

# **TRANSCO PRICING CONSULTATION PAPER PC80**

## **Introduction of Different Levels of LDZ Charges between Networks**

### **SUMMARY**

Under Transco's present charging methodology LDZ charges are postalised, that is exactly the same charges, in terms of level and structure, apply across all the Networks. With the introduction of separate price controls for each of the eight Networks it is now appropriate to change the methodology to allow for different levels of LDZ charges between the Networks, if required. The proposal for consultation is that the charging methodology should be amended so that the level of the LDZ charges, within the existing structure of charges, can differ between different Networks.

### **1 BACKGROUND**

In June 2003 Ofgem published its document "Final Proposals for the Separation of Transco's Distribution Price Control". Under these proposals each of the existing eight distribution Networks will have its own allowed revenue with effect from 1 April 2004. The document contained details of how the total allowed revenue for distribution would be allocated between the Networks. The basic principle followed was that the allowed revenue allocated to each Network would initially align with the actual revenue derived in that Network through the application of the current transportation charges.

#### **Need for differential charges – Short-term**

The application of the above principle means that there should be no need for differential charges before at least 1 April 2005. Whether differential charges are required at that point will depend on the degree of divergence between collected revenue and allowed revenue for the different Networks, i.e. the size of K for each Network. One reason for significant divergences in the level of K between Networks at 31 March 2005 might be the impact of the weather. Other reasons for divergences might be differential load growth or variances in replacement workload volumes.

The proposal in this paper would change the charging methodology to allow a Network to apply a percentage change to its main transportation charges, without the need to consult, in order to keep its collected revenue in line with its allowed revenue, irrespective of what the other Networks were doing. Before making the change it would simply have to meet the notice requirements for changing charges set out in the GT Licence and the Network Code.

The specific change to the methodology would be that whereas now the level of charges is scaled nationally so as to recover the national total distribution allowed revenue, after April 2005 the level will be scaled within each Network to recover the allowed revenue for that Network. The levels of charges are therefore likely to differ across different Networks. This proposed change to the charging methodology would allow the level of the LDZ charges within a Network to be changed by applying a flat percentage change to the LDZ system and LDZ customer charges without the need to consult. Any changes to the structure of these charges would count as changes to the methodology and would have to be consulted on. The Administration and Other Charges are not included in the scaling mechanism and therefore

the percent changes would not be applied to these charges, which are normally only changed after consultation.

### **Need for differential charges –Long-term**

In the longer-term costs in the Networks will move in different ways and at different rates and these differential movements should be reflected in the charges if they are to remain cost reflective. It may also be appropriate for Networks to change the structure of their charges in the future. However this paper does not address changes in the structure of the charges or the introduction of new charges. Any proposals to change the structure of the charges, or to introduce new charges within a Network would mean a change in the charging methodology in that Network and would have to be consulted on as set out in Amended Standard Condition 4A of the Gas Transporter Licence.

## **2 CONCLUSION**

In the short-term, that is from April 2005 onwards, there is likely to be a need for differential Network charges if the weather or other factors have significantly different impacts between Networks during the formula year 2004/05. The purpose of this paper is to consult on changing the charging methodology so that charges can be set at different levels in the Networks to accommodate the different levels of under- and over-recovery which are likely to emerge under the separated price control. The paper does not allow for changes in the structure of charges or the introduction of new charges which would have to be consulted on in the usual way.

## **3 ACHIEVEMENT OF PRICING OBJECTIVES**

The proposal assists in the achievement of the relevant pricing methodology objectives because it takes account of developments in the transportation business. The change is necessary to ensure that the charging methodology allows Transco and other possible new Distribution Network Operators the flexibility to adjust charges within the Networks to keep actual revenue in line with allowed revenue without the need to consult on simple changes.

## **4 QUESTION FOR CONSULTATION**

The question for consultation is:

That the distribution charging methodology should be modified so that the current regime under which LDZ charges are postalised is replaced with one in which the level of the LDZ charges can be different in different Networks. A simple percentage change could be applied to the level of the main transportation charges in a Network without further consultation, so long as the notice requirements of the Licence and the Network Code were complied with. However, it would be necessary to consult if it was intended to change the structure of the main charges or introduce new charges in a Network.

It is proposed that this change in methodology should be implemented from 1 October 2004, so that it is in place prior to the notice periods for price changes for 1 April 2005 becoming operative.