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Transco, shippers and other interested parties

Our Ref: net/cod/mod/448
Direct Dial: 020 7901 7327
Email: steve.smith@ofgem.gov.uk

Dear Colleague,

Modification 448 'Removal of Output Unauthorised Gas Flow Charges from the Network Code'

Ofgem has carefully considered the issues raised in modification proposal 448 *'Removal of Output Unauthorised Gas Flow Charges from the Network Code'* and has decided to direct Transco to implement the modification because we believe that it better facilitates the relevant objectives of Transco's Network Code.

Ofgem expects that the modification will be implemented from 1 October 2001. In this letter, we explain the background to the modification proposal, the nature of the proposal and give our reasons for making this decision.

Background

Unauthorised Gas Flows (UGF) charges have been part of the gas balancing regime since the inception of the Network Code in March 1996. The charges were originally put in place to provide shippers with commercial incentives to make nominations at entry and exit points on Transco's AT-Link system, thus providing information to Transco for the purpose of producing accurate system scheduling and Non Daily Metered (NDM) demand forecasts.

A failure on the part of a shipper to provide such nominations could result in that shipper facing
UGF charges at System Marginal Price (SMP). The shipper could, however, avoid UGF charges by entering a nomination of zero against the relevant activity on AT-Link. If a company ships gas to a large number of entry and exit points this can be administratively burdensome for a shipper. In the event that a shipper fails to enter a zero nomination by mistake it would face UGF charges which could be very expensive. These errors are more likely with respect to exit UGFs as a shipper's portfolio will typically contain many more exit than entry points.

In 1998, in response to shippers avoiding UGF charges by entering zeros against the relevant activity, Transco raised a modification proposal to remove Input UGF charges, namely Modification proposal 0232 '*Removal of Input UGF at Sub-terminals'*.
Ofgas approved Modification 232 in September 1998. As a result of this modification, Transco entered zeroes at all *entry* sub-terminals for all shippers. Given that entry terminals are relatively few in number, this was a simple exercise for Transco. Exit UGF charges, however, remained in the code and the view taken at the time of Modification 232 was that their removal from the Network Code should be the subject of future discussion. Progress in removing exit UGF charges, however, has been slow and thus such charges have remained in the Network Code to date.

Exit UGF charges arise only if a shipper fails to insert a nomination on AT Link for a daily-metered exit point. Such charges are calculated by multiplying the quantity of the volume of gas off-taken without a corresponding AT-Link nomination (of any description) having been made by the SMP. In addition, system-scheduling charges apply as normal. These charges are applied when the quantity of gas delivered to or off-taken at an exit point differs by more than an allowed tolerance (as defined in Section F of the Network Code) from the quantities nominated by the shipper in respect of that exit point. The volume of gas flows outside this tolerance level is subject to a scheduling charge of 1% of system average price.

If a shipper had entered a zero nomination but a gas flow measurement had nonetheless occurred, the shipper would be subject to scheduling charges only, not exit UGF charges.

In December 2000, British Gas Trading proposed Modification Proposal 448 – *Removal of Output Unauthorised Gas Flow Charges from the Network Code*.

Original modification proposal

This modification proposed that Transco enters zeroes on its IT systems for all shippers for all exit points where no nomination currently exists (as it currently does at entry sub terminals).

Respondents' views

This proposal received nine responses. Eight expressed support, whilst one was against.

One respondent who had expressed support for BGT's proposal pointed out the administrative burden for shippers to enter zero nominations and that UGF charges were penal costs for what was ultimately an administrative error. Another respondent supported BGT's proposal in principle providing that the AT Link system remained robust.

Another respondent supported immediate implementation of BGT's proposal because it considered that Transco's alternative proposal could take time to implement. It indicated its hope that Transco develop a more efficient solution by removing the charge at a more fundamental level and improving systems efficiency by reducing the amount of data entry necessary.

One respondent commented that it was in favour of BGT's proposal because it had been frustrated by the delay in removing exit UGF charges. The same respondent noted, however, a potential alternative Transco approach, and hoped that Transco would be able to clarify the impact of the BGT proposal on the timing and implementation of this alternative approach as well as the nature of the alternative approach itself.

The respondent not in favour of BGT's modification proposal stated that the reason for this was that it was awaiting an alternative solution from Transco that would not only remove exit UGF charges but which would also ensure that there was no deterioration in the scheduling regime.

Transco's views

Transco agrees that the insertion of a zero, as opposed to a blank entry, provides no added information to Transco. However Transco considered that BGT's proposed solution for the removal of exit UGF charges could lead to possible deterioration in scheduling performance.

