

TRANSCO NETWORK CODE MODIFICATION PROPOSAL No. 0573

"Further revisions to system entry capacity overrun charges"
Version 2.0

Date: 07/08/2002

Proposed Implementation Date: 01/10/2002

Urgency: Non-Urgent

Justification

The overrun charge is applied to users who flow gas in excess of their capacity holding over the Gas Day. The current overrun regime was introduced in 1999 as part of the RGTA capacity reforms and has subsequently been reviewed and changed in the light of experience under the new regime. There has been considerable debate about whether the current level of overrun charges are appropriate.

Overrun charges are designed to provide an incentive on shippers to pre-book capacity (the so-called "ticket to ride" principle). Overrun charges should ensure that shippers who flow in excess of booked capacity are exposed to the costs they impose on Transco and other users (through capacity neutrality). Transco can incur significant costs if Transco has to use capacity management tools as a result of shippers overrunning.

The current overrun charge is too high and in achieving this objective the charge significantly and artificially raises the risks that shippers face in booking and trading capacity. The eight times multiple is arbitrary and does not reflect the costs to Transco and/or users associated with the overrun. The use of a smaller multiple of market prices is more cost-reflective whilst maintaining the incentive to pre-book capacity. The multiple will also maintain a strong incentive on shippers not to overrun at constrained system entry points.

The overrun regime may affect shippers' valuations of monthly system entry capacity. Any proposed change to the level of overrun charges needs to be decided upon before the next set of MSEC auctions commence. The proposal therefore justifies urgent status so that shippers have certainty ahead of the next set of auctions.

Nature of Proposal

The current entry capacity overrun charges should be amended to remove the eight times multiple of monthly auction prices from the calculation and replaced with a multiple of 1.1 times the monthly auction prices. The other elements of the overrun calculation should remain unchanged.

Purpose of Proposal

This modification would better facilitate the relevant objectives by ensuring more efficient utilisation and operation of the pipeline system. By increasing incentives to trade and decreasing incentives to hoard capacity, it will lower capacity management and trading costs and prices.

The modification will also better facilitate competition between shippers and suppliers by making it easier to bring gas to market through the creation of a more liquid secondary capacity market.

Consequence of not making this change

Maintaining the current level of overrun charges will stifle capacity trading and liquidity in secondary markets. It will also continue to artificially raise the risk to shippers associated with trading capacity. This will lead to higher prices associated with capacity in secondary markets. This will also raise the cost of capacity management to Transco. Customers will ultimately face these additional costs.

Increased risk will reduce the willingness to shippers to trade capacity. This could encourage capacity hoarding to manage this risk. As it is not possible to design a fully effective use-it-or-lose-it regime, this could prevent gas reaching the market and competition to supply gas to the market.

Area of Network Code Concerned

Section B

Proposer's Representative

Stephen Charles Smith

Proposer

Aep Energy Services Ltd

Signature

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