

GCM12 (Draft) Separate Management of K for Charge Setting Purposes

Gas TCMF

11th June 2008

Issue

- ◆ Ofgem vetoed GCM11
 - ◆ GCM11 would have led to minimal Entry Over recovery
 - ◆ Entry Under recovery would lead to Exit cross subsidising Entry Users, and
 - ◆ Exit Users would gain minimal benefit from Entry over-recovery.
 - ◆ Ofgem argue that this would be asymmetric, and the status quo (with GCM10 implemented) is symmetric.
- ◆ GCM12
 - ◆ GCM12 (Draft) = GCM11 + Manage the K mechanism separately for entry and exit ~ exact symmetry
 - ◆ Draft Consultation Paper placed on website [nationalgrid](#)

Additional Methodology Process

- ◆ $GCM12 = GCM11 + \text{Separate Management of entry and exit 'K' for charging purposes only}$
- ◆ The TO K mechanism amount, *defined within the Licence as the difference between allowed revenue and collected revenue inflated for the average specified interest rate*, would be attributed to entry and exit separately for charge setting purposes only.
- ◆ Calculation of K depends on net under or over recovery

'K' Entry/Exit Calculation

- ♦ Aim is to minimise amounts in a consistent way and ensure
 - ♦ $\text{Entry K} + \text{Exit K} = \text{Licence K}$

Net Under Recovery (or zero)

- ♦ Calculate K for each component using applicable (lower) interest rate

Net Over Recovery

- ♦ Calculate K for under recovered component using the lower interest rate
- ♦ Licence K calculated using the applicable (higher) interest rate
- ♦ Calculate K for over recovered component as the difference between the total K and the under recovered component

Entry & Exit Over Recovery

- ♦ Calculate K for each component using applicable (higher) interest rate

Examples

Example	Entry After GCM10/12 payments	Exit	Total	Licence K	Existing	Proposed	
					Entry & Exit K	Entry K	Exit K
1.	-£1m	-£1m	-£2m	-£2.1m	-1.05m	-£1.05m	-£1.05m
2.	-£1m	£0.5m	-£0.5m	-£0.525m	0.2625m	-£1.05m	£0.525m
3.	-£1m	£1m	0	0	0	-£1.05m	£1.05m
4.	-£1m	£1.5m	£0.5m	£0.54m	0.27m	-£1.05m	£1.59m
5.	0	-£1m	-£1m	-£1.05m	-0.525m	0	-£1.05m
6.	0	£1m	£1m	£1.08m	0.54m	0	£1.08m
7	£0.5m	-£1.5m	-£1m	-£1.05m	-0.5025m	£0.525m	-£1.575m
8.	£0.5m	-£0.5m	0	0	0	£0.525m	-£0.525m
9.	£0.5m	-£0.4m	£0.1m	£0.108m	£0.054m	£0.528m	-£0.42m
10.	£0.5m	£0.5m	£1m	£1.08m	£0.54m	£0.54m	£0.54m

K = Actual minus Allowed Revenue. (Positive = Over-recovery, Negative=under-recovery, K is subtracted from allowed revenue in the following year)

Interest rate assumed ~ 5.00% under-recovery, 8% over-recovery

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'K' Entry/Exit Management Mechanism

Net Position	Exit	Entry	Calculation
Net Over Recovery	Exit Over-recovery	Entry Under-recovery	$\text{TOKEN}_t = (\text{TOREn}_{t-1} - \text{TOMAREn}_{t-1}) \times (1 + \text{IR}_t/100)$ $\text{TOKEx}_t = \text{TOK}_t - \text{TOKEN}_t$
	Exit Under-recovery	Entry Over-recovery	$\text{TOKEx}_t = (\text{TOREx}_{t-1} - \text{TOMAREx}_{t-1}) \times (1 + \text{IR}_t/100)$ $\text{TOKEN}_t = \text{TOK}_t - \text{TOKEx}_t$
	Over Recovery		$\text{TOKEx}_t = (\text{TOREx}_{t-1} - \text{TOMAREx}_{t-1}) \times (1 + (\text{IR}_t + \text{PI}_t)/100)$ $\text{TOKEN}_t = (\text{TOREn}_{t-1} - \text{TOMAREn}_{t-1}) \times (1 + (\text{IR}_t + \text{PI}_t)/100)$
Net Under Recovery	Exit Over-recovery	Entry Under-recovery	$\text{TOKEx}_t = (\text{TOREx}_{t-1} - \text{TOMAREx}_{t-1}) \times (1 + \text{IR}_t/100)$ $\text{TOKEN}_t = (\text{TOREn}_{t-1} - \text{TOMAREn}_{t-1}) \times (1 + \text{IR}_t/100)$
	Exit Under-recovery	Entry Over-recovery	
	Under Recovery		

Where

TOKEN_t ~ TO Entry Revenue adjustment factor in respect of formula year t for charging purposes

TOREn_{t-1} ~ TO Entry Revenue collected in year t-1

TOMAREn_{t-1} ~ TO Maximum Allowed Revenue allocated to Entry in the Charging Methodology

IR_t ~ Percentage interest rate in respect of formula year t [Licence Special Condition C8B (3)(d)]

PI_t ~ Penalty interest rate in respect of formula year t [Licence Special Condition C8B (3)(d)]

TOK_t ~ Revenue adjustment factor in respect of formula year t [Licence Special Condition C8B (3)(d)]

TOKEx_t ~ TO Exit Revenue adjustment factor in respect of formula year t for charging purposes

TOREx_{t-1} ~ TO Exit Revenue collected in year t-1

TOMAREx_{t-1} ~ TO Maximum Allowed Revenue allocated to Exit in the Charging Methodology

Potential Charging Methodology (GCM12)

Timelines

Milestone	Potential	Latest
Charging Methodology Proposal issued	August 2008	October 2008
Consultation Ends	September 2008	November 2008
Consultation Conclusions Report inc. Final Proposals	October 2008	December 2008
Ofgem veto period ends (Assumes no Impact Assessment)	November 2008	January 2008
Notice of Charges	1 st February 2009	
Implementation	1 st April 2009	

Views?

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