Transco indicated that at the Energy and Capacity Workstreams in January 2000 and February 2000, it had presented several options for simultaneously removing exit UGF charges and improving the scheduling regime but received no support for any of these options. Transco argued that this had contributed to the delay in resolving the issue of exit UGF charges.

Transco also agreed that for shippers to insert zeroes can be burdensome, particularly if they have a large number of exit points. However, Transco has also stated that the efficient operation of its computer systems could not be guaranteed as BGT's proposal might generate a large volume of unnecessary data.

Transco also believes that because of the large number of exit points, an 'entry-type' solution involving insertion of zero input nominations would be an inefficient way of removing exit UGF charges.

Transco has identified the potential impact of BGT's solution of inserting zero nominations on existing Network Code rules and that specific default allocation rules, particularly those concerning CSEPs, might become inapplicable. A similar problem could occur with the insertion of zeroes at entry sub-terminals but thus far no problems had been reported.

Transco shared BGT's concern for a prompt resolution to the issue of exit UGF charges. However, Transco indicated its wish to ensure that any potential solution is efficient, does not lead to a deterioration in the scheduling regime, and does not create any anomalies in the Network Code.

Transco stated that whilst it supported the underlying aim of the modification it wanted to explore alternative methods that would achieve the same result but in a manner that would also better facilitate the relevant objectives.

Transco's preferred solution

Transco wrote to shippers on 15 June 2001 and sought agreement for the removal of exit UGF charges but using an alternative method. Transco's alternative proposal was to remove exit UGF charges via BGT's modification proposal by entering/deeming zero nominations at exit points where a measurement had been made but no nomination had existed, and this would be done at the end of the gas day.

The contrast with BGT's proposal is that BGT had proposed that Transco enter '*zeroes for all shippers at all activity numbers on AT Link*' without a nomination, regardless of whether there had been a subsequent gas flow measurement.

Transco has indicated that its alternative solution would ensure that processes involving shipper User Daily Quantity Outputs such as scheduling charges and imbalance cash-out would be carried out correctly.

Transco has indicated to Ofgem that BGT would be prepared to see exit UGF charges suppressed in the manner suggested by Transco's alternative.

Respondents views on Transco's alternative solution

There were five responses to this alternative proposal. All were in favour, including the respondent who had voted against BGT's original modification proposal.

None of the respondents made any substantive comments other than an indication of support for Transco's alternative proposal.

Ofgem's views

Ofgem recognises that accurate shipper nominations can play an important role in providing information to Transco that assists it in its role as residual gas balancer. In particular accurate nominations at entry and exit assist Transco in determining likely gas flows and whether, as a result, the system will remain within safe operating pressure limits over the day. This, in turn, determines whether Transco needs to take balancing actions over the day.

However, Ofgem agrees with respondents that exit output UGF charges do not appear to provide any incentive to provide any additional information to Transco over and above the incentives provided by the scheduling charges. This is because shippers can simply avoid the charge by entering a zero. The exit output UGF charge does, however, arguably place a potentially costly administrative burden upon shippers, particularly those with a large number of exit meters.

Transco has not presented any arguments in its response that demonstrate that the incentives provided by this charge leads to any better information flows to Transco. Ofgem can therefore only conclude that Transco does not believe that the current incentives provide shippers with additional incentives, over and above the incentives provided by scheduling charges, to provide accurate nominations information that would assist Transco in balancing the system efficiently.

In the light of respondents' support for Transco's alternative solution, Ofgem accepts that it is preferable to the original proposal as it will ensure that there is no impact on the calculation of scheduling charges or imbalance cash-out. Ofgem is however disappointed that it has taken until now for Transco to address the issue of exit output UGF charges.

Ofgem therefore believes that Transco's alternative proposal would better facilitate the relevant objectives of the Network Code set out in Standard Condition 7 of Transco's licence. In particular, Ofgem believes that it will better facilitate the economic and efficient operation of the pipeline system. The modification will prevent shippers having to face an unnecessary additional administrative burden associated with responding to a commercial incentive that does not improve the incentive on shippers to provide more accurate nomination information to Transco.

Ofgem's decision

Ofgem has decided to direct Transco to implement this modification using the alternative method suggested by Transco.

We believe that this would better facilitate the relevant objectives outlined in Standard Condition 7 of Transco's Gas Transporter's licence. In particular, we believe that this modification will better facilitate the objective of ensuring the efficient and economic operation of the National Transmission System.

Ofgem expects Transco to implement this modification from 1 October 2001.

If you have any queries in relation to the issues raised in this letter, please feel free to contact me on the number above.

Yours sincerely

Steve Smith
Director, Trading Arrangements