

Draft Modification Report
Structure of the NTS SO Commodity Charge
Modification Reference Number 0626

Version 1.0

This Draft Modification Report is made pursuant to Rule 7.3 of the Modification Rules and follows the format required under Rule 8.9.3.

1. The Modification Proposal

It is proposed that the NTS SO Commodity Charge, which is currently calculated by applying the NTS SO Commodity Charge rate to daily offtake quantities, be calculated by applying a revised NTS SO Commodity Charge rate to both daily input and offtake quantities.

The NTS SO Commodity Charge for each User would be the sum of the NTS Entry Commodity Charge and the NTS Exit Commodity Charge; where

NTS Entry Commodity Charge = NTS Entry allocated quantities x NTS Commodity Charge Rate

NTS Exit Commodity Charge = NTS Exit allocated quantities x NTS Commodity Charge Rate.

The proposed charges would, with the exception of Storage Connection Points, apply to all NTS exit and entry points. Consistent with the PC73 methodology, it is anticipated that a common commodity charge rate will be applied to both Entry and Exit allocated quantities.

In respect of Storage Connection Points, it is proposed that there should be no change to the existing approach such that an NTS Commodity Charge would apply solely to exit flows associated with Own-Use Gas consumed at the respective Storage Facility. It is intended that the extension of the NTS SO Commodity Charge to other flows associated with Storage Connection Points would be determined subsequently to satisfy the requirements of the PC70 Pricing Methodology.

2. Transco's Opinion

Pricing Consultation PC73 "Structure of the NTS SO Commodity Charge" proposed that the NTS SO Commodity Charge would be applied to all gas entering the gas transportation system at System Entry Points, as well as to gas exiting the gas transportation system at System Exit Points, with effect from 1 October 2003. Following Ofgem's decision on 30 July 2002 not to veto PC73, the charging methodology proposed in PC73 will become effective from 1 October 2003, should this Proposal be implemented.

Transco proposes a pragmatic approach to the implementation of the charging methodology proposed in PC73 but recognises that there are other related issues which may subsequently need to be considered. The Proposal specifically excludes application of the revised charges to storage flows as envisaged in PC70 "NTS System Operation Transportation Charges". Transco considers that, in light of Ofgem's decision letter in respect of Modification Proposal 0532 "Application of SO Commodity Charges to all NTS loads", it is unlikely that the issue of NTS commodity charging to Storage Connection Points can be resolved sufficiently quickly to facilitate implementation within the timescales envisaged in PC73.

Transco is also of the view that the impact of applying the NTS SO Commodity Charge to entry flows on

the level of SO Commodity Charge is far greater than the impact of including storage flows. In a note to the Network Code Modification Panel, Transco indicated that, whilst the application of the NTS SO Commodity Charge to entry flows would be likely to reduce the NTS SO Commodity Charge rate by approximately 50%, the application to the Storage Connection Point flows would be likely to have less than a 2% further impact. Transco has therefore prioritised implementation of the charges which are likely to have the greatest impact.

Transco concludes that this Proposal should be implemented so that the NTS SO Commodity Charge applies to entry flows from 1 October 2003, with the issue of SO Commodity Charges to storage flows to be resolved as soon as reasonably practical thereafter.

In parallel with the developments on the structure of the NTS SO Commodity Charge, the issue of recovery of the NTS TO Revenue has been considered in the Pricing Discussion Paper PD17 "Setting of the NTS Transportation Charges". The Transco Discussion Report on PD17 will be produced shortly.

Should the Proposal be implemented, the NTS SO Commodity Charge revenues would be recovered by the application of charges to both entry flows and exit flows such that approximately half of the revenue is recovered from entry flows and approximately half from exit flows. The NTS Optional Commodity Rate would, however, continue to be applied in respect of System Points electing the optional NTS commodity tariff; such System Points would continue to attract the NTS Optional Commodity Rate but would not attract the new NTS Entry Commodity Charge in respect of relevant inputs at the local System Entry Point. Transco believes that levying the NTS Entry Commodity Charge, in addition to applying the NTS Optional Commodity Rate, is not consistent with the principle underlying the introduction of the NTS Optional Commodity Rate; the optional NTS commodity tariff is intended to provide economic incentives for Users to use the NTS rather than build dedicated pipelines bypassing the NTS.

The Proposal, if implemented, would result in an amendment to the Commodity Charge invoicing. The 'NTS Commodity Charges' would consist of 'NTS Entry Commodity Charges', 'NTS Exit Commodity Charges' and 'NTS Optional Commodity Charges'. A key issue is the availability of data to permit timely billing of the charges; exit quantities are available after D+5 whereas entry quantities are not available until after M+15. An objective of the invoicing process is to optimise delays in billing, taking account of the system and administrative workload associated with the billing process. Transco has considered a number of options which vary from submission of the charges immediately after close-out of UDQOs and carrying out appropriate adjustments after close-out of UDQIs to the submission of all charges after close-out of UDQIs. Transco has concluded that any processes involving estimations and subsequent adjustments would generate unwarranted complexity in the billing and subsequent reconciliation process. Therefore, Transco advocates that the NTS Exit Commodity Charges are invoiced, as soon as reasonably practical, after close-out of UDQOs, the NTS Entry Commodity Charges after close-out of UDQIs, and the NTS Optional Commodity Charges, which require validation against UDQIs, after close-out of UDQIs. Whilst this option would result in delayed invoicing for recovery of approximately half of the NTS SO Commodity Charge revenues (a loss of around £200k per annum to Transco through loss of interest), Transco considers that this is the preferred option.

Transco therefore recommends implementation of the Proposal.

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

Implementation of the Proposal would enable implementation of charges in accordance with the methodology established by PC73. This methodology was established on the grounds of improved cost-reflectivity and is consistent with the objectives in Standard Condition 4(5)(a) of Transco's GT Licence i.e. the development of a Transportation Charging Methodology that reflect the costs incurred by Transco in its transportation business. Implementation of the Proposal would therefore better facilitate the relevant objective of efficient discharge of Transco's obligations under its licence, as stated in paragraph 1 of Standard Condition 9.

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

a) implications for the operation of the System:

It is not considered that implementation of the Proposal would have any material impact on the operation of the system.

b) development and capital cost and operating cost implications:

Transco would incur additional costs in the development, maintenance and administration of the billing systems and processes. The optional NTS commodity tariff would remain unchanged; the systems would ensure that, where NTS SO Optional Commodity Rate is applicable, Users would not pay the normal NTS SO Commodity Charge associated with relevant inputs at the local terminal. Separate invoices would be submitted for NTS Entry Commodity Charges (new invoice), NTS Exit Commodity Charges (amendment to the current Commodity Invoice), and for charges based on the NTS Optional Commodity Rate (new invoice). The amended Commodity Invoice would be submitted on M+8 (as is currently the case) and the new invoices would be submitted on M+18. Indicative system development costs for invoicing (around £150k) and modifications to the off line systems (around £50k) suggest that the total system implementation costs are around £200k.

Transco currently submits the Commodity Invoice, which includes NTS Transportation Charges, on M+8. Since nearly half of the NTS Transportation Charges would be submitted via the NTS Entry Commodity Invoice on M+18, Transco would incur loss of interest due to delayed submission of the NTS Entry Commodity Invoice. The annual loss of interest from the reduced cashflows is estimated at approximately £200k. There would also be a modest impact of delayed invoicing and earlier collection of adjustment amounts associated with the optional NTS commodity tariffs, resulting in the net impact being negligible.

Introduction of an NTS Entry Commodity Charge might be expected to increase NBP gas prices, and hence gas purchases at NBP for Shrinkage and Operating Margins purposes might adversely impact Transco's performance under the gas cost incentive.

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 costs associated with increased operating costs and system development would be covered under the internal costs incentive.

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

No consequences are envisaged on 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 consequences are envisaged on the level of contractual risk to Transco.

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

Transco currently submits the Commodity Invoice at M+8. The invoice includes both the NTS Commodity Charges based on the 'standard' Applicable Commodity Rate and where the charges are based on the NTS Optional Commodity Rate. Any adjustments as a consequence of applying the 'eligibility criterion' for the NTS Optional Commodity Rate are made later.

The Proposal, if implemented, would lead to an amendment to the Commodity Invoice such that it would only include the NTS Exit Commodity Charges; the charges arising from application of the NTS Optional Commodity Rate would be excluded. There would be no change to the timing of the submission of the amended invoice.

The NTS Entry Commodity Charges would be submitted via a new invoice (NTS Entry Commodity Invoice) on M+18.

With regard to the charges based on the NTS Optional Commodity Rate, a new invoice (NTS Optional Commodity Invoice) would be submitted, also on M+18. Submission of the NTS Optional Commodity Invoice after close-out of UDQIs would ensure that the 'eligibility criterion' could be applied after close-out of entry allocations, and would remove the need to make any adjustments later as is currently the case.

Amendment to the current Commodity Invoice would lead to a change in the invoicing file format, and the creation of the two new invoices would lead to two new file formats. Transco envisages that the IT systems of the Users might need to be amended to cater for these changes. Transco seeks views from respondents regarding implications for their computer systems.

