Draft Modification Report
Removal of 1/15th capacity charge credit when interruption is for supply and demand balancing purposes.
Modification Reference Number 0696

Version 1.0

This Draft 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

This Modification Proposal seeks to remove the payment of the 1/15th credit to Users of Interruptible Supply Points when Transco is required to call for Interruption to resolve a Supply deficit once it considers, having due regard to obligations placed on it by its Gas Transporters Licence, the market will no longer provide a physical response in an appropriate time period.

2. Transco's Opinion

The introduction in 2002 of the NTS SO incentive scheme brought about an incentive on Transco to minimise the level of Interruption that it calls as System Operator. This incentive is contained within the NTS Exit Capacity Investment Incentive (ECII) where Transco is exposed to a level of additional cost should any Supply Point Interruption exceed 15 days in a formula year. It is Transco's opinion that primary Supply & Demand balancing is the responsibility of Users and that Transco's role is as the residual system balancer. Transco's primary use of Interruption is, and should continue to be, as a capacity management tool and the ECII is consistent with this position. Under the existing ECII Transco makes payments to Users based on 1/15th of the relevant annual NTS Exit and LDZ capacity charges. The original intention of Modification 0555 - 'Interruptible Transportation Charges', that proposed the introduction of this 1/15th payment, was that it would only apply when Interruption was required for capacity management purposes.

In essence, Transco is incentivised to call Interruption to relieve capacity constraints in a prudent manner and, where Interruption costs could be efficiently avoided, provide additional system exit capacity to reduce the likelihood of such Interruption being called, i.e., invest to relieve capacity constraints where this would be efficient and economic. Transco can therefore mitigate the risk of excessive capacity management Interruption costs by investing in additional system capacity.

Since the introduction of the current ECII arrangements the tightening supply and demand position has generated a scenario where, in a severe winter, the volume of interruption required to maintain security of supply could be in excess of the volume of interruption required for capacity management purposes. Transco might, therefore, be required to initiate Interruption purely for supply and demand management purposes i.e. sufficient system capacity exists to meet the demand but there are insufficient available supplies. Transco cannot mitigate the risk of excessive supply and demand management interruption costs by investing in additional capacity, therefore Transco considers that this aspect of the ECII is inappropriate and should be removed bringing the incentive in-line with its original intent.

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

Transco's primary use of Interruption is, and in Transco's opinion should continue to be, as a capacity management tool. The ECII is consistent with this position. NT &T Workstream discussions held on the 4th April 2004 recognised that it is inappropriate to apply exit capacity investment incentives, when Interruption is for Supply and Demand management purposes, as Transco is unable to mitigate such exposure through developments in exit capacity. Transco therefore contends that applying such a credit for Interruption for Supply and Demand does not better facilitate the efficient and economic operation of the pipe-line system.

At the NT &T Workstream both Transco and User representatives expressed concern that the present Interruption incentive arrangements may represent a disincentive for Users and gas consumers to enter into non-Transco called interruption arrangements. Where the right to call for "commercial" interruption is not available to Users as part of their gas supply contract with the end consumer this could lead, under certain circumstances, to Transco having to call for such "commercial" supply and demand management interruption on behalf of the User thus acting in a primary balancing role.

By removing an incentive for Users and End Consumers to wait for Transco to initiate Supply and Demand Interruption this Modification Proposal seeks to facilitate greater competition between Users thereby encouraging greater utilisation of market mechanisms to respond to Supply and Demand mismatches. If implemented, this Proposal may also better facilitate the efficient and economic operation of the pipe-line system, in that greater use of the market to balance Supply and Demand may reduce the requirement for Transco, to Interrupt Supply Points for Supply and Demand purposes and as such reduce system balancing costs.

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

a) implications for the operation of the System:

Transco does not anticipate that the implementation of the Modification Proposal will result in any operational implications.

b) development and capital cost and operating cost implications:

Transco does not anticipate that any additional capital or operating cost implications will result from the implementation of this Proposal.

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:

Transco is not proposing to recover any development or capital costs arising from implementation of this Proposal.

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

Transco recognises that this Proposal, if implemented, requires a change to the Transportation Statement in respect of the proposed removal of the 1/15th Exit Capacity Investment Incentive Charge Credit, when Interruption is for Supply and Demand management purposes. Transco has raised a Pricing Consultation - PC81 - 'Interruptible Transportation Charging', the timetable of which is aligned

to this Proposal's timetable. It is anticipated that the alignment of both consultations will facilitate more efficient and complete responses to the changes proposed.

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

Transco is not aware of any such consequences.

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

If implemented, estimated costs for system changes to support the Modification Proposal will be approximately £11k.

Transco does not currently anticipate any system implications related to computer systems of Users.

7. The implications of implementing the Modification Proposal for Users

Users will no longer receive an Exit Capacity Investment Incentive Charge Credit when Interruption is for Supply and Demand management purposes.

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

End consumers, with an interruptible contract, will no longer receive an Exit Capacity Investment Incentive credit charge, when Interruption is for Supply and Demand management purposes. The credit is currently settled with the End Consumer through the User in accordance with relevant contractual arrangements.

Transco recognises that contractual arrangements between the User and End Consumer may require further discussions, should this Proposal be implemented.

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 does not anticipate any such consequences.

Transco does not believe that a change is required to the 'transitional' Exit Capacity incentive provided in it's GT Licence.

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

Advantages:-

- Removes an incentive for Users and End Consumers to wait for Transco to Interrupt in the event of Supply and Demand balance deficit when such a primary balancing role is the responsibility of the User to manage.

- The removal of the credit may encourage more User Portfolio management interruption and greater use of the market to manage Supply and Demand balancing.
- Incentivises Users to complete the Primary Balancing role.
- Aligns Transco's incentives to its ability to respond to such incentives.

Disadvantages:-

- Users will no longer receive an Exit Capacity Investment Incentive charge credit when Interruption is for Supply and Demand management purposes.

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.

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

Implementation is not required to enable Transco to comply with any 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

Transco does not anticipate any such requirement.

14. Programme of works required as a consequence of implementing the ModificationProposal

Finalise system design requirements,
Evaluate systems changes,
Design and build systems,
Test new system
Introduce to 'live' environment.

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

Draft Modification Report circulated - 24 May
Consultation period ends -15 June
Modification Report issued - 6 July
Of gem decision expected -Late August
Network Code implementation -1 October
Systems implementation -1 October

16. Recommendation concerning the implementation of the Modification Proposal

Transco recommends the implementation of this Proposal.

17. Text

Draft Legal Text

SECTION G

Amend paragraph 6.1.9 as follows:

"In respect of an Interruptible Supply Point the Registered User (or Sharing Registered Users) shall:

(a) not be required to pay NTS Exit Capacity Charges and LDZ Capacity Charges;

(b) be entitled to a payment, where in respect of an Interruptible Supply Point Transco requires Interruption in accordance with either:

(i) paragraph 6.7.3(a) (save where the relevant Transportation Constraint is or is anticipated to be in relation to the extent or distribution of supply or demand in any part of the System); or

(ii) paragraph 6.7.3(b),

in aggregate on more than 15 Days in any Formula Year, calculated in the manner provided in the Transportation Statement."

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:

Richard Court
Commercial Frameworks Manager
NT & T

Date: