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Independent gas transporters, shippers and other interested parties

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Dear Colleague,

Calculation of the Connected System Exit Point (CSEP) charge under Relative Price Control (RPC) for IGTs

1. Some industry participants have recently expressed concerns about the current method for calculating the CSEP charge under the RPC charging arrangements. In this letter, we present an alternative approach to calculating the CSEP charge, and invite views on whether this approach should be adopted.

2. Views are invited from interested parties on this alternative approach. Responses should be received by 14 January 2005 and sent to

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3. Electronic responses could be sent to the e-mail address above.

The current approach: average CSEP unit rate

4. Under the existing arrangement, an average CSEP unit charge (pence/kWh) is calculated for each CSEP. This average CSEP unit charge is applicable to each property - irrespective of load size - connected to the same CSEP and governed by the same original binding contract. The method for calculating the CSEP unit rate is outlined in paragraphs 6.5-6.6 and 6.17-6.19 of the RPC Guidance.

5. A single CSEP unit rate arises because the current approach involves calculating the capacity element of the Local Distribution Zone (LDZ) charge using the aggregate (sum of

the individual properties) Supply Point Offtake Quantity (SOQ) and not the individual property SOQ.

The alternative approach: CSEP unit rate per load band

6. An alternative approach would be to follow more closely Transco's approach in charging shippers up to the CSEP. Under this method, the relevant SOQ of each property (rather than an average SOQ) would be used in deriving the property's CSEP charge. As a consequence, a different CSEP unit charge would be calculated for each property.

7. Table 1 shows the two steps in calculating the capacity element of the CSEP charge for each of the two methods. The table shows that while the current approach calculates the charge on an average basis (using the CSEP SOQ and CSEP AQ) the alternative method uses the property level SOQ and AQ to work out the charge for each property. The commodity element of the LDZ charge is calculated in the same manner under both methods.

Table 1: Calculation of CSEP charge per property[1]

Current approach – average CSEP charge	Alternative approach – actual CSEP charge
LDZ unit rate * **aggregate SOQ** * 365 = average CSEP charge	LDZ unit rate * **property SOQ** * 365 = actual CSEP charge
CSEP charge /**CSEP AQ** = capacity element of CSEP charge (p/kWh)	CSEP charge /**property AQ** = capacity element of CSEP charge (p/kWh)

Charging implications for IGT shippers

8. In some cases, the two methods can result in different IGT charges at a property level. This discrepancy only occurs when a site contains properties in more than one load band (end user category). Thus on a purely domestic site (where all properties fall within the same load band), the two approaches would generate the same level of charges.

9. In contrast, a site containing a mix of domestic and I&C premises, or a site that contains I&C premises falling within different end user categories, may have different property charges depending on which method is adopted.

10. Irrespective of the method adopted, IGTs will recover the same total revenue for each site. IGTs should therefore be neutral between the two methods.

11. However, the manner in which site-level charges are recovered between different property types varies between the two approaches. Specifically, our analysis indicates that for a site containing properties with different load bands:

[1] LDZ capacity element of the CSEP charge

- charges for large I&Cs would be higher under the alternative approach than the current method; and

- charges for domestic properties would be lower under the alternative method than the current approach.

12. An example of the discrepancy in charges for domestic and I&C properties based on an actual site is provided in Table 2. The table shows that, if the alternative method were adopted, the relevant shippers would be charged:

    - almost 80% more for the very large I&C property; and

    - about 7.7% less for a domestic customer.

Table 2: Difference in charges

AQ[2] of premises	Difference to current approach (%)	Difference to current approach (£p.a.)
30,500,000	79.95	3,936.51
4,800,000	-15.81	-747.15
31,000	-7.73	-8.50

13. It is important to note that this discrepancy in charges between the two methods tends to be significant only on sites where a very large I&C property accounts for a sizeable share of the CSEP AQ, as illustrated by Table 2.

14. As such, the large majority of IGT sites would not be affected by the choice of approach. In particular, we have found that the sites for which the two approaches may generate significantly different CSEP charges accounted for less than half a percent[3] of the total number of sites submitted to Ofgem during the first two quarters of 2004 (as part of our RPC monitoring process).

Options for change

10. Although the two approaches would generate different CSEP charges for a small proportion of the total number of IGT sites, Ofgem acknowledges that the alternative method would better reflect the Transco-equivalent charge for these sites.

11. We therefore seek views from interested parties on the following options for calculating the CSEP charge:

    - *Option 1:* maintain the *status quo*;

[2] CSEP AQ = 56.5m kWh
[3] This amounts to 12 sites.

- *Option 2:* introduce the alternative approach ONLY for sites with properties with more than one end user category; or

- *Option 3:* introduce the alternative approach for ALL sites.

15. In your response, please indicate if replacing the current method (option 2 and 3) would impose material implementation costs and an estimate of such costs. These costs could include, for example, amending IT and billing systems that have already been designed to reflect the existing RPC arrangements.

Yours sincerely,

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Senior analyst