

MODIFICATION PROPOSAL

Short Title: An Auction of Rough Services 1998/9
Date: 26th February 1998
Proposed Implementation: Immediately
Status: Urgent

JUSTIFICATION

So far the only detailed auction modification the industry has had to comment on has been put forward by BG Storage. BG Storage has made it clear that it prefers Rough services to be sold with fixed prices. We believe there is merit in putting forward an alternative modification to create an auction of Rough services. This proposal differs from that put forward by BG Storage in a number of respects. It proposes that: -

- the auction process is kept simple with a Firm service only sold with 30 days' duration (as opposed to between 30 and 120 days in BG Storage's draft modification);
- the Firm service has priority over all other services;
- the remaining space is auctioned as an Interruptible service with 50 days' duration;
- the Interruptible service has priority over all other services except firm;
- BG Storage is required to post excess (unused and available) storage capacity, i.e. deliverability, injection etc., on AT Link on a daily basis;
- BG Storage sells daily available capacity to the highest bidder and should not be restricted in its ability to offer services that optimise the use of Rough capacity;
- accepting BG Storage's concern about protecting its income, a levy is allowed to protect BG Storage against any under-recovery but it also proposes that any over-recovery is rebated back across the industry;
- any under- or over-recovery is charged/rebated at the end of the year;

CONSEQUENCE OF NOT MAKING THIS CHANGE

An opportunity to make optimum use of Rough facilities would be lost. Top-up storage may remain. The market value of storage remains hidden or distorted.

AREA OF NETWORK CODE CONCERNED

Sections R and F.

NATURE OF PROPOSAL

Auction

To offer a Firm, 30-day withdrawal, 50-day injection service and an Interruptible service (with 50-day withdrawal rights) through an auction. The auction rules could include a

reserve price, provided it was deemed necessary to avoid accusations of predatory pricing, and the reserve price was only to cover of the order of £30 million in operating costs. Deliverability would be allocated in order of price bid, highest first. All successful tenderers would pay the Clearing Price i.e. the lowest price of any successful bid (or, if all the deliverability were not allocated, the reserve price). The firm service would have priority over all other services with 2 hours' notice. We understand, from the first public meeting, that maintaining a 2 hour lead time for both withdrawal and injection would cost around £0.5 million – spread across a billion therms this is of the same order as a rounding error. The interruptible service would have priority over all other services except firm.

Tertiary Services

BG Storage would offer tertiary services on a daily basis by posting excess (unused and available) storage capacity, i.e. deliverability, injection etc., on AT-Link. BG Storage would sell to the highest bidder and would not be restricted in its ability to offer services that would maximise usage of the Rough facility.

Flexibility Bids

Shippers would be able to place flexibility bids using all services. Shippers would decide for themselves the risks of being curtailed by higher priority users and exposing themselves to SMP.

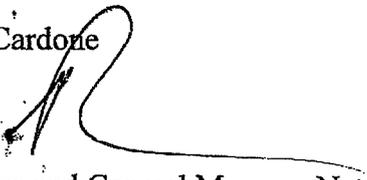
Dealing with under- or over- recovery

At the end of the year, BG Storage's actual income for the year, comprising revenues from the auction, revenues acquired through selling unused capacity on a day-to-day basis and last year's over-recovery would be compared to the "allowed" revenue under the price control. Any difference between this actual income and the "allowed" revenue for Rough storage would be recovered or rebated through Balancing Neutrality at the end of the year. Given BG Storage's protected status we cannot see the justification for their proposed monthly recovery mechanism.

PURPOSE OF PROPOSAL

To make all Rough deliverability available, to eliminate the need for Top-up and to discover the free market value of storage.

PROPOSER: Gary Cardone

SIGNATURE: 

POSITION: Director and General Manager Natural Gas

COMPANY: NGC UK LIMITED

Modification No 0218
Date Received 3/3/98 (Revised mod)