Modification Report
URGENT Modification Reference Number 0380
Increased Availability of Monthly System Entry Capacity

This Modification Report is made pursuant to Rule 9 of the Modification Rules and follows the format required under Rule 8.9.3.

1. Circumstances Making this Modification Proposal Urgent:

In accordance with Rule 9.1.2 Ofgem has agreed that this Modification Proposal should be treated as Urgent.

Following the implementation of Modification Proposal 0378, the Network Code requires Transco to commence the auction of System Entry Capacity for use in April to September 2000 by 6 March 2000. This proposal is to increase the aggregate quantity of Monthly System Entry Capacity (MSEC) which Transco makes available and change the methodology by which the aggregate quantity is apportioned by ASEP to ensure that MSEC is made available at all ASEPs. This would need to be implemented at the start of the next round of auctions. In order to meet this timetable urgent procedures were agreed.

2. Procedures Followed:

Transco agreed with Ofgem (and has followed) the following procedures for this Proposal;

Issued to Ofgem for decision on urgency	28 January 2000
Proposal agreed as Urgent	31 January 2000
Proposal issued for consultation	31 January 2000
Close out for Representations	18 February 2000
Final Report to Ofgem	23 February 2000
Ofgem decision expected	28 February 2000

3. The Modification Proposal:

Aggregate MSEC availability

This Modification Proposal suggests that the aggregate quantity made available as MSEC is increased by 10%. Transco will continue to calculate the “System Normal Demand” as the arithmetic mean of the demand for gas in respect of the system on each day of the calendar month. This figure will then be multiplied by 1.1 to derive the quantity to be made available.

Availability of MSEC by ASEP

This Modification Proposal also envisages that the methodology set out in Section B 2.2 of the Network Code is amended to ensure that an amount of MSEC is available for purchase at all ASEPs. The process by which the amount of capacity which will be made available for auction as MSEC would be as follows.

1. An assessment of the ASEP Estimated System Entry Capacity in respect of each ASEP for each month will be calculated in accordance with the procedures of Section B 2.2.4 and then scaled up or down so that the Aggregate Estimated System Entry Capacity is equal to 1.1 times the System Normal Demand.

2. Where as a result of step 1. an ASEP is identified as having a Determined System Entry Capacity of less than x % of its Peak Flow Forecast, it will be the subject of a minimum MSEC availability. The minimum MSEC quantity for each relevant ASEP identified will be calculated as:

(1.1* System Normal Demand)*(y/100) * A

Where A = Peak Flow Forecast for ASEP / Sum of Peak Flow Forecasts of relevant ASEPs.

3. The ASEP Estimated System Entry Capacity in respect of each ASEP for each month will then be calculated in accordance with the procedures of Section B 2.2.4 and scaled up or down so that the Aggregate Estimated System Entry Capacity is equal to:

(100-y)/100 * (1.1 * System Normal Demand)

4. The Determined System Entry Capacity for each ASEP in each month will be the sum of the amounts derived under steps 2 and 3 of this process subject to any correction for maintenance in accordance with Section B 2.2.5(b), 2.2.6 (b) and 2.2.7 of the Network Code.

It is proposed that x and y be 5 and 3 respectively.

Alternative Option

Views were requested both on the proposal as described above and on an alternative option of increasing the aggregate available MSEC by 10% but retaining the existing method of apportionment of MSEC by ASEP.

4. Transco's opinion:

Transco believes that this proposal could provide Users with the opportunity to purchase a greater proportion of their System Entry Capacity needs as MSEC and reduce the amount of System Entry Capacity which Users purchase as Daily System Entry Capacity (DSEC). This proposal could also ensure that Users of all ASEPs would have the opportunity to bid for some of their capacity needs as MSEC as opposed to having to rely exclusively on the purchase of daily capacity services.

5. Extent to which the proposed modification would better facilitate the relevant objectives:

The proposal should further develop an economic and efficient allocation of entry capacity. This may be achieved by increasing the availability of MSEC and reducing Users' need for daily capacity. In addition, the proposed methodology will furnish Users with the opportunity to obtain MSEC at smaller ASEPs.

6. The implications for Transco of implementing the Modification Proposal , including:

a) implications for the operation of the System:

If implemented, the proposal would increase the probability that Transco will be required to buy back capacity at locations where the full allocation of MSEC capacity is utillised.

b) development and capital cost and operating cost implications:

Transco would not incur significant IT development costs resulting from this proposal.

c) extent to which it is appropriate for Transco to recover the costs, and proposal for the most appropriate way for Transco to recover the costs:

Not applicable.

d) analysis of the consequences (if any) this proposal would have on price regulation:

Not applicable.

7. The consequence of implementing the Modification Proposal on the level of contractual risk to Transco under the Network Code as modified by the Modification Proposal:

Transco may face increased exposure under the capacity incentive scheme. The sale of an additional 10% of Monthly System Entry Capacity would increase the risk of buy back. This potentially reduces Transco's incentive to make additional capacity available within the New Gas Trading Arrangements.

8. The development implications and other implications for computer systems of Transco and related computer systems of Users:

There would be no significant development implications for computer systems arising from implementation of this proposal.

9. The implications of implementing the Modification Proposal for Users:

Users would have available to them an increased quantity of MSEC, for which they can bid at auction. The increased quantities may lead to lower average prices in the relevant auctions, which consequently will flow through to daily capacity floor prices which are set in relation to cleared prices in the monthly auctions.

10. The implications of implementing the Modification Proposal for Terminal Operators, Consumers, Connected System Operators, Storage Operators suppliers, producers and, any Non-Network Code Party:

Users that book monthly capacity at a storage site would provide Storage Operator's with a medium term signal of their intentions where previously capacity booking had been based entirely on the purchase of daily capacity.

11. Consequences on the legislative and regulatory obligations and contractual relationships of Transco and each User and Non-Network Code Party of implementing the Modification Proposal:

No significant consequences on the legislative and regulatory obligations and contractual relationships of Transco and each User and Non-Network Code Party are anticipated as a result of implementation of this proposal.

12. Analysis of any advantages or disadvantages of the implementation of the Modification Proposal:

Advantages :

- Users would have the opportunity to purchase a greater proportion of their System Entry Capacity needs as MSEC and reduce the amount of System Entry Capacity purchased as Daily System Entry Capacity (DSEC).

- Users of all ASEPs would have the opportunity to bid for some of their capacity needs as MSEC as opposed to having to rely exclusively on the purchase of daily capacity services.

Disadvantages :

There would be a greater probability of buy back of entry capacity being required where increased MSEC capacity leads to nominations at levels beyond physical flow capability.

13. Summary of the Representations (to the extent that the import of those representations are not reflected elsewhere in the Modification Report):

Transco received twenty one representations on the Modification Proposal.

In its present form the proposal received support from the following eighteen respondents :

Agip (UK) Limited	(AGIP)
Alliance Gas Limited	(AGL)
Aquila	(Aq)
Association of Electricity Producers	(AEP)
British Gas Trading Limited	(BGT)
Claims Validation Services Limited	(CVSL)
Elf Gas and Power Limited	(ELF)
Enron	(En)
National Power	(NP)
Powergen	(PG)
Quantum Gas Management	(QGM)
Scottish and Southern Energy Limited	(SSE)
Scottish Power	(SP)
Shell Gas Direct	(SGD)
Shell UK Limited	(SUK)
TXU Europe Energy Trading	(TXU)
UK Offshore Operators Association	(UKOOA)
Yorkshire Energy	(YE)

BP Amoco (BP) withheld support, but offers a proposal that the quantity of MSEC should be increased to SND +15%. Conoco (Co) remains concerned that the present allocation methodology discriminates between ASEPs and that a 10% increase is arbitrary. Amerada Hess (AH) has withheld support out of principle because they see a link between this proposal and Modification Proposal 0382, which proposes a revision to the capacity incentive arrangements.

A number of specific issues were discussed which for clarity have been summarised below under the following headings.

i. Quantities
ii. Allocation Proposal
iii. Allocation Parameters
iv. Audit
v. Direct flows to LDZ.
vi. LDZ Entry Points

<u>Quantities</u>

In general most respondents welcome proposals to increase MSEC availability.

BP proposes that the availability should be increased further to SND +15% and BGT is of the opinion that availability could be increased to SND +20%. A number of respondents are of the opinion that further increases may be warranted prior to future auctions.

En welcomes the increase but cautions against any further increases which, in its opinion, would represent a move to the previously rejected "top down" model. In particular, concern was expressed that a significant increase in MSEC availability towards 1 in 20 peak demand levels may expose both Transco and the shipping community to extreme buy-back costs.

The CVSL indicates that, if implemented, Modification Proposal 0380 would enable Users to more readily align capacity holdings to gas entry flows such that the level of materially under-claimed sub-terminal days would revert to a more acceptable level.

Co does not support the proposal in its current form because a 10% increase is viewed as arbitrary and the allocation methodology, being historically based, did not provide an efficient allocation between ASEPs.

Allocation Proposal

Four respondents, Aq, QGM, SP and SSE support the proposed revision to the Network Code to enable MSEC to become available at all ASEPs from April 2000.

The proposed method to allocate MSEC to non-beach ASEPs is not supported by four respondents, En, SGD, UKOOA and BGT. BGT and En doubt if there is any need for MSEC at such locations, particularly in the summer months. They go on to argue that purchasing MSEC capacity for storage sites is not economic and potentially diverts capacity from ASEPs where it is required for beach gas. En, whilst recognising that the present methodology is imperfect, is never the less of the opinion that the historically based methodology appears to be intuitively acceptable.

Allocation Parameters.

Three respondents, Co, QGM and SSE draw attention to their difficulty in commenting upon the proposed x and y parameters because it is not clear how they are derived.

SSE comments that they would prefer not to see a weighting of capacity to terminals. UKOOA believes that a prescriptive approach based on arbitrary x and y parameters cannot be regarded as a Network Code development which will help to resolve the issue of MSEC being unavailable at onshore storage sites. UKOOA's preference is to retain the methodology contained in Modification Proposal 0363 (Capacity Transfers to ASEPs without Monthly System Entry Capacity) on an interim basis until an appropriate long term solution can be developed.

Audit

A number of respondents, including Aq, BP, SUK and SSE, are supportive of the proposal but would wish for a full review or audit of the methodology used to determine the volume of MSEC prior to October 2000. It is suggested that an independent audit of the SND methodology would help the capacity planning aspect of Transco's business and consequently tie in with long term investment signals.

Direct flows to LDZ

BGT proposes that ASEPs that input gas directly into an LDZ should automatically be allocated a quantity of monthly capacity to match their input flows. However, it is suggested that this capacity will not directly impact on the NTS and so it should not be included with the aggregate MSEC quantity (SND +10%) released elsewhere.

LNG Entry Points

In a similar proposal to that made above, En suggests that given the location of LNG facilities, any allocation to such facilities should be in addition to SND +10%. This should be possible because capacity provision at LNG facilities should not alter the likelihood of Transco needing to buy back or sell beach entry capacity.

Transco Response:

Transco welcomes the high level of support for this proposal which will increase MSEC to SND plus 10%. Transco's comments regarding each of the discussion areas are provided below.

Quantities

Transco agrees with the AEP that the proposal to increase MSEC quantities should result in lower average clearing prices and a reduced level of uncertainty and risk for Users. The lower average prices, if achieved, will carry over to floor prices for daily capacity.

Any increases in MSEC quantities do, however, need to be balanced against increasing risk of buy back costs that would be incurred by Transco and Registered MSEC holders. Whilst a number of respondents have highlighted the absence of buy back activity for the present allocation of capacity, such knowledge provides little guidance as to the level of capacity which represents the buy back threshold at each ASEP. For this reason Transco supports a measured, if somewhat arbitrary, change to MSEC availability in the forthcoming auctions. The consequence of such activity is to progressively increase availability whilst limiting industry exposure to extreme and widespread buy back.

Allocation Proposal

Transco accepts the view put forward by a number of respondents that MSEC may not be the most economic solution for Users that require entry capacity at non beach locations. However, the demand for Modification Proposal 0363 has demonstrated that other less tangible values, such as certainty, may figure in the calculations of Users. For this reason Transco has put forward a proposal that allows Users to take up the option of bidding for quantities of MSEC at all ASEPs should they so desire. Contained within Modification Proposal 0371, which is being considered with the same timetable as this proposal, is the facility for capacity remaining unsold to be offered for use at other locations in a fifth auction round.

Allocation Parameters

The outcome of the present methodology was that MSEC was allocated to the major beach entry points, with little or nothing allocated to smaller ASEPs. This led to a situation during the October 1999 auctions where Users expressed a desire to obtain MSEC at smaller ASEPs, which the methodology prevented. The proposed new methodology for allocating MSEC, including the parameters, has been devised to ensure that all ASEPs will receive an allocation of MSEC. Transco accepts that the x and y parameters are arbitrary but maintains that such an arbitrary mechanism is required if a threshold is to be created below which a limited allocation can be made. In devising the methodology Transco has not sought to discriminate between the roles which various ASEPs are understood to play with regard to gas provision.

Audit

Transco recognises that an independent audit of Transco’s methodology for determination of MSEC quantities was discussed prior to the determination of the methodology introduced in September 1999.

Transco believes that, to a large extent, the use of SND as the basis for capacity availability negates the need for such an audit. Transco calculates SND for a number of activities and manipulation in one area is likely to have adverse effects on other areas of the Network Code.

Direct Flow to LDZ.

At present the ASEPs that flow gas directly into an LDZ are Caythorpe, Wytch Farm and the boil-off facilities at each LNG site. Whilst no physical constraint is likely to exist when introducing gas on to the system from each of these locations, it is equally likely that aggregate gas flow at these and any other ASEP could be combined to satisfy local demand which may consequently drive entry constraints at other ASEPs. For this reason Transco is of the opinion that quantities at all ASEPs should be counted towards the aggregate quantity on offer.

LNG Entry Points

Transco does not agree that the likelihood of buy back or sales of capacity at beach ASEPs is unaffected by the sale of MSEC at LNG facilities. The high delivery capability of most LNG facilities ensures that there is a reasonable probability that on high demand days, when LNG is introduced to the system, the transportation capability from beach to the locality of the LNG facility will consequently be reduced. On days of widespread high demand it may be expected that the displaced beach supplies will be diverted to other destinations. However, on days of localised supply or demand difficulties then deliverability at beach entry points may be reduced.

14. The extent to which the implementation is required to enable Transco to facilitate compliance with safety or other legislation:

Implementation is not required to facilitate compliance with safety or other legislation.

15. The extent to which the implementation is required having regard to any proposed change in the methodology established under Standard Condition 3(5) of the statement; furnished by Transco under Standard Condition 3(1) of the Licence:

No such change to the methodology is anticipated in respect of the modification proposal.

16. Programme of works required as a consequence of implementing the Modification Proposal:

No additional programme of works would be required as a consequence of implementing the proposal.

17. Proposed implementation timetable (inc timetable for any necessary information systems changes):

It is anticipated that the proposal would be implemented in time for the next auctions of MSEC commencing on 6 March 2000.

18. Recommendation concerning implementation of the Modification Proposal:

Transco recommends that this Modification Proposal is implemented.

19. **<u>Restrictive Trade Practices Act</u>**:

If implemented this proposal will constitute an amendment to the Network Code. Accordingly the proposal is subject to the Suspense Clause set out in the attached Annex.

20. **<u>Transco's Proposal</u>:**

This Modification Report contains Transco's proposal to modify the Network Code and Transco now seeks direction from the Director General in accordance with this report.

21. **<u>Text:</u>**

SECTION B: SYSTEM USE AND CAPACITY

Amend paragraph 2.2.2 to read as follows:

"….the "**Determined System Entry Capacity**" is:

(a) unless paragraph (b) applies, the ASEP Estimated System Entry Capacity as adjusted (if appropriate) pursuant to paragraph 2.2.5;

(b) where this paragraph 2.2.2(b) applies pursuant to paragraph 2.2.10:

(i) for any Shortfall Aggregate System Entry Point, the sum of:

(1) the Mandatory ASEP System Entry Capacity; and

(2) the ASEP Estimated System Entry Capacity as adjusted (if appropriate) pursuant to paragraph 2.2.5(a) for which purposes an adjustment will only be made where the Aggregate Estimated System Entry Capacity differs from 100 less the Relevant Percentage (expressed a percentage) of 1.1 * SND (where SND is the System Normal Demand for the relevant calendar month);

(ii) for any other Aggregate System Entry Point the ASEP Estimated System Entry Capacity determined in accordance with the paragraphs 2.2.4, 2.2.5 (and for the purposes of paragraph 2.2.5(a) the rule in this paragraph 2.2(b)(i)(2) shall apply), 2.2.6 and 2.2.8

in each case as set out in the Transportation Statement.

Amend paragraph 2.2.4 to read as follows:

"PR ….for the Gas Year (the "**ASEP Peak Flow Forecast**").".

Amend paragraph 2.2.5(a) to read as follows:

"without prejudice to paragraph 2.2.2(b)(i)(2) or (ii), the Aggregate Estimated System Entry Capacity differs from 110% of System Normal Demand for such calendar month….".

Add new paragraphs 2.2.10, 2.2.11 and 2.2.12 to read as follows:

"2.2.10 Where in relation to any Aggregate System Entry Point for any calendar month the ASEP Estimated System Entry Capacity determined in accordance with paragraphs 2.2.4, 2.2.5(a), 2.2.6(a) and 2.2.7, but not paragraph 2.2.8, is less than the Relevant Percentage of the ASEP Peak Flow Forecast (a "**Shortfall Aggregate System Entry Point**") the Determined System Entry Capacity for any Aggregate System Entry Point will be determined in accordance with paragraph 2.2.2(b).

2.2.11 In respect of a Shortfall Aggregate System Entry Point for any calendar month:

(a) the "**Mandatory ASEP System Entry Capacity**" shall be:

$$AMSC * (APR / AAPR)$$

where for the relevant calendar month:

AMSC is the Aggregate Mandatory ASEP System Entry Capacity;

APR is Peak Flow Forecast for the Shortfall Aggregate System Entry Point; and

AAPR is the aggregate of the Peak Flow Forecast for each Shortfall Aggregate System Entry Point;

(b) for the purposes of paragraph (a), the "**Aggregate Mandatory ASEP System Entry Capacity**" shall be:

$$RP * (1.1 * SND)$$

where:

RP is the Relevant Percentage;

SND is the System Normal Demand for the relevant calendar month.

2.2.12 The "**Relevant Percentage**" for the purposes of:

(a) paragraph 2.2.10, is [5] %; and

(b) paragraphs 2.2.2(b)(i)(2) and 2.2.11(b), is [3] %.".

Signed for and on behalf of Transco.

Signature:

Tim Davis
Manager, Network Code

Date:

<u>Director General of Gas Supply Response</u>:

In accordance with Condition 7 (10) (b) of the Standard Conditions of Public Gas Transporters' Licences dated 21st February 1996 I hereby direct Transco that the above proposal (as contained in Modification Report Reference **0380**, version **2.0** dated **28/02/2000**) be made as a modification to the Network Code.

Signed for and on behalf of the Director General of Gas Supply.

Signature:

The Network Code is hereby modified, with effect from , in accordance with the proposal as set out in this Modification Report, version **2.0.**

Signature:

Process Manager - Network Code
Transco

Date:

ANNEX

Restrictive Trade Practices Act - Suspense Clause

For the purposes of the Restrictive Trade Practices Act 1976, this document forms part of the Agreement relating to the Network Code which has been exempted from the Act pursuant to the provisions of the Restrictive Trade Practices (Gas Conveyance and Storage) Order 1996. Additional information inserted into the document since the previous version constitutes a variation of the Agreement and as such, this document must contain the following suspense clause.

1. Suspense Clause:

1.1 Any provision contained in this Agreement or in any arrangement of which this Agreement forms part by virtue of which this Agreement or such arrangement is subject to registration under the Restrictive Trade Practices Act 1976 shall not come into effect:

(i) if a copy of the Agreement is not provided to the Director General of Gas Supply (the "Director") within 28 days of the date on which the Agreement is made; or

(ii) if, within 28 days of the provision of the copy, the Director gives notice in writing, to the party providing it, that he does not approve the Agreement because it does not satisfy the criterion specified in paragraph 2(3) of the Schedule to The Restrictive Trade Practices (Gas Conveyance and Storage) Order 1996.

provided that if the Director does not so approve the Agreement then Clause 1.2 shall apply.

1.2 Any provision contained in this Agreement or in any arrangement of which this Agreement forms part by virtue of which this Agreement or such arrangement is subject to registration under the Restrictive Trade Practices Act 1976 shall not come into effect until the day following the date on which particulars of this Agreement and of any such arrangement have been furnished to the Office of Fair Trading under Section 24 of the Act (or on such later date as may be provided for in relation to any such provision) and the parties hereto agree to furnish such particulars within three months of the date of this Agreement.