Stage 02: Workgroup Report

What stage is this document in the process?

01 Proposal

02 Workgroup Report

03 Draft Modification Report

04 Final Modification Report

0404:

Profiling payment of LDZ capacity transportation charges for Small Shipper Organisations.

There is a view that some smaller Shipper organisations are experiencing cash flow issues as a result of the mis-alignment between their income and the transportation charges levied by DNs. This modification proposes that Shippers meeting certain criteria are permitted to profile the payment of certain charges more in line with their income.

The Workgroup recommends that this modification should now proceed to Consultation

High Impact:
Smaller Shippers

Medium Impact:
Distribution Networks.

Low Impact:
Insert name(s) of impact

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About this document:

The purpose of this report is make a recommendation to the Panel, to be held on 15 March 2012, on whether Modification 0404 is sufficiently developed to proceed to consultation and to submit any further recommendations in respect of the definition and assessment of this modification.

Any questions?

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1 Summary

Is this a Self-Governance Modification

The Modification Panel determined that this is not a self-governance modification.

Why Change?

Some Workgroup members hold a view that some smaller Shipper organisations are experiencing cash flow issues as a result of the mis-alignment between their income and the transportation charges levied by DNs. This modification proposes that Shippers meeting certain criteria are permitted to profile the payment of certain charges more in line with their income.

Solution

It is proposed that, subject to meeting specific criteria, smaller Shippers be will be offered the option to profile their payment of LDZ transportation charges, such that a greater proportion is paid in the winter months and less will be paid in the summer months, although the charges levied will remain the same and all invoiced charges must be paid in full to the DN (including any relevant interest and administration charges) by the end of the relevant financial year.

Impacts & Costs

No Xoserve systems' impacts are anticipated to be necessary to support this modification. There would be no change to LDZ transportation invoices, however Shippers that met the criteria and elected to profile payments would not be required to pay the full amount of invoices during the summer months, but would be required to pay all outstanding amounts during the winter months and in any event pay in full within the relevant financial year. Transporters would be required to monitor the unpaid amounts to ensure that the correct amounts were re-paid by the stipulated payment dates (detailed in this modification) and would not invoke the current arrangements available to the DN (detailed in UNC TPD Section S 3.5.3 and V 4.3) where the Shipper adhered in full to the rules specified in this modification.

Implementation

Some Workgroup members agree that this modification proposal should be implemented in time to allow small Shippers the option to profile transportation payments for financial year 2012/13. See section 6 for detail on dates.

The Case for Change

Implementation may facilitate competition by helping to ensure small Shipper's revenue and costs are more closely aligned, reducing the possibility of gas being shipped / supplied at a loss during the summer months and addressing a cashflow issue which can act as a barrier to market entry and a barrier to business development for smaller Shipper / Suppliers.

Recommendations

The Workgroup considers that the modification is sufficiently developed and should now proceed to consultation.

2 Why Change?

The present LDZ charging arrangements are primarily based on capacity bookings, which are largely fixed throughout the year. In the case of domestic Shippers, transportation charges are based on SOQs derived from the AQ, which is set for a year. By contrast, Shipper and Supplier revenue is driven by the amount of gas consumed, which is higher in winter than in summer.

The mismatch between the profiles of Shipper / Supplier revenue and transportation charges potentially makes the sale of gas a loss making activity during the summer months for certain Shipper / Suppliers. While this may not create particular difficulties for Shippers and Suppliers with large, diverse portfolios, or those with a low cost of capital, a significant cashflow issue may be created for some smaller Shipper / Supplier organisations. The issue may be particularly acute for smaller Shipper / Suppliers with a primarily domestic customer base or portfolios with a large number of pre-payment meters. The mismatch therefore may create an inappropriate barrier to market entry and business development and change is potentially needed to encourage greater competition within the domestic market.

Some Workgroup members were concerned that there is very little evidence to suggest there is a need for these arrangements.

3 Solution

It is proposed that Shippers which meet certain criteria be permitted to profile the payment of Distribution Network Capacity transportation invoices across a year, with the intention of paying in full all outstanding amounts by the end of March in each financial year.

The intention is for the facility to profile payments to be available to smaller Shippers only, and to be restricted to those who supply the SSP market. It is therefore proposed that only Shippers supplying less than 100,000 Smaller Supply Points nationally and where the individual Shipper's Code Credit Limit is less than £500,000, (also less than £500,000 where multiple Shipper licences are owned by the same organisation) would be eligible to take advantage of the option to profile payments. The following business rules would apply:-

1. Shippers meeting the following criteria would be permitted to participate in the summer / winter profiling payment process:-

   (a) Shippers with less than or equal to 100,000 Smaller Supply Points across all Distribution Networks, and

   (b) where Shippers meet the criteria in 1 (a), who also have an organisational Code Credit Limit (as defined in UNC TPD Section V 3.2.1 (a)) of less than £500,000 recorded with the Distribution Network they wish to profile Summer / Winter payments with; and

   (c) where Shippers meet the criteria in 1 (a) & (b) and the Shipper's maximum Value at Risk in the three months preceding May of the relevant year was less than the Shipper's Code Credit Limit.

2. For the months May, June, July and August each year a qualifying Shipper may pay a minimum of 50% of the LDZ Capacity invoice for the Smaller Supply Point element of the invoice for that month. (ZCA & CCA charge types).

3. Qualifying Shippers would re-pay outstanding amounts owing to the relevant DN (resulting from the adoption of business rule 2) from the May, June, July and August LDZ Capacity invoices over the months of October, November, December, January, February and March of the same financial year (adhering to the timeline detailed below)

4. The payment of outstanding amounts by the Qualifying Shipper would be in line with the following schedule:

   (i) The total outstanding amount from the May, June, July and August LDZ Capacity Invoice (resulting from the adoption of business rule 2 by the Qualifying Shipper) would be paid on the basis of one sixth of the total outstanding amount (as of 31st August) to be paid by the end of October, November, December, January, February and March of the same financial year.

   (ii) Were a qualifying Shipper to opt to pay more than one sixth of the total outstanding amount (as of 31st August) in any one month October to March they would be permitted to do so.

5. For the avoidance of doubt, interest on any outstanding amounts would continue to be applied by the Transporter in line with existing provisions detailed in UNC TPD Section S 3.6.

6. All payments made by the qualifying Shipper in relation to the outstanding amount would be offset against the earliest occurring outstanding amount for the purposes of interest calculation and VAT payment purposes. Shippers would be required to clarify their VAT payments in relation to the outstanding amounts.

7. For the avoidance of doubt obligations set out in UNC TPD Section V3 "Code Credit Limits" or UNC TPD Section V4 "Discontinuing Users and Termination" would not be altered by this Modification Proposal.

8. For the avoidance of doubt provisions detailed in UNC TPD Section S3.5.3 relating to unpaid amounts would not be altered by this Modification Proposal. However, where Shippers adhere in full to the repayment timescales associated with summer invoice deferment the DN would not invoke these options for the non payment of these amounts only.

4 Relevant Objectives

Implementation will better facilitate the achievement of **Relevant Objective d.**

Proposer's view of the benefits against the Code Relevant Objectives	
Description of Relevant Objective	No
a) Efficient and economic operation of the pipe-line system.	No
b) 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.	No
c) Efficient discharge of the licensee's obligations.	No
d) 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.	Yes (d i and ii)
e) 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.	No
f) Promotion of efficiency in the implementation and administration of the Code	No
g) Compliance with the Regulation and any relevant legally binding decisions of the European Commission and/or the Agency for the Co-operation of Energy Regulators	No

Some Workgroup members consider Relevant objective d (i) and (ii) (Securing of effective competition between relevant Shippers and relevant Suppliers) may be better facilitated by the implementation of this modification. By allowing qualifying small Shipper organisations to more closely align their Distribution Network transportation costs to their income, this would improve their cash flow situation. Improving cash flow for small Shippers would remove a deterrent to expand their businesses, encouraging organisations to take on increased numbers of small supply points and offering more innovative tariff structures. However, some Workgroup members consider that this modification will create a perverse incentive by encouraging smaller shippers to remain within the qualification levels and therefore prevent competition.

Some workgroup members were concerned that there is a lack of analysis and evidence to back up the statement that this arrangement is wanted or needed by Shippers in order to test that the relevant objective is met.

Workgroup members understand that the current arrangements may make supply to small supply points in the summer a loss making activity for all organisations in this sector. However, this modification aims to introduce measures, which may prevent this being a deterrent to new market entrants and to supply point acquisition in this area of the market.

5 Impacts and Costs

Consideration of Wider Industry Impacts

None identified.

Costs

Indicative industry costs – User Pays
Classification of the proposal as User Pays or not and justification for classification
Not user pays. It is not envisaged there would be any Transporter central systems' changes.
Identification of Users, proposed split of the recovery between Gas Transporters and Users for User Pays costs and justification
Not applicable
Proposed charge(s) for application of Users Pays charges to Shippers
Not applicable
Proposed charge for inclusion in ACS – to be completed upon receipt of cost estimate from Xoserve
Not applicable

Impacts

Impact on Transporters' Systems and Process	
Transporters' System/Process	Potential impact
UK Link	• None
Operational Processes	• There would be an increased cost associated with the monitoring and administration of transportation invoices and credit arrangements.
User Pays implications	• None

Impact on Users	
Area of Users' business	Potential impact
Administrative and operational	• There would be an increased cost associated with the monitoring and administration of transportation invoices.

Insert heading here

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Impact on Users	
Development, capital and operating costs	• None
Contractual risks	• None
Legislative, regulatory and contractual obligations and relationships	• None

Impact on Transporters	
Area of Transporters' business	Potential impact
System operation	• None
Development, capital and operating costs	• Additional operating costs would be incurred by the Distribution Networks in monitoring the profiled payments by participating Shippers.
Recovery of costs	• None
Price regulation	• None
Contractual risks	• Increased contractual risk associated with the potential for increased bad debt. A maximum exposure of approx. £1.5m per annum was identified by the DNOs.
Legislative, regulatory and contractual obligations and relationships	• None
Standards of service	• None

Impact on Code Administration	
Area of Code Administration	Potential impact
Modification Rules	• None
UNC Committees	• None
General administration	• None

Impact on Code	
Code section	Potential impact
Legal text to be provided.	• UNC TPD Section S

Where can I find details of the UNC Standards of Service?

In the Revised FMR for Transco's Network Code Modification **0565 Transco Proposal for Revision of Network Code Standards of Service** at the following location: www.gasgovernance.co.uk/sites/default/files/0565.zip

Impact on UNC Related Documents and Other Referenced Documents	
Related Document	Potential impact
Network Entry Agreement (TPD I1.3)	• None
Network Exit Agreement (Including Connected System Exit Points) (TPD J1.5.4)	• None
Storage Connection Agreement (TPD R1.3.1)	• None
UK Link Manual (TPD U1.4)	• None
Network Code Operations Reporting Manual (TPD V12)	• None
Network Code Validation Rules (TPD V12)	• None
ECQ Methodology (TPD V12)	• None
Measurement Error Notification Guidelines (TPD V12)	• None
Energy Balancing Credit Rules (TPD X2.1)	• None
Uniform Network Code Standards of Service (Various)	• None

Impact on Core Industry Documents and other documents	
Document	Potential impact
Safety Case or other document under Gas Safety (Management) Regulations	• None
Gas Transporter Licence	• None

Other Impacts	
Item impacted	Potential impact
Security of Supply	• None
Operation of the Total System	• None
Industry fragmentation	• None
Terminal operators, consumers, connected system operators, suppliers, producers and other non code parties	• None

6 Implementation

To facilitate the option of profiling the payment of LDZ Transportation charges in financial year 2012/13 this modification proposal would require the following implementation timescale:

1. Fixed Implementation Dates of 1st May 2012 or 1st June 2012.
2. A Proposed Authority Decision Date by 30th April 2012 to allow an implementation date of 1st May 2012 or a decision date by 31st May 2012 to provide for an implementation date of 1st June 2012.
3. A backstop lead time of 1 month.

The first invoice available for summer/winter profiling would be the May 2012 LDZ Capacity invoice which will have an invoice due date of circa 20th June 2012. To allow the DNs to put in place procedures to monitor and track payments and also to discuss with qualifying Shippers their intentions regarding deferment of transportation charges, the preferred implementation date would be 1st May 2012. An implementation date of 1st June 2012 would still facilitate the option of deferring payment; however this would not be ideal for DNs for the reasons stated.

7 The Case for Change

None in addition to that identified above.

8 Legal Text

The Workgroup was not provided legal Text for assessment; therefore it recommends that Legal Text be provided for consultation.

9 Recommendation

The Workgroup invites the Panel to:

- AGREE that Modification 0404 be submitted for consultation.