

Modification Report
Provision of information relating to the SO commodity charge
Modification Reference Number 0576

Version 1.0

This Modification Report is made pursuant to Rule 8.9 of the Modification Rules and follows the format required under Rule 8.9.3.

1. The Modification Proposal

"The Proposal is to enable shippers and customers to manage the risks associated with volatility in the level of the SO commodity charge, Transco should be obliged to publish sufficient information to allow shippers and customers to forecast the level of charges based on the outturn costs relative to forecast costs used when setting the SO commodity charge.

Transco sets the SO commodity charge at the start of the charging year by as the sum of all of the target level of costs under its SO incentive schemes. It is AEP's understanding that the current SO commodity charge is calculated by first summing the target level of costs for: SO internal costs; SO system balancing incentives; and the NTS exit capacity incentive. The target levels of costs are set out in Ofgem's December 2001 document "Transco NTS SO Incentives 2002-7: Final Proposals" document. Transco then subtracts its estimate of revenue it will receive over the year from users paying the SO optional commodity tariff and the St Fergus compression charge to determine target cost recovery.

This target level of cost recovery is then divided by Transco's forecast of system throughput for the year to determine the SO commodity charge.

Transco should therefore be obliged to publish:

- Transco's forecast of annual system throughput and monthly system throughput for the next charging year at the start of each charging year;
- actual system throughput on a weekly basis;
- Transco's forecast of annual and monthly target costs under the relevant SO incentive schemes (system balancing, SO internal costs and exit capacity) at the start of the charging year;
- the sum of outturn costs under the relevant SO incentive schemes (system balancing, SO internal costs and exit capacity) on a weekly basis; and
- disaggregated outturn costs for each of the relevant SO incentive schemes (system balancing, SO internal costs and exit capacity) on a quarterly basis.

Transco should be required to publish all of the information listed at the frequencies indicated on the Transco Information Exchange at <http://info.transco.uk.com/>

2. Transco's Opinion

Transco does not support implementation of this Modification Proposal and does not believe that publishing the requested information would significantly increase Users' ability to accurately predict the path of the SO Commodity Charge. In addition, Transco would emphasise that the majority of the requested information is not available.

The Proposal does not accurately describe either Transco's obligations nor its approach to setting the SO Commodity Charge. Transco is aware of concerns about the potential volatility of transportation charges in general and the SO Commodity Charge in particular. Transco does not set charges for a charging year but, consistent with its Licence obligations, seeks to make adjustments to charges only when it is clear that to do so otherwise would lead to collected revenue exceeding the maximum allowed revenue calculated in accordance with the relevant price control formula. As would be expected, Transco also sets charges with a view to collecting the revenue allowed by each price control formula. But when doing this, Transco considers more than one year in the interests of achieving price stability within the obligations set out in its Gas Transporters Licence.

Following Ofgem's decision to veto the proposal to introduce a TO Commodity Charge (PC75), Transco intends to consult on options for setting transportation charges in future. This will provide an opportunity for all interested parties to contribute to consideration of the potential benefits of increased certainty regarding the future level of transportation charges and, if it is concluded that this is desirable, the means by which it might be delivered.

In respect of this Modification Proposal, Transco would point out that, in respect of the requested information:

- Throughput information is already published on a daily basis;
- Targets under the relevant SO incentive schemes were set by Ofgem on the basis of a formula year, and a monthly split of the target is not available; and
- The sum of outturn costs under the relevant SO incentive schemes are not produced on a weekly or quarterly basis and hence are not available. For example, SO internal costs include recharges from a number of Transco departments, and these are not available on a weekly basis. Exit capacity costs are also a significant part of the requested costs which, rather than accruing on a daily basis, are calculated on the basis of a snapshot at one point in time.

Transco therefore considers that the implementation of the proposal would generate substantial requirements for systems, business process changes and cumulative within year estimates of target (which are currently not available) and actual performance that are currently not available. Given the very limited, if any, benefits that might accrue to Users, Transco therefore does not recommend implementation of the proposal.

3. Extent to which the proposed modification would better facilitate the relevant objectives

The proposer suggests that implementing this Modification Proposal will better facilitate competition between shippers and suppliers.

4. The implications for Transco of implementing the Modification Proposal, including

a) implications for the operation of the System:

No direct implications are anticipated.

b) development and capital cost and operating cost implications:

Changes to Transco's existing systems would be required to facilitate the provision of this information resulting in estimated development costs of the order of £100k. Some additional operating costs due directly to the information release would also be expected.

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

Any additional System Operator costs incurred as a result of implementing this proposal would be accounted for under the proposed internal cost incentive scheme, as set out in Ofgem's final proposals for the System Operator incentives, and hence be largely recovered from Users.

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

The proposal is not considered to have any consequences in respect of price regulation.