7. The implications of implementing the Modification Proposal for Users

The recovery of NTS SO Commodity Charge revenues will be split between the Commodity Invoice (amended to include NTS Exit Commodity Charges) and an NTS Entry Commodity Invoice. Because of the differences in close-outs for entry and exit allocations, these invoices will be submitted separately. The amended Commodity Invoice will be issued on M+8 in the month following gas flow, as is currently the case, and the NTS Entry Commodity Invoice will be issued on around M+18 in the month following gas flow. The NTS Optional Commodity Invoice will also be submitted around the same time as the NTS Entry Commodity Invoice, and will include adjustment to the charges based on the NTS Optional Commodity Rate for any over charging on the NTS Entry Commodity Invoice.

Since most entry flows, which are currently exempt from any Commodity Charges, will attract the NTS Entry Commodity Charge, implementation of the Proposal could introduce extra uncertainty in the NBP gas prices and forward trading. Transco would welcome the views of respondents as to whether this uncertainty might have any implications in the context of the relevant objectives of the Network Code.

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

Transco is not aware of any implications of implementing the Proposal for 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

Transco is not aware of any such consequences.

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

Advantage:

- Achieves consistency with PC73;

Disadvantage:

- Requires two additional invoices and amendment to an existing one;
- May create extra uncertainty in respect of NBP gas prices, particularly for those trading forward at the NBP and expecting to deliver gas at the input to the system.

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

Representations are now sought for the Proposal.

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

This Proposal is not required to facilitate 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

Implementation of the Proposal is required to facilitate implementation of Pricing Consultation PC73.

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

The main activities in developing and modifying computer systems are:

- Business Requirements Approval
- System Design & Development
- System Testing

- User Acceptance Testing

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

Indicative timescales for system development and implementation are given below.

Activity	Completion Date
Business Requirements Approval	16/05/03
System Design & Development	18/08/03
System Testing	12/09/03
User Acceptance Testing	10/10/03
Implementation	01/11/03

16. Recommendation concerning the implementation of the Modification Proposal

Transco recommends implementation of the Proposal from 1 October 2003.

17. Text

SECTION B: SYSTEM USE AND CAPACITY

Amend title of paragraph 2.11 to,

“Entry Charges, NTS Entry Commodity Charges and Capacity Surrender Charges.”

Amend paragraph 2.11.1 to read,

“2.11.1

- (i) A User shall pay Capacity Charges (“**System Entry Capacity Charges**”) in respect of its Registered System Entry Capacity at Aggregate System Entry Points, and
- (ii) Commodity Charges (“**NTS Entry Commodity Charges**”), in respect of the flow of gas into the NTS on any day, or a charge calculated by reference to Special Condition [28B] of the Transco Licence.”

Renumber existing paragraph 2.11.6 as 2.11.7; Insert new paragraph 2.11.6,

“2.11.6 The NTS Entry Commodity Charge payable by a User in respect of each Day will be determined for each NTS Entry Point as the User Daily Quantity Input less any quantity to which the NTS Optional Commodity Rate applies in accordance with Code multiplied by the Applicable Commodity Rate for such Commodity Charge.”

Amend paragraph 2.11.7. to read,

“2.11.7. System Entry Capacity Charges, NTS Entry Commodity Charges and Capacity Surrender Charges.....”

Amend paragraph 3.5.1(ii) to read,

“3.5.1(ii) Commodity Charges (“NTS Exit Commodity Charges”)”

Amend paragraph 3.5.3 to read,

“3.5.3 The NTS Exit Commodity Charge payable (for any Day) by a User will be determined (for each NTS Exit Point) as”

Amend paragraph 3.5.4 to read,

“3.5.4 NTS Exit Capacity Charges and NTS Exit Commodity Charges will be invoiced...”

Amend paragraph 3.5.5 to read,

“3.5.5 “.....the Applicable commodity rate of NTS Exit Commodity Charge in respect of a ...”

“3.5.5(ii) “The NTS Exit Commodity Charge payable ...”

SECTION S : INVOICING AND PAYMENT

Amend Annex S-1, paragraph 4 to read:

“4. Commodity Invoice

A “Commodity Invoice” is an Invoice Document in respect of any or each of the following Invoice items:

- (a) (i) NTS Entry Commodity Charges;
- (ii) NTS Exit Commodity Charges; and
- (iii) NTS Optional Commodity Charges;
- (b)

Amend Annex S-1, paragraph 6(b) to read:

“6.

- (b) Reconciliation Transportation Charge Adjustment in respect of the NTS Exit Commodity Charge

Representations are now sought in respect of this Draft Report and prior to Transco finalising the Report

Signed for and on behalf of Transco.

Signature:

Nigel Sisman
Manager Commercial Development
NT & T

Date: