

A REPORT ON AGREEMENTS MADE PURSUANT TO THE NETWORK CODE, INCLUDING ADVANCE RESERVATION OF CAPACITY AGREEMENTS (ARCAs)

Introduction

The network code came into effect into March 1996. The need for a network code had been highlighted in the MMC's 1993 report on British Gas. The purpose of the network code was to provide non-discriminatory access for all users to Transco's network. It is therefore intended that the terms and conditions of the network code apply to all users of Transco's system.

However, in some circumstances, there may be a requirement for agreements in addition to the network code for the provision of services not otherwise included in the network code (described as agreements made pursuant to the network code in the rest of this paper). Such agreements require the approval of the Director General. This note outlines and discusses the general principles that would be unlikely to delay Ofgas approval of such agreements. In particular, this note outlines how those general principles apply to Advanced Reservation of Capacity Agreements (ARCAs) as well as reporting on briefly on those ARCAs concluded for 1998.

General principles

When considering whether to grant approval for agreements made pursuant to the network code, the Director must take into account her duties under the Gas Act together with Transco's obligations under its the Gas Act as well as its PGT licence conditions. For her part, the Director General is required to:

- ensure that licence holders can finance their functions,
- enable supplies for gas demand to be satisfied, and
- secure effective competition between gas suppliers and shippers.

Under the Gas Act, Transco:

- is required to meet all reasonable demands for gas transportation;
- must develop and maintain an efficient and economical pipeline system; and
- must offer access to its system in a non-discriminatory manner.

Transco's public gas transporter licence requires it to develop a network code that facilitates the achievement of the "relevant objectives", one of which is the "securing of effective competition between relevant shippers and between relevant suppliers."

Transco's licence also requires that it only enter into transportation arrangements that are consistent with its network code, unless the Director General accepts otherwise.

Outlined below is a list of the main features of an agreement that is made pursuant to the network code which arise from the duties laid down by the Gas Act and Transco's PGT licence conditions that Ofgas considers should apply to all such agreements:

- the general form of all such agreements should be subject to consultation;
- all such agreements are generally subsidiary to the network code and should be capable of modification in line with changes to the network code;
- to the extent that such agreements offer gas transportation services in addition to those available under the network code and hence confer advantages on the signatories, additional commitments are also made by Transco;
- any additional charges (in addition to those normally arising under the network code) are subject to consultation¹;
- additional services are available on the same terms to all similar loads transported over Transco's system; and the effect of such an agreement should be similar when the circumstances underlying that agreement are similar, and

¹ Normally, this would be under section 4 of PGT's licence

- there must be reasons why the service offered by Transco in such agreements are not included in the network code (for example the additional services being offered are particular to specific exit points).

Agreements to which these principles should apply may include advance reservation of capacity agreements, network exit agreements, interconnector agreements and network code allocation agreements.

The way in which the requirements of the Gas Act and Transco's PGT licence have shaped Ofgas' view of agreements made pursuant to the network code and enabled us to develop, with Transco, the framework of the 1998 ARCAs is explained below.

ARCAs

An Advanced Reservation of Capacity Agreement (ARCA) is an agreement made pursuant to the network code that allows advance reservation of capacity on Transco's system. Such agreements require Ofgas approval.

There follows a description of how the principles outlined above in relation to agreements made pursuant to the network code have been applied to ARCAs in particular. This also outlines the acceptable terms and conditions that an ARCA may contain without delaying Ofgas approval.

Requirement for consultation

In 1996, Ofgas created a advisory group² to assist the Director General in her consideration of matters relating to Transco's charging structure. The group suggested that Ofgas should prepare a discussion paper on the issues relating to access to capacity on Transco's network. A draft paper, dated 24 October 1996, was prepared for that purpose and circulated to members of the group. An expanded final version of the October draft (dated 2 December 1996) was circulated widely within the industry. That paper reviewed the issues, summarised the views of the respondents, and presented Ofgas' conclusions on the issues involved³.

Subsidiary to the network code

All ARCAs incorporate the principle that the ARCA will be modified to be consistent with any relevant modification of the network code. As such they are subsidiary to, and are consistent with, the network code. They are capable of modification as the network code is modified.

Advantages of the signatories matched by commitments from Transco

ARCAs offer gas transportation services in addition to those available under the network code and hence confer advantages on the signatories. ARCAs allow signatories to reserve capacity in advance of the first gas flow day. In return, Transco commit that the appropriate capacity will be available on the stated day. To protect Transco from some of the risk that load will not result even though transmission investment has been made, an ARCA includes a guarantee that the signatory will pay one year's exit capacity charges and weighted average entry charges even if gas does not flow.

² Known as the Transportation Charges Steering Group

³ This paper did not address issues relating to network exit agreements, as these had been the subject of an earlier consultation

In addition, when a large new load requires National Transmission System (NTS) reinforcement, it is appropriate that Transco receives sufficient notice. Transco also has to ensure that its network is developed and run efficiently. As such it is appropriate that Transco should not have to reinforce for a specific new load if there is a particular risk that the load does not materialise as planned.

If Transco can demonstrate to Ofgas that a particular load is riskier than the overall portfolio of firm loads then an additional commitment from the shipper or customer may be appropriate. For instance, this may be seen as a means of tackling any future extra perceived risk to Transco of bypass at the interconnector.

Any charges subject to consultation

In the case of ARCAs, no extra charges from Transco arise if gas flows. The level of the payment by shippers if gas does not flow was consulted upon in our earlier consultation on ARCAs. We decided that commitment beyond one year is not normally appropriate as the network code only requires capacity to be booked on an annual basis. This commitment could be made by a shipper or by the customer.

Availability for similar loads

ARCAs are available, indeed Transco require them, for all new firm large firm loads requiring a peak supply of 0.5 mcmd (which generally equates to 20 million therms per annum, depending on load factors).

Case for exclusion from the network code

ARCAs have been developed for a limited number of particular loads on Transco's system. At this stage, without being clear what the future demand for ARCAs is likely to be, we were content that ARCAs not be included as part of the network code. If ARCAs continue to be desired by Transco, it will be necessary to consider whether they should be incorporated as part of the network code.

Other comments

Once a new load is on the system, and after the first gas flow day, the established network code liabilities and obligations upon which capacity continues to be made available by Transco apply. That is, once a load has made an initial capacity booking it will receive the same transportation service as any similar load under the network code.

It remains open to a customer or shipper to not sign an ARCA. In those circumstances the shipper or customer can notify its requirements to Transco for planning purposes, and, providing such a request was considered reasonable, Transco would be obliged to make capacity available in accordance with the network code. But this procedure would not necessarily guarantee the ability to flow gas on a certain date. This may be due to higher than expected load growth from other market sectors or changing supply patterns.

For price control purposes we propose to exclude from Transco's transportation revenues any payments they may receive in respect of ARCAs for which gas flow did not materialise as expected. This is to ensure that Transco are not penalised unduly by the price control when expected gas does not materialise. However, the final terms of the price control licence condition have yet to be finalised.

Report on 1998 ARCAs

At present nine ARCAs for 1998 have been approved by Ofgas; five for the interconnector to Belgium and four for power station projects. The ARCAs accepted by Ofgas are virtually identical with one exception⁴.

Implications for 1999 ARCAs

The lead time for investment required currently by Transco is normally between 18 and 24 months.⁵ There is some continued demand⁶ to conclude ARCAs for gas flow in 1999. There has been no significant pressure that 1999 ARCAs need be any different to those ARCAs signed for 1998 gas flow. We therefore conclude that 1999 ARCAs should follow the framework outlined above for 1998 ARCAs.

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⁴ An early ARCA contained provisions enabling the Director General to bring certain of its conditions into line with other ARCAs; this has now been achieved

⁵ On occasions, the lead time can be up to three years. Customers should therefore discuss their needs with Transco at the earliest opportunity.

⁶ Ofgas is aware of two letters outlining demands for extra firm capacity in 1999