

TRANSCO CONSULTATION REPORT ON PC46

Administration Charges Associated with Connected System Exit Points

1. TRANSCO'S INITIAL PROPOSAL

Transco's Pricing Consultation paper PC46 proposed revised charges for administering Connected System Exit Points (CSEPs) containing Non-Daily Metered (NDM) and Daily Metered (DM) supply points. Separate charges are proposed for NDM and DM CSEPs. The present charge for the administration of CSEPs is £5 per supply point.

For DM CSEPs the proposed charges are dependent on whether the site is telemetered or non-telemetered and are split into three categories: daily, set up and transfer. They are:

	<u>Non-telemetered</u>	<u>Telemetered</u>
Daily	£2.06	£1.61
Set up	£66	£53
Transfer	£24	£18

Analysis of the costs of administering NDM CSEPs shows that cost reflective charges based on a supply point basis would consist of a charge of £6.50 per supply point.

2. SUMMARY OF RESPONSES

Transco received eight responses relating to the CSEP charging proposals of which four were from shippers and four from Independent PGTs (iPGTs).

Five respondents opposed the proposal. One respondent supported the differential charging structure for DM CSEPs and recognised the difficulty in levying a charge per shipper for NDM CSEPs. One respondent said that the proposed charges for DM CSEPs seemed satisfactory but that costs on PGT networks were already high without additional administrative costs. One respondent thought the charges should be cost reflective but not allowed to change at this time.

2.1 Principle Of An Administration Charge

Comments Received

- ◆ One respondent supported differential charging for DM and NDM CSEPs, but could not see why the charges for DM CSEPs need to be like a shared meter point
- ◆ One respondent supported the move towards cost reflective charging for CSEPs but wanted a more complete breakdown of the costs. The same respondent also wanted to know how the existing cross-subsidy would be resolved.
- ◆ Five respondents stated that the charge arises because of the inability of UK-LINK to handle these services. One respondent stated that the decision to carry out CSEP administration off-line was not a considered one.
- ◆ Two respondents said that a shipper on an iPGT network must also pay Transco transportation charges and can therefore pay higher charges than a Transco "all the way" charge

- ◆ One respondent said that iPGTs do not levy a charge on Transco for the information that Transco requests
- ◆ One respondent contends that Transco sees off-line processes as not necessarily inefficient and therefore sees the charge as a reward for inefficiency
- ◆ One respondent contends that Transco is not being open about how the charges are derived
- ◆ One respondent noted that the absence of the charge would represent a cross-subsidy of 0.0001% across all transportation charges.

Transco's Response

Two fundamental points emerge from respondents concerns. First is the evolution of the UK-LINK system, and second is the level of transportation charges a shipper transporting to a CSEP supply point attracts. The first is covered below. The second is addressed in the example in section 2.3 which shows the transportation charges that shippers shipping to CSEP supply points face compared to shippers using the Transco transportation system alone.

The scope of the UK-LINK system was agreed with the industry at the time of implementation of the Network Code. At that time it was agreed that the CSEP commercial regime was not sufficiently defined to justify systematisation via UK-LINK. Transco therefore developed CSEP administration processes that have evolved into the present system with the following features:

- ◆ Efficiency: the system is based on a Microsoft Access database that automatically handles supply point administration and billing processes
- { Flexibility: changes (such as changes to the commercial regime) can be more readily implemented than would be the case for a mainframe system
- { Low entry costs: the present system does not require iPGTs to invest in systems to interface with Transco. Several iPGTs have indicated that they are unwilling to commit to such investment, which may constitute a barrier to entry.

However, CSEP administration does cause Transco to incur administration costs and therefore a charge is valid since:

- { BG's PGT Licence requires that transportation charges reflect costs. CSEP administration incurs costs and therefore a charge is consistent with the Licence objectives;
- { If there were no charge, CSEP shippers would be cross subsidised by those shippers that do not require CSEP administration services (as acknowledged and quantified by one respondent); and
- { An administration charge is consistent with the existing charges for allocation arrangements at shared supply points and Moffat

Furthermore, the principle of a charge is embodied within the Network Code, with the present charge being implemented in 1996, following industry consultation. Since shippers consume Transco's transportation services, it is right that transportation charges are met by shippers, not PGTs.

2.2 Cost Reflectivity

Comments Received

Several respondents expressed concern about the cost reflectivity of the proposed charges, some more detailed than others:

- ◆ Three respondents said that there was no incentive on Transco to reduce costs
- ◆ One respondent said that development of the system should be complete. Another said that Transco presumably charges for enhancements to the systems
- ◆ Two respondents said that the unit charge, based on a marginal cost, should have reduced the charge. One added that further automation should have reduced charges. One respondent said that the costs vary from year to year
- ◆ One respondent said that returns to scale had been ignored
- ◆ Two respondents said that the number of supply points used in the assumptions was very low, and that weekly AQ updates instead of the daily frequency assumed would decrease the charge
- ◆ One respondent said no mention had been made of the impact of Modifications 0216 and 0319, and another suggested that Transco was trying to by-pass Modification 0319
- ◆ Two respondents questioned the treatment of commercial framework costs. One said they should be defrayed across the whole business, and the other that they should not be included
- ◆ Two respondents questioned the treatment of faxed allocations. One said that there should be no need for this service and therefore the associated cost. The other queried why the unit cost had increased from £2.20 last year to £9.58 in the present proposals
- ◆ One respondent queried why the cost for set-up on UK-LINK had increased from £4.02 and was now £5.90, whereas this was £5.09 in PC45
- ◆ Three respondents thought there was an element of double charging, for costs associated with UK-LINK for example
- ◆ One respondent said that the costs of CSEP reconciliation should not be included, but defrayed across the whole business
- ◆ One respondent said that the uplift was too high and should be 25%
- ◆ One respondent presented data for a comparison with a similar service for an iPGT
- ◆ Two respondents explicitly welcomed cost reflective charging. One of these thought that Transco was being selective when presenting arguments for cost reflectivity and competition (the same point is made in section 2.3 below)

Transco's Response

Many of the concerns expressed by respondents may be based on misconceptions about the methodology used to derive the proposed charges. Transco would emphasise the following:

The incentive for Transco to reduce costs is provided by its price control formula. The formula determines Transco's maximum allowed revenue. Any reduction in the cost of administering CSEPs, and consequently reduced CSEP administration charges, would not affect Transco's total allowed revenue, and hence any cost saving would lead to increased profit. In practice, Transco has already systematised many CSEP administrative processes in order to improve efficiency and reduce costs.

The costs presented in the paper do not include system development costs. Transco is constantly looking to update its off-line processes and increase efficiency, and hence development is not complete.

Transco will continue to work with the industry to improve the efficiency of CSEP administration processes. The efficiency gains that might be expected to arise from such improvements were reflected in the costs presented in the consultation paper. However, system development costs associated with these improvements are not reflected in the proposed charges.

Transco unit costs are reducing. If charge proposals had been put forward on a per supply point basis in the past then the charge per supply point would have been £10 in 1997, £8.31 in 1998 and £6.50 in 1999. Transco does not believe the present charge of £5 is fully cost reflective. In addition, it would be surprising if the outturn costs did not vary from year to year as systems and processes are updated. The costs presented in the consultation paper were forward looking cost estimates reflecting likely improvements in efficiency, an approach which seeks to reduce the potential variation in charges between years.

The assumption used of 28 supply points per CSEP is based on past and present supply point nomination data as received by Transco from iPGTs. Month on month data since January 1998 has consistently shown the average number of supply points per CSEP to be between 25 and 30. Transco would welcome alternative evidence from any party.

In relation to potential Network Code modifications, a degree of judgement is necessary when assuming the likely path of future costs. The proposed charge in PC46 assumed that AQ updates will move to a daily frequency in 1999/2000 as per Modification 0216. Final agreement has also not been reached on whether PGTs will want daily faxed allocations as they receive at present. The charge has increased from last year based on outturn costs from last year and the projected numbers of future CSEPs. If this service was not required the charge would reduce to £5.80 per supply point. Discussion on Modification 0319 is in its early stages and no account has been taken of its potential impact.

The commercial framework costs and CSEP reconciliation costs relate specifically to CSEPs. The costs for the commercial framework are at present on-going as the framework is still being developed. The costs for both services have been excluded from the shipper service costs in order to avoid double counting. Similarly there is no double counting of UK-LINK or billing costs. These are also not included in the shipper service costs that are reflected in other transportation charges.

The costs of setting up on UK-LINK have increased because analysis has revealed that an element for weekend working has had to be built in. This was not the case last year or in PC45.

The level of uplift and methodology for determination is described in Transco's paper, 'Charging for Specific Services - Cost Assignment Methodology - A Background note by Transco (May 1999)'. Transco does not believe it would be appropriate nor cost reflective to assume a fixed 25% uplift in this case.

2.3 Effect On Competition

Comments Received

- ◆ Two respondents said that it would seem more logical to levy a shipper only charge but realised there were implications for competition
- ◆ One respondent said that increased charges will be a barrier to competition
- ◆ Three respondents suggest that in effect the charges will polarise the transportation market. One goes further to say that the combined effect of the pricing proposals will be to increase the Transco charge by 7% for a shipper supplying a domestic customer on a typical connected system. One says that competition between PGTs is inhibited because they are price takers
- ◆ Two respondents say that the charge inhibits competition in the connections market. They say that Transco is a direct competitor and one says Transco is being deliberately anti-competitive but that it is difficult to gauge Transco's competitiveness in the market because of the way Transco publishes its prices
- ◆ One respondent says that Transco is using the charge as a flywheel to generate unregulated income

Transco's Response

Transco's PGT licence requires that, as far as is consistent with the primary objective of reflecting costs, transportation charges should facilitate competition between shippers and between suppliers. Transco's response is therefore confined to issues concerning competition in supply. However, Transco note that CSEP growth has continued at an exponential rate in the past year, and that the observed rate of growth is not consistent with the argument that an administration charge represents a barrier to competition in transportation.

The effect of the CSEP administration charge on competition in supply should be assessed in the context of the total transportation charges for CSEP supply points, that is the transportation charges made by Transco plus the charges made by the iPGT.

Transco's transportation charges per supply point on a CSEP are considerably less than the charges for an equivalent supply point connected to Transco's system.

Table 1 - CSEP Transportation Charges Compared to Equivalent Transco Supply Point

	Transportation charges (1) (£ per supply point per annum)	
	Present	Proposed
CSEP supply point (2)	59	59
Transco supply point	117	113

Notes :

1. Present transportation charges for a domestic supply point. NTS entry charges based on Bacton and NTS exit charges based on exit zone WM3. Each premises annual load 20,000 kWh
2. Based on a CSEP comprising thirty domestic premises.

This differential is due to two factors: LDZ charges for CSEPs are lower than for an equivalent Transco system since the unit rate is based on the entire CSEP peak day load; and CSEPs pay no customer charge.

In terms of the connections market, Transco would welcome clarification on how this administration charge can affect competition in this market.

3. SUMMARY OF TRANSCO'S FINAL PROPOSALS

Transco maintains that a CSEP administration charge is correct in principle for the following reasons:

- { BG's PGT Licence requires that Transco's transportation charges reflect costs. CSEP administration incurs additional costs
- { If there were no charge, CSEP shippers would be cross-subsidised by those shippers who do not require CSEP administration services
- { The administration charge covers the bit of customer charge which CSEPs don't pay

Transco proposes therefore that the administration charge for CSEPs should be as set out below:

For DM CSEPs the proposed charges are dependent on whether the site is telemetered or non-telemetered and are split into three categories: daily, set up and transfer. They are:

	<u>Non-telemetered</u>	<u>Telemetered</u>
Daily	£2.06	£1.61
Set up	£66	£53
Transfer	£24	£18

For NDM CSEPs a charge of £6.50 per supply point.

It is proposed that these charges take effect from 1 October 1999.