

Direct Dial: 020-7932-5927

21 July 2000

BG Transco, Shippers and Other Interested Parties

Your Ref:

Our Ref: Net/Cod/Mod/0408

Dear Colleague,

**Modification Proposal 0408 ' Review of Entry Overrun Charges'**

Ofgem has considered the issues raised in Modification Proposal 0408: 'Review of Entry Overrun Charges'. Ofgem has decided to direct BG Transco to implement the modification, because we believe that this proposal will better facilitate the relevant objectives of BG Transco's Network Code.

In this letter, we explain the background to the modification proposal and give the reasons for making our decision.

**Background to the proposal**

In September 1999 Transco conducted the first auctions for the sale of entry capacity to its National Transmission System ('NTS'). The auctions provided for the allocation of monthly system entry capacity to successful bidders for a total period of 6 months from 1 October 1999 to 31 March 2000. A second series of auctions was held in March 2000. In addition to holding monthly auctions, Transco makes additional entry firm and interruptible capacity available on a day-ahead basis and conducts day-ahead capacity buy backs where necessary. A within day capacity market became operational on 1 June 2000.

A key element of the new capacity regime is the overrun regime. The overrun regime provides an incentive to encourage market participants to book entry capacity prior to nominating and flowing gas, thereby helping to ensure entry rights are firm.

The overrun charge currently paid by shippers is set as the maximum of:

- ◆ 1.1 times the highest offer price accepted day-ahead in the daily entry capacity auction;
- ◆ 1.1 times the highest offer price accepted day-ahead in the daily buy-back market; and
- ◆ 8 times the daily rate for monthly system entry capacity (based on the weighted average price (WAP) of the top 50% of bids, determined in the monthly auction);

and the lower of:

- ◆ 1.5 times the daily SAP; or
- ◆ maximum overrun of charge of 0.6054 p/kWh.

### **The modification proposal**

This proposal considers changes to the overrun regime. It is hoped that this proposal will discourage the hoarding of surplus capacity and improve liquidity in the secondary capacity market.

The proposed changes to the calculation of the overrun charge include:

- ◆ removing the energy component of the overrun charge on days when BG Transco has not scaled back all interruptible capacity and bought-back firm capacity; and
- ◆ linking the components linked to the day ahead sales and buy back market to prices generated by the within-day capacity mechanism.

Following respondents views, BG Transco has proposed that the overrun charge on all days be set equal to the higher of:

- ◆ 1.1\* the weighted average price of the top 25% accepted bid prices for daily capacity;
- ◆ 1.1\* the highest accepted offer price to sell capacity to BG Transco; and
- ◆ 8\*the weighted average top 25% of bids accepted in the monthly auction.

However, BG Transco has system functionality problems that means the first clause cannot be able to be calculated until 1December 2000. As a result, for the months October to November 2000, the overrun charge will be calculated as:

- ◆ 1.1\* the highest accepted bid prices for daily capacity;
- ◆ 1.1\* the highest accepted offer price to sell capacity to BG Transco; and
- ◆ 8\*the weighted average top 25% of bids accepted in the monthly auction.

### **Respondents' views/Ofgem's views**

Respondents' views and Ofgem's views on this modification have been outlined in detail in chapter 7 of the "New gas trading arrangements: A review of the new arrangements and further development of the regime. A review and decision document" issued 21 July.

### **Ofgem's Decision**

We have decided to consent to this modification, as we believe that it better facilitates the achievement of the relevant objectives as outlined under Standard Condition 7 of BG Transco's Public Gas Transporter's licence.

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

Yours sincerely,

Steve Smith  
**Director, Trading Arrangements**