

Modification Report
URGENT Modification Reference Number 0203

'Manage the effects of inappropriate AQs resulting from the 1997 AQ Review Process'

This Modification Report is made pursuant to Rule 9 of the Modification Rules and follows the format required under Rule 8.12.4.

1. Circumstances Making this Modification Proposal Urgent:

In accordance with Rule 9.2(a) Ofgas has agreed that this Modification Proposal should be treated as Urgent to allow Shippers sufficient time to appeal erroneous AQs before the proposed extended deadline of 31 January 1998.

2. Procedures Followed:

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

- 17/12/97 - Modification Proposal forwarded to Ofgas
- 23/12/97 - Ofgas agreed Modification should be treated as Urgent
- 23/12/97 - Urgent Modification Proposal circulated to Shippers inviting representations
- 9/1/98 - Close out for representations 4pm
- 14/1/98 - Draft Modification Report to Ofgas
- 27/1/98 - Response from Ofgas on Draft Modification Report
- 3/2/98 - Final Modification Report to Ofgas
- 24/6/98 - Revised Final Modification Report to Ofgas
- 26/6/98 - Direction expected from Ofgas
- 26/6/98 - Implementation date

3. The Modification Proposal:

The 1997 AQ Review Process revised some AQs to materially erroneous values. This resulted in some anomalous increases in NTS and LDZ Capacity charges for certain Shippers from 1st October 1997. In some cases, Commodity charges were also temporarily affected. Due to the number of AQs requiring investigation and correction, some erroneous AQs may not be corrected until 1998. Until then, some Transportation Charges may continue to be inappropriately inflated.

Review Group 0121 was re-convened to consider ways in which anomalous Transportation Charges could be corrected and erroneous AQs revised to more appropriate values. Proposals were developed and circulated to the industry on 26th November 1997. In order to formalise these arrangements, Modification 0203 was proposed. This Modification proposes the following changes to the Network Code:

1. To enable Shippers to withhold an amount, calculated by Transco, from their October 1997 to January 1998 (inclusive) Capacity invoices (against NNX,

CCA and ZCA charge types only). This amount to be based on the difference between the invoice values for Shippers October 1997 to January 1998 Capacity invoices and their September 1997 Capacity charges, adjusted for the price changes that occurred on 1st October 1997.

2. On or after 1st March 1998, Transco to recalculate each Shippers NTS and LDZ Capacity charges for the months of October 1997 to January 1998 inclusive, based on the AQs that apply as at 1st March 1998.
3. Following this recalculation, Transco to issue an adjustment invoice for the amount owing to, or payable by the Shipper. This amount to attract interest at Base Rate + 1%.
4. For those Shippers whose total NDM output allocation increased by more than 40% from 30th September 1997 to 1st October 1997, Transco will calculate an amount that may be withheld from that Shippers October 1997 Commodity invoice. This amount will be payable with the November 1997 Commodity invoice.
5. To extend the appeals window to 31st January 1998.
6. Following discussion, it was identified that some Shippers may have experienced temporary difficulties in re-nominating and confirming successful AQ appeals. It was therefore proposed to extend the deadline for Shippers to reconfirm revised AQs for inclusion in the Capacity adjustment. The revised deadline was for AQs reconfirmed with an effective date of 6th March 1998. These proposals were circulated to the industry on 6/2/98 and Transco agreed to revise Modification proposal 203 accordingly. A copy of the letter circulated to Shippers is attached.

Further to this extension, it was recognised that there were concerns that some AQ appeals may have been inappropriately rejected, or that the AQ value offered by Transco following a successful appeal may have been inappropriate. In order to remedy these concerns, Transco proposed to re-open the appeals window for a limited period, to allow AQs in these two categories to be re-appealed. It was proposed that any AQs successfully appealed during this additional window would be included in the Capacity adjustment for October 1997 to January 1998 inclusive, where they were re-confirmed with an effective date of 30th June or earlier. Transco circulated its proposal on this additional appeals window on 7th April 1998 (copy attached).

7. In respect of DM interruptible Supply Points and their Bottom-Stop SOQs, to extend the transitional arrangements.

4. **Transco's opinion:**

The primary objective of this modification is to mitigate the effects of materially erroneous AQs that resulted from the 1997 AQ update process. Without this

modification, any capacity charges that have been inappropriately inflated as a result of erroneous AQs will not be rectified and Shippers may be financially disadvantaged. Furthermore, the extension to the appeal window proposed by this Modification enabled Shippers to appeal all those AQs they believed were incorrect.

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

This modification will minimise the impact erroneous AQs may have had on the Shipping Community and allow the majority of these errors to be corrected. Accurate AQs not only assist Transco in facilitating the relevant objectives of operating an efficient and economic system but are an important factor in the smooth operation of the competitive market.

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

a) **implications for the operation of the System and any BG Storage Facility:**

Transco is not aware of any such implications.

b) **development and capital cost and operating cost implications:**

Implementation of this Modification will involve Transco in significant administrative costs and some limited systems development costs associated with the adjustment process.

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:**

Subject to the outcome of Modification 197, 'Recovery of Extraordinary Costs Incurred due to Erroneous AQs', Transco believes that the costs to Transco will be treated as ordinary business costs, being dealt with via the formula.

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

Transco is not aware of any impact on price regulation.

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:**

This Modification reduces the risks to both Transco and Shippers of inaccurate AQs and any inappropriate Transportation charges that may be derived from them.

8. **The development implications and other implications for computer systems of Transco and related computer systems of Relevant Shippers:**

Minimal changes will be required to Transcos computer systems to facilitate the adjustment process for Capacity charges. Transco is not aware of any implications on the computer systems of Relevant Shippers.

9. **The implications of implementing the Modification Proposal for Relevant Shippers:**

Shippers whose Capacity charges were inappropriately inflated due to erroneous increases in AQs were able to pay reduced capacity charges for the months of October 1997 to January 1998 inclusive.

For those Shippers whose NDM output allocations increased by more than 40% between 30th September and 1st October 1997, there was an opportunity to defer payment of an element of their October Commodity charges until the due date for their November Commodity charges.

The extension of the appeal window to 31st January 1998 provided Shippers with an additional month in which to appeal AQs. Furthermore, the additional appeal window, available from 7th April to 20th April 1998, enabled Shippers to re-appeal AQs they believe may have been inappropriately rejected, or those where the Shipper could demonstrate that there was a manifest error in the AQ offered by Transco following the original appeal.

10. **The implications of implementing the Modification Proposal for terminal operators, suppliers, producers and, any Non-Network Code Party:**

Transco is not aware of any such implications.

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

Transco is not aware of any such consequences.

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

Advantages - The modification will ensure that Shippers are not subject to inappropriate Transportation charges resulting from potentially erroneous AQs. It will also ensure that there is sufficient time for Shippers to review their revised AQs and correct them where appropriate.

Disadvantages - Transco gave significant commitment to this process to facilitate the successful implementation of the requirements as developed by the industry. For the process to work successfully, Shippers were equally required to commit resources not only to appeal AQs before 26th January, but in addition to renominate and confirm

successful appeals with effective dates prior to 6th March 1998, so that they are included in the adjustment of capacity charges undertaken by Transco.

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

6 representations have been received for Modification 0203.

Representations were received from BGT, Mobil, Eastern Natural Gas, BP Gas Marketing, United and Reephram. All 6 Shippers were supportive of the Modification in principle. However, 5 Shippers raised issues with the detail of the proposal.

One Shipper identified a concern with the legal drafting relating to the extended appeal window, where they considered the wording as drafted would apply to all years, not just the 1997 process. Transco agrees that this was an error and has revised the legal text accordingly. A further Shipper identified two concerns with the legal drafting. The first related to the text on invoice queries relating to the amounts withheld from the four capacity invoices, which they felt implied that no invoice queries would be allowed relating to inappropriate AQs. This provision is intended to apply only to queries against the amounts that Shippers are initially able to withhold against their October '97 to January '98 Capacity invoices. It is not intended to prevent any queries against the subsequent adjustment invoices that will be produced after the 1st March '98. Transco agrees that this was not fully clear and has amended the legal text to address this. The second issue raised related to some ambiguity over the payment date for withheld Commodity charges. Transco has amended the paragraph numbering to remove any ambiguity.

Whilst supportive of the principles contained in the Modification, two Shippers suggested these proposals should be extended. One Shipper stated that the Modification should include proposals for remedying additional costs incurred in respect of Energy Balancing charges as a result of erroneous AQs. A second Shipper believed that the facility for withholding specified amounts from October's Commodity invoice should be extended to November's invoice and that payment should not be required until reconciliation items had been cleared. Modification 0203 reflects the proposals that were developed and agreed with Shippers at a series of meetings held during the latter part of 1997 and circulated to the industry on 26th November. The impact of inflated AQs on Energy Balancing has been discussed extensively by the Energy Balancing Credit Committee. Following their statement, issued in November, the Committee has clearly demonstrated its ability to handle the individual cases where Shippers have been financially impacted by the AQ process. Therefore Transco does not believe it is necessary to incorporate Energy Balancing issues within this Modification. Where issues have arisen, they have been adequately dealt with through current Network Code processes. For Commodity charges, Transco offered Shippers the facility to submit customer reads to force early reconciliation. In addition, Transco has been pro-actively identifying items that are in the reconciliation suppressed pot but which have been successfully appealed and is releasing these items to the subsequent reconciliation invoice.

One Shipper also identified a problem with Transco providing offer files. This problem has now been resolved and Shippers have been advised. Transco do not believe that this issue would have had a material effect on Shippers' ability to correct AQs.

One further Shipper stated that they believed it was necessary to include an end-date for the adjustment process. This was discussed, however Transco have concerns about including an end-date as the timescales will be dependant upon the volume of adjustment required. The adjustment has now been further delayed by the additional appeal window offered by Transco on 7th April 1998.

Two Shippers stated that BSSOQs remained an issue in the longer term. Transco recognises these concerns. This issue will be taken to the appropriate Workstream for discussion as to the longer term industry requirements.

One Shipper raised concerns that AQs had not been derived from Valid Meter Reads and questioned whether the issues addressed by this Modification should have been resolved through individual Shippers liaising directly with Transco. However, Transco has previously stated that AQs were derived using the processes as defined in the Network Code. Furthermore, Transco firmly believes, and has agreed with Shippers, that these issues are appropriately resolved through common and transparent processes.

One Shipper stated that it was not clear from the modification proposal that for appealed AQs to be included in the adjustment process, they were required to be re-nominated and confirmed with an effective date of 28th February 1998. Transco believes that this was clear from the original modification proposal and is reflected in the legal drafting.

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

Not applicable.

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:

None.

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

1. Transco to calculate and advise to Shippers the amount that may be withheld from Capacity invoices for October, November, December and January 1998

2. Recalculation of Capacity Charges that should have been applied for each of those four months, in respect of those AQs that have been successfully appealed and reconfirmed by 6th March 1998.
3. Recalculation of Capacity Charges for AQs successfully appealed during the additional appeal window from 7/4/98 to 20/4/98 and reconfirmed with an effective date no later than 30th June.

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

This Modification should be implemented with an effective date of 1st October 1997.

18. Recommendation concerning the implementation of the Modification Proposal:

Transco recommend that the modification is implemented on 5th May 1998, such that the effective date for changes is 1st October 1997.

19. Restrictive Trade Practices Act:

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. Transco's Proposal:

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. Text provided pursuant to Rule 9:

To be inserted in Transition Document Part II, Paragraph 7:

Amend paragraph 7.9.1:

"....subject to paragraph 7.9.7,....".

Amend paragraph 7.9.3:

"Subject to paragraph 7.9.7,....".

Add new paragraph 7.9.4:

7.9.4 Subject to paragraph 7.9.7, where following a notification under Section G1.6.8(a) the Registered User reasonably considers that:

(a) a material error has been made by Transco in revising the Annual Quantity; or

(b) Transco should have agreed to revise the Annual Quantity but did not the Registered User may, between 7th and 20th April 1998, renotify Transco that the User considers that the Annual Quantity of the relevant Supply Meter Point still substantially fails to satisfy the requirement in Section G1.6.9."

Renumber existing paragraph 7.9.4 as 7.9.5 and amend:

"In relation to any such notification as is referred to in paragraph 7.9.3 or any such renotification as is referred to in paragraph 7.9.4...."

Add: new paragraph 7.9.6:

"7.9.6 In relation to any such renotification as is referred to in paragraph 7.9.4:

- (a) for the purposes of the estimate of the quantity which the User considers should be the Annual Quantity, the User shall base such estimate on a quantity derived from two Meter Reads (details of which it shall provide to Transco) for which the Meter Read Dates are not less than six months apart (provided that the second such Meter Read Date is no later than 31st October 1997); and
- (b) Transco will notify the User of the outcome of its consideration (pursuant to Section G1.6.8(b)(ii)) not later than 28 Days after receipt of the User's renotification and where Transco does not agree to revise the Annual Quantity it shall provide the User with details of the reasons for its decision."

Renumber existing paragraph 7.9.5 as 7.9.7 and amend:

"...under Section G1.6.8(a) or renotification under paragraph 7.9.4 in respect of the relevant Supply Meter Point, or under paragraph 7.9.3 may only be given...."

To be inserted in Transition Document Part II, Paragraph 8

Section G: (Supply Points)

Amend two existing references G1.6:

"G1.6 (1) Where the Initial Annual Quantity...
(2) Annual Quantities of Supply Meter Points...."

Add at G1.6:

"(3) For the purposes of the Gas Year 1997/98 references at Section G1.6.8(a), 1.6.11 and 1.6.12 to 31st December shall be deemed to be references to 31st January."

Amend G5.2.3:

"Until 30th September 1998.....".

Section S: (Invoicing)

Add:

"S3 (1) For the purposes of paragraph (2), a "relevant month" is each of October, November and December 1997 and January 1998.

(2) In respect of NTS Exit Capacity Charges, LDZ Capacity Charges and the Capacity Variable Component of Customer Charges (each a "relevant charge"):

(a) Transco shall determine the applicable reduction amount for each User;

(b) the "applicable reduction amount" (ra) shall be:

$$ra = (A - B)$$

where:

A the relevant charge paid or payable by the User for the month of September 1997;

B the relevant charge that would have been payable by the User for the month of September 1997 had the Transportation Statement prevailing on 1st October 1997 applied to such month;

(c) in relation to the Invoice Amount for a relevant charge under an NTS Capacity Invoice and an LDZ Capacity Invoice in respect of a relevant month, Users shall be entitled to withhold payment of an amount in respect of each relevant charge not greater than the applicable reduction amount.

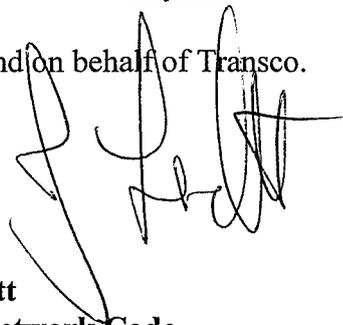
(3) Transco shall recalculate NTS Exit Capacity Charges and LDZ Capacity Charges paid or payable by a User for the months of October, November and December 1997 and January 1998 by reference to:

(a) subject to (b), where Transco agrees to revise the Annual Quantity following a notification under Section G1.6.8(a) and the User submits a Supply Point Reconfirmation which becomes effective on or before 6th March 1998, the revised Annual Quantity; or

- (b) where Transco agrees to revise the Annual Quantity following a renotification under paragraph 7.9.4 and the User submits a Supply Point Reconfirmation which becomes effective on or before 30th June 1998, the revised Annual Quantity.
- (4) Where following the recalculation referred to at (3), it is shown that an Invoice Amount has been incorrectly stated Transco shall submit an Adjustment Invoice or as the case may be an Ad-hoc Invoice and interest shall be payable (from the Invoice Due Date of the relevant NTS Capacity Invoice or LDZ Capacity Invoice to the Invoice Due Date of the Ad-hoc Invoice or Adjustment Invoice) in respect of any such adjustment (for which purpose the Applicable Interest Rate shall be the rate under Section S3.6.4(ii))
- (5) A User may not submit an Invoice Query in respect of an Invoice Amount relating to a relevant charge under an NTS Capacity Invoice or an LDZ Capacity Invoice for the months of October, November and December 1997 and January 1998 where the Invoice Query relates to the Annual Quantity used in calculating such relevant charge.
- (6) In the event that the User's NDM Output Nomination Supply Point Meter Demands for 1st October 1997 exceeds 140% of the User's NDM Output Nomination for 30th September 1997 (any such excess being the "excess percentage"):
- (a) in respect of the whole amount payable under User's Commodity Invoice for October 1997, the User may withhold payment of an amount not greater than the excess percentage;
- (b) where the User withholds payment of an amount under (a), the amount withheld shall be paid by the User to Transco on or before the Invoice Due Date of the User's Commodity Invoice for November 1997; and
- (c) for the purposes of this paragraph (4), the User's NDM Output Nomination shall be that prevailing at the end of each of the relevant Days."

Signed for and on behalf of Transco.

Signature:



John Lockett
Manager, Network Code

Date:

24.6.98

9810612603

Director General of Gas Supply Response:

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 0203, version 1.6 dated 24/06/98) be made as a modification to the Network Code.

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

Signature:

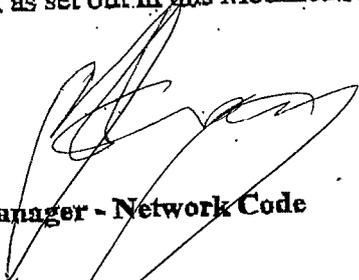


**Kyran Hanks
Director of Transportation Regulation**

Date: 25/6/98

The Network Code is hereby modified, with effect from 26th June 98, in accordance with the proposal as set out in this Modification Report, version 1.6.

Signature:



**Process Manager - Network Code
Transco**

Date: 30/6/98

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.