

A background image showing a close-up of electrical components, including a white plastic outlet with two gold-colored prongs and a metal terminal block with several wires connected. The image is slightly blurred and has a blue tint.

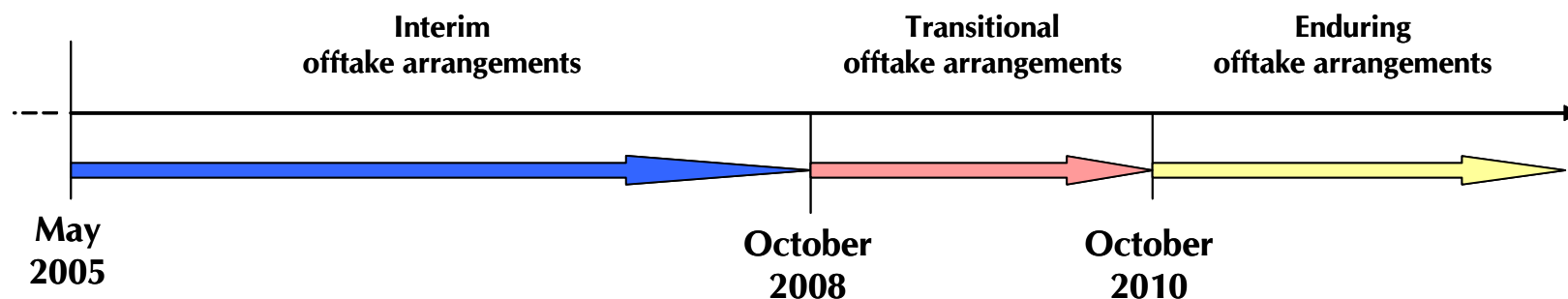
# Overview of TPCR Third Consultation

EOWG 7

- Overview
- Enduring arrangements
  - Impact assessment
  - Strawman of arrangements
  - Revenue drivers and baselines
  - Incentives
- Transitional arrangements
  - Revenue drivers and baselines
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# Overview

- TPCR Third Consultation published 30 March 2006
- Outlines latest views on incentives relating to:
  - transitional regime; and
  - enduring regime.
- Overview in Chapter 5 & detail in Appendix 12.



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# Enduring offtake arrangements

- Views have developed through EOWG process to date
- Key principle is the extent of user commitment:
  - All users – GDNs and TCCs (both existing and new) required to indicate their future usage of the NTS
  - Commitment should be sufficiently far in advance to advise NTS investment planning
  - NTS then receives investment signals that are financially firm with sufficient time to respond, reducing risk of stranded assets
- These proposals should:
  - improve investment signals;
  - provide greater clarity over commitment required to secure capacity; and
  - increase transparency of offtake arrangements

# Impact assessment

- TPCR Second Consultation (Dec 2005) outlined high level options for enduring offtake arrangements

	Status Quo	Long term user commitment models			
	Option Ex1	Option Ex2	Option Ex3	Option Ex3A	Option Ex4
Baseline	(LDZ)	Nodal	Zonal	Global/ network wide	Zonal
Product definition	Nodal	Nodal	Nodal	Nodal	Zonal
Substitution	x	✓	x	x	x

- Qualitative assessment of these models included in the Third Consultation

# Impact assessment

	Long term user commitment models				
	Option Ex2A	Option Ex2	Option Ex3	Option Ex3A	Option Ex4
Efficient network development and system operation	✓✓	✓✓	✓	✓✓	✗✗
Preventing undue discrimination	✓✓	✓✓	✓✓	✓✓	✓✓
Promotion of competition	✓	✓	✓	✓	✓✓
Appropriate allocation of risk	✓✓	✓✓	✓✓	✓✓	✓✓
Simplicity / transparency	✗	✗	✗✗	✗✗	✗✗
Preservation of security of supply	✓✓	✓✓	✓✓	✓✓	✗✗
Minimise implementation and ongoing costs	✗	✗✗	✗	✗	✗✗
Clear and appropriate accountability and responsibility	✓	✗	✗	✗✗	✗✗
Compliance with applicable legal requirements	✓✓	✓✓	✓✓	✓✓	✓✓

- Favoured approach based on Option EX2 (nodal / nodal)
- Do not consider a substitution incentive appropriate
- New Option EX2A contains substitution **obligation**, rather than incentive

# Strawman of arrangements

- NGG and SSE strawmen referenced in Third Consultation document, along with our preliminary views on the key issues raised:

## Product definition



- Users should signal requirements for “flat” and “flexible” offtake capacity on the same terms
- “Expanding flexibility” product seems appropriate (subject to ongoing analysis by NGG NTS)
- Favour allocation through a single “capability” product

## Long term capacity allocation



- Sufficient user commitment a key requirement
- “Prevailing rights” model worthy of further development and consideration
- Appropriate level of user commitment requires further analysis, informed by profile of investment costs

# Strawman of arrangements

Medium / short  
term capacity  
allocation



- Nodal allocation of unsold baseline capacity, with rationing by price (subject to a reserve price) seems appropriate
- Release of non-obligated capacity (and associated incentive) requires further analysis

Interruption  
arrangements



- Consider further development of arrangements in line with NGG NTS strawman proposals is appropriate
- Further work required to understand:
  - process for long term contracting for interruption; and
  - how volume of short term interruptible product is set.

# User commitment and 1 in 20 obligation

Third TPCR consultation document stated “minded to” Ofgem position:

- User commitment should be at the heart of network development
- Only incremental investment driven by user signals will be remunerated
- Compliance with NGG NTS’s 1 in 20 licence obligation could be achieved by investing in line with user commitments which signals peak aggregate daily demand
  - ➔ Greater clarity of responsibility between NTS users and NGG NTS
  - ➔ Causality for investment unambiguous – users incentivised to provide long-term signals

# Revenue drivers and baselines

Baseline level



- Should be specified by node
- Act as both revenue driver “trigger” and define the obligation to release capacity by NGG NTS
- Baselines should be determined through “practical maximum physical capability” approach
- Substitution obligation in long term

Baseline scope



- Baselines to be static across control period
- NGG NTS only remunerated for investments with appropriate level of user commitment
- Revenue for incremental investments only triggered following delivery

Indicative baselines prepared under a practical max phys approach included in Annex 1 of Appendix 12

# Incentives

## Buy backs



- Similar approach to entry proposed
- Administered buy back prices for investment-related buy backs
- Sliding scale incentive for buy backs for planned / unplanned outages
- Views invited on cap for investment-related buy back exposure
- Views invited on market or administered prices for operational buy backs

## Other issues



### *Payment flows*

- Movement to Option 2A payments flows model proposed in enduring offtake implementation timescales
- Views invited on implementation of Option 2A model

### *Exit investment incentive*

- Propose removing this incentive, in light of proposals on revenue drivers

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# Revenue drivers and baselines

## Baselines



- Propose that baselines in transitional period will be used only as “trigger” point for incremental investment revenue
- Based on practical maximum physical capability of network
- No baselines proposed for interruptible capacity
- No baselines for flexibility proposed for this period

## Revenue drivers



- Propose incremental revenue only being triggered once investment is delivered in transitional period
- Consistent with enduring proposals, as far as possible
- Given not full user commitment model some revenue may be triggered absent a user commitment

# Transitional incentives

- Interim NTS incentives have three elements:
  - charges foregone / exit investment incentive;
  - constrained LNG incentive; and
  - Buy back / greater than 15 day interruptions incentive.

## **Charges foregone / exit investment:**

- Propose removing this incentive
- Currently restricted to £1m cap
- Not proposed for enduring period
- Inconsistent with investment planning timescales

## **Constrained LNG:**

- Propose retaining this incentive, and 100% sharing factors, with no cap or collar
- Also propose including in enduring period
- Views invited on level of target

# Transitional incentives

## **Buy back / greater than 15 day interruptions incentive :**

- Incentive currently has 75% upside / 50% downside sharing factors, with a target equal to expected level of greater than 15 day interruption cost
- Propose to exclude investment related buy-backs from this incentive (consistent with earlier proposal)
- NGG NTS will have right to reduce offtake capacity for maintenance purposes in transitional period, therefore no buy back allowance proposed
- Propose retaining greater than 15 day interruption on same basis as currently specified
- Views invited on appropriate target, cap and collar for greater than 15 day incentive

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# Way forward

- Responses deadline: 28 April 2006
  - Note detailed questions listed in Appendix 12
  - Helpful to indicate:
    - Whether response is confidential, and
    - In what capacity you are responding eg, licensee, shipper, GDN etc
- Keen to understand costs & benefits of package of proposals relative to status quo – plan to issue cost survey in this regard
- EOWG to continue until at least June
- Initial Proposals due for publication at end of June