Shippers, Transco and other interested parties

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Dear Colleague,

Modification Proposal 0698 *Requirement for Publication of Transco's Billed Charges Against Target*

Ofgem[1] has considered the issues raised in this modification proposal and all the consultation responses and has decided to direct Transco to implement this proposal as it would allow Transco to better facilitate the relevant objectives as set out under standard condition 9 of its Gas Transporter (GT) licence.

In making this decision Ofgem had regard to its statutory duties and Transco's obligations under its GT licence. The reasons for making this decision are set out below.

Background

Transco levies transportation charges on users of its national transmission system (NTS) and distribution networks (formerly known as local distribution zones) to recover its price control allowed revenue for transmission asset owner (TO), transmission system operator (SO) and distribution network (DN) activities. The charging methodology for recovering its allowed revenue from system users is governed by obligations set out under standard condition 4A of Transco's GT licence.

Under standard condition 9 of its GT licence, Transco has an obligation to establish transportation charging arrangements which facilitate the efficient and economic operation of its pipeline system, secure effective competition between relevant shippers and suppliers and which secure domestic customer security standards.

Transco is also required to ensure that its charges reflect the costs that it incurs in its transportation business. In setting charges, Transco is required to use best endeavours to set transportation charges such that the total revenue from such charges does not exceed its allowed revenue in any given year.

[1] Ofgem is the office of the Gas and Electricity Markets Authority (the Authority)

Under the NTS arrangements, transportation charges comprise entry capacity charges (determined through entry capacity auctions), exit capacity charges, a TO commodity charge (to address under recovery of entry charges) and an SO commodity charge to recover SO related costs and incentive payments.

DN charges for Transco's current eight low pressure pipeline zones are composed of capacity and commodity charges (split on a 50:50 basis) and customer charges. Capacity charges are based on peak daily load flow and are dependent upon customer load size. Commodity charges are based on each customer's expected annual utilisation (for firm and interruptible load). Customer charges reflect specific supply point and customer related costs.

Transco's reporting obligations

When Transco intends to publish any revised or amended statement of transportation charges it must notify the Authority at least 28 days in advance. Transco also has to provide the Authority with the following information:

- a forecast of maximum TO, SO and DN transportation revenues and their components for the formula year in which the proposed change in charges will take place and for the following year; and
- an estimate of the maximum TO, SO and DN revenues and their components for the formula year preceding the proposed change in charges.

If Transco does not publish or effect any change in charges within three months of the commencement of a formula year, it has an obligation to provide the Authority with a forecast of the maximum revenue and its components for each of its transportation activities in respect of that formula year. Within three months after the end of each formula year, Transco is also required to send to the Authority a statement showing the actual revenue recovered for each of its transportation activities in respect of that formula year.

Further details of the information to be provided to the Authority in connection with the transportation system revenue restriction are set out in Special Condition 28B and Special Condition 33[2] of Transco's GT Licence.

The proposal

Under this modification proposal Transco would be required to produce a monthly report for Shippers and Suppliers. This would detail the billed monthly charges and forecasts of annual revenue allowed by the price control for each charge levied by Transco. The proposer suggested a format for the monthly statement and anticipated that in the event of the sale of a distribution network, then any obligation to report on DN revenue flows would pass from Transco to the new DN owner under a unified network code.

[2] Special condition 28B Part 1 paras (4) (10) and (15): *Reporting Obligations* and Special Condition 33 *Information to be provided to the Authority in connection with the transportation system revenue restriction*

Respondents' views

There were seven responses to this modification proposal. The majority of respondents supported the proposal as they considered that the information would provide a useful indicator of prospective changes to charges.

In summary, respondents who supported the proposal indicated that:

- the proposed forecast of revenue would provide Shippers with more certainty about likely future changes in charges and so reduce their business risk in setting their charges;
- this information would assist with transparency given the potential for the introduction of separate DN price controls;
- the proposal would alert Shippers to price changes and will allow shippers and consumers to make informed decisions; and
- there would be no significant implementation costs for Transco.

A small number of respondents had concerns about the publication of forecast revenue data. Respondents who were against the proposal considered that:

- the information would not reduce the frequency and magnitude of changes to charges; and
- the indicative information provided by Transco would not provide certainty of the magnitude or timing of price changes.

Full copies of the consultation responses to this proposal are available on Transco's Network Code information services website[3].

Transco's views

Transco did not support this proposal. It considered that the information requested would not provide a reliable indication of future changes in charges because it considered that a number of factors would be taken into account in a decision to change charges.

Transco noted that it already complies with a reasonable endeavours obligation to provide 150 days notice of changes to charges to the Authority and that it shares this information with Shippers.

Transco further considered that other changes to charging arrangements could reduce the uncertainty associated with changes to charges. For example, pricing consultation paper 78 (PC 78) *Introduction of TO Commodity Charge*, (implemented from October 2004) provided for a TO commodity charge to address under recoveries of auction revenue. This charge will be set in October and April of each year, where appropriate.

Ofgem's views

Modification proposal 0670 *Requirement for Publication of Transco's Revenue Flows Against Target* proposed that Transco should publish aggregate sums invoiced to shippers on a monthly basis for each transportation charge. Ofgem rejected modification proposal 0670 in April 2004. The decision letter recognised there was merit in the intentions that lay behind that proposal. Modification proposal 0698

[3] www.Transco.co.uk

follows the intent of modification proposal 0670 but provides greater clarity on the range of data and the requirement for forecast information that Transco would be obliged to provide.

There are a number of advantages in releasing information to Shippers, in particular when Transco's performance against its targeted revenues could result in unforeseen changes to the level of its charges. This proposal provides information which should improve transparency and may allow Shippers to better anticipate changes to transportation charges. The provision of this information should not lead to significant costs for Transco. Therefore, the release of this information could better facilitate effective competition between relevant Shippers and Suppliers.

Nevertheless, this proposal does not fully address Shippers' concerns about the frequency of changes to charges. Additionally, the proposed format of the monthly report will include both actual billed sums and forecast annual revenue, but it will include limited information on the assumptions that Transco has made in deriving its forecasts. Ofgem would encourage Transco to fully explain the assumptions behind its forecasts wherever possible and continue to try and provide adequate notice to Shippers of changes to charges.

Ofgem's decision

For the reasons set out above Ofgem has directed Transco to implement this proposal as it would better facilitate the achievement of the relevant objectives by facilitating effective competition between relevant Shippers and Suppliers.

If you require any further information in relation to this proposal please feel free to contact Tolani Azeez on telephone number 0207 9017043.

Yours sincerely

Andrew Walker
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