Draft Modification Report
Implementation of DNPC03 (LDZ System Charges – Capacity / Commodity Split and Interruptible Discounts), the Alignment of Failure to Interrupt Charges and the Alignment of the IFA Charge
Modification Reference Number 0210
Version 1.0

This Draft Modification Report is made pursuant to Rule 9.1 of the Modification Rules and follows the format required under Rule 9.4.

1 The Modification Proposal

In February 2006 Ofgem published their document "Conclusions on the review of the structure of gas distribution charges". One of the conclusions of this document was that increasing the proportion of capacity related charges would better reflect the actual balance of capacity and commodity related costs of gas distribution. Ofgem also suggested that more cost-reflective charges could have a significant impact on the efficient use of the Distribution assets and help reduce future investment costs. These savings would eventually be reflected in lower charges to all customers. A higher proportion of capacity related charges would also bring additional benefits to users in the form of more stable charges.

A consultation paper on behalf of all Gas Distribution Networks (GDNs) ('*LDZ System Charges - Capacity / Commodity Split and Interruptible Discounts',)* known as DNPC03, was issued in July 2007. Following on from consultation the GDNs put forward a proposal to modify their charging methodologies with effect from 1st October 2008. Ofgem issued a Draft Impact Assessment in October 2007 and issued a final version, in conjunction with their decision letter, in December 2007; Ofgem decided not to veto the proposal.

This UNC Modification Proposal has been raised as a result of the Ofgem decision which allows the GDNs to "amend their charging methodologies with effect from 1 October 2008 so that:

- The proportion of revenue collected from the Use of System capacity charges increases from 50% to 95%, while the proportion collected from Use of System commodity charges decreases from 50% to 5%.
- Interruptible supply points pay capacity charges equal to 47.37% of those paid by an equivalent firm connection, so maintaining the existing value of capacity charge discounts received by these supply points".

The proportion of revenue collected from the Use of System capacity charges and commodity charges are not set out in the UNC and the majority of DNPC03 will be implemented through changes to the individual GDN's Transportation Charging Statement. However, the UNC currently states that in respect of an Interruptible Supply Point the Registered User shall not be required to pay NTS Exit Capacity Charges or LDZ Capacity Charges (UNC Transition Document Part IIC 9.1.9(a)). The intention of this UNC Modification Proposal is to remove the part of this exemption that relates to LDZ Capacity Charges. For clarity, the Registered User would still not pay NTS Exit Capacity Charges.

An unintended consequence of the change to the charging methodologies will be to increase the first day Failure to Interrupt (FTI) charge by 90%. For the first day of failure, the FTI charge is currently charged at two times the Applicable Annual Rate of the **Firm** LDZ Capacity Charge (UNC Transition Document Part IIC 9.9.2(a)(i)).

With the change in Capacity from 50% to 95%, the first day FTI charge would rise by 90% if no further change were made. The GDN's preferred solution to this, and the intent of this Proposal is to amend the first day FTI charge to be two times the difference between the Applicable Annual Rate (as introduced by DNPC03 at 1st October 2008) and the Firm Applicable Annual Rate; this will maintain the current level of the first day FTI charge.

In a similar way the change to the charging methodologies will also impact on the 'IFA Charge' (charges payable, by the Registered User, to the DN Operator and National Grid NTS where a relevant Supply Point has an Interruptible Supply Point Firm Allowance). The IFA Charge, payable to the DN Operator, is currently based on the Firm LDZ Capacity Charge and is supplementary to the LDZ System Charges (UNC Transition Document Part IIC 10.4).

With the change in Capacity from 50% to 95%, and the introduction of the interruption LDZ Capacity Charge, the IFA Charge will increase by approximately 53%.

We are therefore proposing that the IFA Charge payable to the DN Operator as a single charge in October of each year (not National Grid NTS) is calculated as equivalent Firm LDZ Capacity Charge, based on the Firm Allowance, (using it as the SOQ of the firm element), less any capacity payments expected over the subsequent 12 months made in respect of the Firm Allowance and paid as interruptible LDZ Capacity Charge, (resulting from the implementation of DNPC03 on 1st October 2008).

There is also an incorrect reference to 10.5.3 within UNC Transition Document Part IIC 10.4.2. This should refer to 10.4.3 and will also be amended by implementation of this Modification Proposal.

For clarification this proposal will have no impact on the following:

- Arrangements for interruptible sites directly connected to the National Transmission System
- The charge rate for subsequent days where a FTI charge is due
- IFA Charge payable to National Grid NTS
- Ratchet Charges (interruptible sites can not attract such charges under the current, transitional, arrangements)
- The basis for calculating the applicable LDZ Capacity and Commodity Charge rates (i.e. the usage of Bottom Stop SOQ for interruptible sites)

Interruption arrangements as of 1st October 2011 (commencement of revised DN Interruption Arrangements (Mod 0090))

Suggested Text

To be provided separately for the Consultation Phase.

2 Extent to which implementation of the proposed modification would better

facilitate the relevant objectives

Standard Special Condition A11.1 (a): the efficient and economic operation of the pipe-line system to which this licence relates;

By facilitating the implementation of DNPC03 and maintaining the current level of failure to interrupt charges this Modification Proposal may be expected to facilitate this relevant objective and help to ensure the efficient and economic operation of the pipe-line system

Standard Special Condition A11.1 (b): so far as is consistent with sub-paragraph (a), the coordinated, efficient and economic operation of

(i) the combined pipe-line system, and/ or

(ii) the pipe-line system of one or more other relevant gas transporters;

Implementation would not be expected to better facilitate this relevant objective.

Standard Special Condition A11.1 (c): so far as is consistent with sub-paragraphs (a) and (b), the efficient discharge of the licensee's obligations under this licence;

Implementation of this Proposal will allow the change to the GDN's charging methodology to be implemented on 1st October 2008 and therefore be consistent with SSC A5, this in turn would therefore better facilitate this relevant objective.

Standard Special Condition A11.1 (d): so far as is consistent with sub-paragraphs (a) to (c) the securing of effective competition:

(i) between relevant shippers;

(ii) between relevant suppliers; and/or

(iii)between DN operators (who have entered into transportation arrangements with other relevant gas transporters) and relevant shippers;

Implementation of appropriate charging methodologies will help to ensure that there is no inappropriate discrimination between different market sectors and that, in this instance, charges to interruptible sites remain cost reflective and Users are not in receipt of inappropriate 'discounts' or subject to inappropriate failure and IFA charges. We therefore believe that implementation of this Modification Proposal is likely to better facilitate this relevant objective.

Standard Special Condition A11.1 (e): so far as is consistent with sub-paragraphs (a) to (d), the provision of reasonable economic incentives for relevant suppliers to secure that the domestic customer supply security standards… are satisfied as respects the availability of gas to their domestic customers;

Implementation would not be expected to better facilitate this relevant objective.

Standard Special Condition A11.1 (f): so far as is consistent with sub-paragraphs (a) to (e), the promotion of efficiency in the implementation and administration of the network code and/or the uniform network code;

Implementation of this Proposal will ensure that any further changes to the LDZ capacity and commodity proportions will not require a UNC Modification Proposal to re-align the first day FTI charge or the IFA Charge. We therefore believe that implementation of this Modification Proposal will better facilitate this relevant objective by the promotion of efficiency in the administration of the UNC.

3 The implications of implementing the Modification Proposal on security of supply, operation of the Total System and industry fragmentation

No implications on security of supply, operation of the Total System or industry fragmentation have been identified.

4 The implications for Transporters and each Transporter of implementing the Modification Proposal, including:

a) Implications for operation of the System:

No implications for operation of the system have been identified.

b) Development and capital cost and operating cost implications:

There are no development and capital cost or operating cost implications associated with implementation of this Proposal.

c) Extent to which it is appropriate to recover the costs, and proposal for the most appropriate way to recover the costs:

No cost recovery mechanism is proposed.

d) Analysis of the consequences (if any) this proposal would have on price regulation:

No such consequences on price regulation have been identified.

5 The consequence of implementing the Modification Proposal on the level of contractual risk of each Transporter under the Code as modified by the Modification Proposal

No such consequences on contract risk have been identified.

6 The high level indication of the areas of the UK Link System likely to be affected, together with the development implications and other implications for the UK Link Systems and related computer systems of each Transporter and Users

There are no development, or other, implications for Transporter or Users systems

7 The implications of implementing the Modification Proposal for Users, including administrative and operational costs and level of contractual risk

Administrative and operational implications (including impact upon manual processes and procedures)

No such implications have been identified.

Development and capital cost and operating cost implications

No such implications have been identified.

Consequence for the level of contractual risk of Users

Without implementation of this Modification Proposal the level of charge associated with the first day of a failure to interrupt, and any applicable IFA Charge, will increase by 90% and 53% respectively; thus increasing the contractual risk of Users.

8 The implications of implementing the Modification Proposal for Terminal Operators, Consumers, Connected System Operators, Suppliers, producers and, any Non Code Party

No such implications have been identified for any other relevant persons.

9 Consequences on the legislative and regulatory obligations and contractual relationships of each Transporter and each User and Non Code Party of implementing the Modification Proposal

As a Gas Distribution Network (GDN) we are obliged to keep our charging methodology under review to ensure that the objectives of the charging methodology are being achieved further to Standard Special Condition (SSC) A5 (2A)(a) of the gas transporters' licence. The pricing consultation DNPC03 resulted in a proposed modification to the GDN's charging methodologies, Ofgem decided not to veto that proposal. Implementation of this Modification Proposal will allow the GDNs to successfully implement the change to the charging methodology and be consistent with SSC A5

10 Analysis of any advantages or disadvantages of implementation of the Modification Proposal

Advantages

Allows implementation of DNPC03

Ensures Failure to Interrupt charges remain, unchanged, at the appropriate level

Ensures IFA Charges, payable to DN Operators are at the appropriate level

Disadvantages

No Disadvantages have been identified

11 Summary of representations received (to the extent that the import of those representations are not reflected elsewhere in the Modification Report)

Written Representations are now sought in respect of this Draft Report.

12 The extent to which the implementation is required to enable each Transporter to facilitate compliance with safety or other legislation

Implementation is not required to enable each Transporter to facilitate compliance with safety or other legislation.

13 The extent to which the implementation is required having regard to any proposed change in the methodology established under paragraph 5 of Condition A4 or the statement furnished by each Transporter under paragraph 1 of Condition 4 of the Transporter's Licence

Implementation is not required having regard to any proposed change in the methodology established under paragraph 5 of Condition A4 or the statement furnished by each Transporter under paragraph 1 of Condition 4 of the Transporter's Licence.

14 Programme for works required as a consequence of implementing the Modification Proposal

No programme of works would be required as a consequence of implementing the Modification Proposal.

15 Proposed implementation timetable (including timetable for any necessary information systems changes and detailing any potentially retrospective impacts)

This Modification Proposal will need to be implemented on the 1st October 2008 in order to be consistent with the publication of each of the GDN’s Transportation Charging Statement

16 Implications of implementing this Modification Proposal upon existing Code Standards of Service

No implications of implementing this Modification Proposal upon existing Code Standards of Service have been identified.

17 Recommendation regarding implementation of this Modification Proposal and the number of votes of the Modification Panel

18 Transporter's Proposal

19 Text

Representations are now sought in respect of this Draft Report and prior to the Transporters finalising the Report.

For and on behalf of the Relevant Gas Transporters:

Tim Davis
Chief Executive, Joint Office of Gas Transporters