5. The consequence of implementing the Modification Proposal on the level of contractual risk to Transco under the Network Code as modified by the Modification Proposal

No such consequences are anticipated.

6. The development implications and other implications for computer systems of Transco and related computer systems of Users

Changes to Transco systems are required to facilitate the provision of this information.

7. The implications of implementing the Modification Proposal for Users

Users would be provided with information that might allow them to better forecast changes to the level of the SO Commodity charge.

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

Non-Network Code Party

Transco believes that there would be no direct effect on the above parties.

9. Consequences on the legislative and regulatory obligations and contractual relationships of Transco and each User and Non-Network Code Party of implementing the Modification Proposal

No changes to contractual relationships are anticipated.

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

Advantages:

- The provision of information might improve the ability of Users to predict more accurately SO commodity charge levels.

Disadvantages

- Increased administrative complexity and operating costs for Transco
- Much of the requested information is not available as specified in the Modification Proposal and hence the published information could be regarded as misleading.

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

Seven representations were received:

British Gas Trading Ltd. (BGT)
TotalFinaElf Gas & Power Ltd. (TFE)
Shell Gas Direct (Shell)
SSE Energy Supply Ltd. (SSE)
AEP Energy Services (AEP)
LE Group (LE)
TXU Europe Energy (TXU)

Five respondents (BGT, TFE, SSE, AEP, LE) support the proposal.

One respondent (TXU) supports the proposal in the absence of a Transco alternative

One respondent (Shell) does not support the proposal.

1. Risk

TXU, AEP and LE commented that provision of information, allowing Users to form an opinion on the likely direction and magnitude of movement in the SO commodity charges, would allow them to better manage risk. If a method of managing risk is not introduced then it is likely that such risk will be factored into end consumer prices. It was argued that the ability to better forecast SO commodity charges would better facilitate competition between shippers and suppliers.

Transco Response

Transco accept that increased certainty regarding future charge levels is of potential benefit. However, Transco believes that providing the information sought in this proposal would not necessarily increase certainty. In practice Transco expects to continue to make only occasional changes to the level of the SO Commodity Charge, and will follow the required notice periods. In addition, following Ofgem's decision to veto the proposal to introduce a TO Commodity Charge (PC75), Transco proposes to consult on options for setting transportation charges in future. This will provide an opportunity for all interested parties to contribute to consideration of the potential benefits of increased certainty regarding the future level of transportation charges and, if it is concluded that this is desirable, the means by which it may be delivered.

2. Monitoring of Transco Performance

SSE assume that Transco will be putting into place mechanisms to track and monitor its performance under the SO incentive schemes in order that it might comply with its licence obligations.

Transco Response

In terms of complying with Licence obligations, Transco would emphasise that its obligation is, when setting charges, to use best endeavours to ensure that it does recover more revenue than permitted by the relevant price control formula within a given formula year.

3. Data Provision

SSE suggest that three groups of data could be provided on a cumulative and weekly basis;

- Forecast system throughput vs actual and the forecast outturn for the year;
- Forecast performance under each component of the SO incentive scheme vs actual and the forecast outturn for the year; and
- Actual revenue received from SO commodity charges vs forecast and the forecast outturn.

Transcos Response

While noting SSEs views on potential information which might be released, Transco would observe that, in accordance with Modification Rules, the Proposal should be considered for implementation in the form in which it was raised rather than being developed.

4. Weekly Reporting

AEP suggest that if data is not available on a weekly basis then the best available

estimates could be published and reconciled to actual data as it becomes available. BGT suggest that there is scope for regular reporting but potentially not as described within the mod.

Transcos Response

Transco accepts that it would be possible to provide estimates as described, but is not clear why such estimated data, which may only be confirmed after the end of a formula year, would be helpful in projecting the likely level of the SO Commodity Charge while Transco continues its present approach of avoiding frequent changes to the level of charges.

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

Transco does not believe that implementation of this Modification Proposal would affect 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 Standard Condition 4(5) or the statement furnished by Transco under Standard Condition 4(1) of the Licence

Not applicable.

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

A programme of works would need to be developed should the Modification Proposal be implemented.

15. Proposed implementation timetable (including timetable for any necessary information systems changes)

Transco does not propose implementation.

16. Recommendation concerning the implementation of the Modification Proposal

Transco's view is that the proposal should not be implemented.

17. Restrictive Trade Practices Act

If implemented this proposal will constitute an amendment to the Network Code. Accordingly the proposal is subject to the Suspense Clause set out in the attached Annex.

18. Transco's Proposal

This Modification Report contains Transco's proposal not to modify the Network Code and Transco now seeks agreement from the Gas & Electricity Markets Authority in accordance with this report.

19. Text

Signed for and on behalf of Transco.

Signature:

Tim Davis
Head of Regulation NT&T

Date: