

Draft Modification Report
Proposal to allow for RbD Adjustments to be processed consequent to the
recalculation of LDZ Specific Shrinkage Factors for revised temperature data for
the period from the implementation of RbD to the start of current Supply Year
1999/2000
Modification Reference Number 0396
Version 2.0

This Draft Modification Report is made pursuant to Rule 8.9 of the Modification Rules and follows the format required under Rule 8.9.3.

1. The Modification Proposal

The Original Proposer's Statement was as follows:

The relevant paragraphs of the current Section N should be amended in consultation with the Planning and Security and RbD Workstreams to remove any doubt as to whether more than one reconciliation of LDZ Shrinkage for a single Gas Year after the event is permitted. The current rules are designed to allow for RbD adjustments to be processed to correct from the estimated LDZ Shrinkage factors set prior to the Gas Year to those assessed after the year has been completed. They have also been used to process other corrections, but not for earlier periods. The intention is that the retrospective adjustment required for this Modification should be passed through the RbD adjustment mechanism based on appropriate market shares during the 20 month period covered in line with proposals for such one-off adjustments embodied in Modification 0327.

It is currently planned to implement the new domestic temperature data in a number of phases as improved figures become progressively available, thereby necessitating potentially a number of retrospective adjustments. The target is to agree the initial domestic temperatures to be used based on both the 1999 DMTS and the 2000 DMTS by 1st July 2000. Prospective application will then be deferred until the start of the new Gas Year on 1st October 2000, as any adjustments for the 1999/2000 Gas Year can be included in the normal annual reconciliation process early next year. This Modification should facilitate the retrospective adjustment linked to these initial temperatures.

The second phase, which may trigger further adjustments, is currently planned to relate to a review of the assumed internal/external split of domestic meters, and will be based on work to be undertaken for Transco by the Meter Reading Agencies. Further adjustments may then be required when the results of the 2001 DMTS, which will be based on an expanded sample of domestic meters, become available and possibly again in the future as further data improvements are defined. At an

appropriate time a line will be drawn on retrospective adjustments related to this matter.

The Modification Panel requested that the Invoicing and Adjustment Workstream develop a billing methodology to support the proposal, and to report this back to the Panel. The RbD Sub-Group of this Workstream, at its meeting on 5 May 2000, discussed the issues and asked Transco to prepare a suggested billing and assessment methodology for a specific meeting in which Transco arranged for 24 May 2000. Prior to this meeting all Workstream attendees were invited to submit representations and one was received from TXU. The meeting on 24 May 2000 discussed:

Billing Methodology

Transco tabled the Billing Methodology, which is attached to this report as Appendix 1. The meeting agreed that separate billing adjustments should be made for each Gas Year and the period from 1 February 1998 (the first day of RbD) to 30 September 1998. Transco clarified that this methodology would ensure that month by month changes in shippers' portfolios would be tracked, but the same revised LDZ shrinkage factors would apply to each month of the Gas Year concerned. Transco stated that this underlying methodology of RbD adjustments had been audited for conformance with the Network Code. The meeting therefore accepted Transco's proposed Billing Methodology.

Assessment Methodology

Transco also presented its proposed assessment methodology. This showed how the results of Domestic Temperature and other surveys planned or already conducted by Transco, up to and including the 2001 Domestic Temperature Survey (DMTS) could be embodied in the adjustment processes.

As part of the presentation Transco outlined the manner by which LDZ shrinkage factors calculated on the basis of Initial Data (I&C) could be refined on the basis of:

The 1999, 2000 and 2001 DMTS

The planned internal/external meter location survey

Arising from this, the main issues discussed within the Workgroup were as follows:

Robustness of Transco's gas temperature data

Need for one or several billing adjustment cycles

Adjustment orders of magnitude (in terms of energy) for each LDZ

Need for “close-out” so that adjustments retrospective from the first day of RbD are not carried out indefinitely

(i) Robustness of Transco’s gas temperature data

The LDZ Shrinkage Forum had been engaged in agreeing the philosophy for obtaining and processing representative temperature data. The 2001 DMTS plus the survey of external vs internal meter locations was intended to give a high level of confidence in the data obtained and its applicability to the entire Domestic Supply Point population. Some shippers, however, continued to be concerned about lack of representation of the 2000/01 data set. This could potentially be resolved as data sets from successive years are reviewed for convergence. It was therefore agreed that the LDZ Shrinkage Forum was the appropriate body to continue to review survey activity and to discuss any concerns that shippers may have on robustness of data and sampling plans.

(ii) Need for one or several billing adjustment cycles

The meeting agreed that there was a need to balance the shippers’ administrative load of carrying out more than one adjustment against the requirements of maintaining consequent cash flows to shippers, which would indicate adjustment at the earliest possible stage. The solution agreed, therefore, was to consider billing adjustments as soon as the data has been processed from each survey, which is potentially three separate adjustments. The meeting felt, however, that where Transco believed that any of these adjustments were minor it should consult with the LDZ Shrinkage Forum with a view to incorporating the adjustment concerned with the one that follows. This would essentially maintain shippers’ rights of consultation.

(iii) Adjustment orders of magnitude

Transco had not carried out shipper by shipper adjustment calculations but, based upon the first DMTS results, tabled adjustment estimates on an LDZ basis from which shippers could estimate their likely adjustments. One of the shippers had previously calculated similar values, which showed adjustments on a whole LDZ basis varying from –0.4 TWh to 0.6 TWh. The meeting concluded that the proposed billing and adjustment cycle methodologies were appropriate for the scale of adjustments likely to be involved.

(iv) Need for close-out

Whilst all the meeting attendees recognised that at some stage it would be necessary to close-out the first Gas Years of RbD, there was a reluctance to decide at this point when that stage would be reached. It was agreed that a decision on close-out should be taken after discussion by the LDZ Shrinkage Forum and that this should form part of Transco's ongoing consultation process. The parties concerned would in these circumstances also take comfort in Ofgem's ability to veto proposals within the domestic arena.

2. Transco's Opinion

Transco supports the basic principles behind this Modification Proposal and has developed a billing methodology that allows it to be implemented in practice. Transco believes that further work is required within the appropriate forum to refine the adjustment principles. This will ensure that the consequential billing adjustments are scheduled in a way that recognises the balance to be struck between maintenance of cash-flow to shippers and the minimisation of administrative costs.

Transco supports the view that a decision has to be made on closing out the billing adjustments for the initial years of RbD. It proposes, therefore, that following the implementation of the 2001 DMTS results, no further adjustments should be made, other than those already covered within the main body of the Network Code. This will not prevent any party to the Network Code proposing a Modification if it becomes clear, for example, that there has not been the expected convergence of data as each subsequent DMTS phase is conducted.

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

The initial setting of LDZ Shrinkage Factors, whilst reflecting the best information available at the time, nevertheless resulted in charges among Shippers within the Reconciliation by Difference (RbD) processes which did not totally reflect the charges which would have resulted from more accurate temperature weighting of LDZ Shrinkage Factors. Modification Proposal 0396 seeks to make these charges more cost reflective by retrospective adjustments on the basis of subsequent information received. Such improvement in cost reflectivity of charging would be expected to enhance competition amongst Shippers.

This Modification Proposal therefore facilitates the following relevant objective:

Condition 7 (1) (b) *".....the efficient discharging of its obligations under this licence"*

In this case the most relevant obligation is the requirement for cost-reflective charging.

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

a) implications for the operation of the System:

As the Modification Proposal seeks to amend reconciliation processes Transco is not aware of any implications on the daily operation of its Transportation System.

b) development and capital cost and operating cost implications:

The major costs for Transco is in the execution of any necessary field surveys such as the Domestic Temperature Surveys and the survey of external vs internal meter box populations.

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:

Transco has agreed to fund the present programme of surveys and the other associated costs from existing revenue.

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

Transco is unaware of any such consequence

5. 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 is unaware of any such consequence

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

Transco's computer systems and related processes are already set up to undertake reconciliation for a whole Gas Year as a result of an LDZ Shrinkage Adjustment. This Modification Proposal extends the period without amending the underlying methodology. The implications are therefore limited to changes in system parameters which are readily achieved at minimal cost. Transco would expect that the implications for Users would be limited to amendments to their invoice validation systems

7. The implications of implementing the Modification Proposal for Users

Essentially this Modification Proposal would achieve a reapportionment of existing charges among the RbD Users through one or more reconciliation processes.

8. The implications of implementing the Modification Proposal for Terminal Operators, Consumers, Connected System Operators, Suppliers, producers and, any Non-Network Code Party

Users may wish to reflect these adjustments in charges in the prices they charge domestic consumers.

9. 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

Transco is not aware of any such consequences

10. Analysis of any advantages or disadvantages of implementation of the Modification Proposal

Advantage

Corrects any inaccuracies in previous charges apportioned amongst RbD Users

Disadvantage

Additional systems and administrative work-load for Transco and RbD Users

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

TXU has made two submissions which are attached in full as Appendix 3:

Submission 1 11th May 2000

Whilst not opposing the principle of the Modification Proposal TXU had significant issues with the Proposal as originally drafted. In particular TXU believed that:

A special "pot" may be required for the retrospective adjustment through RbD, and did not believe that the current methodologies as drafted for Modification 327 met the need.

A single adjustment should be processed not several adjustments in respect of the same period as seems to be indicated in the current drafting, this may mean a delay in processing.

The modification should also include a provision to "close out" a shrinkage period, for example, in the same way that invoices become final after 18 months.

It shared the concerns of other Shippers as to the robustness of the new temperature data, particularly in respect of the internal/external split and the geographical distribution of the sample.

Submission 2 22 June 2000

Subsequent to the June Modification Panel, TXU made a further submission expressing some concerns with the Workstream Report :

TXU repeated its main concerns that:

- a) Repeated adjustments in respect of the same period, could possibly result in complete reversals of positions
- b) No close-out of the provisions
- c) Billing and adjustment methodologies not included, need to be consulted upon
- d) Robustness of the DMTS
- e) Once Modification Proposal 0396 is agreed, there will be no check on future adjustments flowing

Transco Position

Transco believes that it has been clear on the phasing of retrospective adjustments. It has agreed that members of the appropriate forum should be consulted on whether adjustments should be done piecemeal or only once (at the completion of the 2001 DMTS) or whether an intermediate position of say combining two adjustments is the optimum. This is a billing methodology issue that does not need to be incorporated as revised legal text in the Network Code.

Transco has, however, included the billing and adjustment methodologies as part of this report. These methodologies are in accordance with the Network Code. Transco has no plans at present to conduct a 2002 DMTS. The need and the finance for any future surveys will be discussed within the appropriate forum.

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

This Modification Proposal is not required to facilitate compliance with safety or other legislation.

13. The extent to which the implementation is required having regard to any proposed change in the methodology established under Standard Condition 4(5) or the statement furnished by Transco under Standard Condition 4(1) of the Licence

This Modification Proposal is not required as a result of any change in the methodology established under Standard Condition 3(5) of its PGT Licence.

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

Calculate LDZ Shrinkage Factors when the results of each survey are available
Calculate billing adjustment quantities and make recommendation to the appropriate forum on implementation of the adjustments

As a result of consultation with the appropriate forum Transco either implement the billing adjustment or carry over the adjustment until the billing adjustments from the next survey are available

Repeat until the 2001 DMTS adjustments are made

15. Proposed implementation timetable (including timetable for any necessary information systems changes)

The timetable would be set by the approval of this Modification Proposal and by the dates at which the results of each survey can be discussed at the LDZ Shrinkage Forum, which at present meets monthly.

16. Recommendation concerning the implementation of the Modification Proposal

Transco recommends that this Modification Proposal be implemented as soon as possible

17. Text

Representations are now sought in respect of this Draft Report and prior to Transco finalising the Report

Signed for and on behalf of Transco.

Signature:

Tim Davis
Manager, Network Code

Date: