (Shell Gas Direct Ltd)

Proposer

Tanya Morrison (Shell Gas Direct Ltd)

Signature

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