

Modification Report
Urgent Modification Reference Number 205/205a
Auction Sale of Remaining Rough Firm Deliverability and Space and Use of Rough
Interruptible Deliverability Above 'V' = 85%

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 because the proposer is seeking immediate alleviation from the lack of peak gas when maximum demand is most likely to occur.

2. Procedures Followed:

Transco agreed with Ofgas the following procedures for this Proposal;

19th December 1997	Ofgas agree proposal 205 as Urgent
23rd December 1997	Ofgas agree proposal 205a as Urgent
30th December 1997	Close out of Shipper Representations
2nd January 1998	Modification Report to Ofgas (Late)
9th January 1998	Ofgas decision expected

3. The Modification Proposal:

NGC have raised an Urgent Modification that would allow unbooked Rough deliverability and space to be auctioned with immediate effect. Transco, on behalf of BG Storage, has raised an alternative Modification to allow interruptible deliverability to be available, but, with a commodity surcharge based on the daily Rough firm deliverability. The charge would vary from a multiplier of 60 to 240 as laid out in the Modification Proposal.

This joint report is made as a number of representations make identical points for the two Modification Reports and as such, Transco believe it appropriate to only submit a single Modification Report with regards to the unbooked firm deliverability at Rough.

4. Transco's Opinion:

Transco does not believe that it is appropriate to change fundamental aspects of the regime prior to completion of a comprehensive analysis of recent events or demonstration that these events can be shown to be damaging to the industry or competition.

Fundamentally changing the storage booking regime during the storage year undermines the commercial positions already taken by prudent Shippers/Suppliers who have invested significantly to satisfy their licence obligations. Additionally the proposed changes would particularly benefit those Shippers who have contracted for the Rough Space only service. However in response to discussion at the Modifications Panel on 18th December, Transco has sought and obtained a dispensation to reopen storage bookings. Shippers have shown interest in further bookings, but are understandably reluctant to commit themselves until a decision is made on this proposal.

Transco also believe that the events of 17th December reveal the commercial value of interruption. Whilst Transco clearly has no desire to see interruption it is important that this supply/demand matching tool is efficiently priced in the market and indeed Transco believes that the interruptible market has developed recently and that this might help mitigate the risk of price spikes later this winter.

Transco is required to provide a system of incentives on shippers to provide adequate supplies for their consumers. The definition of "adequate" is, for domestic consumers, in accordance with the 1 in 20 peak day and 1 in 50 severe year criteria. Given these criteria, it is necessary that shippers who accept more risk are exposed to the consequences of that strategy.

Implementation of Mod 205 or 205a will change the commercial positions of Shippers, significantly devaluing expenditure on firm storage services. This could significantly undermine incentives in future years, giving rise to increased Top Up costs and perhaps even risks to security of supply.

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

In the short term the Modifications might create a better and more efficient system, however by undermining current incentives the Modification may give rise to higher costs and increased inefficiency in the longer term.

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

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

Additional Rough deliverability would be made available with both proposals.

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

Additional operating costs would occur, but additional revenues would also result, as such, the implications are minimal.

- 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:**

Costs are included within current formula provisions.

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

The modification fundamentally changes the basis of pricing methodologies (in respect of Rough firm storage services) approved by the Regulator. Such changes might undermine confidence in the Pricing regime which might have fundamental impacts on the industry.

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:**

The contractual risks to Transco arise from the implications of changing the commercial regime within the winter period. It undermines any incentive in the future to ensure the community makes Storage bookings early, if there is always the potential to change the contractual obligations within year.

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

No UK-LINK implications. BG Storage Billing systems would need amendment.

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

Relevant Shippers would have to change their operational policies for the use of Rough deliverability.

The contractual risk of the Shippers will change as a result of this Modification as it will affect their current commercial positions. Effects on individual Shippers will have to be considered, as some will gain and some will lose.

10. **The implications of implementing the Modification Proposal for Terminal Operators, Suppliers, Producers and any Non-Network Code Party:**

This Modification changes the way in which shippers can choose to secure peak gas and so may reduce the requirement to procure it from other sources.

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:**

Implementation could put BG plc in breach of Standard Condition 11 (non-discrimination) of its PGT Licence and/or Standard Condition 3(7)(a).

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

a) **Advantages**

Rough capacity which is currently unbooked would be made available at potentially lower prices to those on offer.

This may increase beach gas available by "unlocking" gas currently in Rough that can only be withdrawn on days when forecast demands is below 85% of peak.

Such gas may decrease the price of system buys on days when forecast demand exceeds 85%, which may therefore moderate gas cashout prices.

b) **Disadvantages**

The Modifications would constitute precipitative action, changing the balance of commercial positions taken on the basis of considered judgement, without detailed analysis of symptoms and apparent consequences of remedies.

The Modification would fundamentally alter the basis of regulated pricing methodology potentially damaging particular industry players in the short term and the broader industry in the longer term.

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

Fifteen Shipper representations were received with regard to these Modifications and BG Storage also submitted a representation with regard to the Proposals raised for them by Transco. Of these, three expressed support for the auction of remaining firm deliverability. Of the remaining representations one or two expressed some support, but had reservations about the timing. The remainder opposed it strongly as it creates inappropriate commercial incentives in mid winter. Key areas that were raised from the representations are now summarised;

a) Discrimination:

The vast majority of Shippers and BG Storage included, objected to the proposal because of the discrimination elements. Organisations have already taken a commercial position with regard to their peak deliverability for winter 1997/98. Changing the regime in mid stream, would advantage and disadvantage organisations depending upon the positions that they took earlier. Those that believe they would be disadvantaged have indicated that they would seek compensation should the Modification go ahead.

b) Transco Licence Obligation:

A number of Shippers have indicated that Transco has a licence obligation to offer services on a non discriminatory basis. By allowing the tender process mid way through the year they question whether Transco satisfy their licence obligation.

c) Other alternatives for making peak gas available:

A number of Shippers expressed concern about precipitative actions. Some Shippers believe that the market should be permitted to develop within the current regime framework and that this should increase availability of gas via the use of end customer interruption.

d) Role of Top Up Manager:

Some Shippers indicate that the role of the Top Up Manager could be changed and hint that this may be a more appropriate solution to enable the deliverability of peak gas.

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

Implementation is not required for these purposes.

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

Standard Condition 3(5) requires the licensee to establish a methodology for the determination of transportation prices, and 3(1) requires the licensee to furnish the Director with a statement of transportation arrangements and prices, and the methods and principles by which prices are determined. Neither clause is directly relevant. However 3(7)(a) requires the licensee to avoid any undue preference or discrimination in storage prices, and implementation may breach this clause.

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

If Modification 205 is approved on 9th January 1998 then a tender would need to be prepared. It is currently unclear what the rules for any tender would be or indeed how these would be determined. BG Storage would presumably need to conduct a consultation on the change of methodology in accordance with Standard Condition 3 of the PGT Licence.

If Modification 205a is approved then the revised service would be available from 19th January 1998.

17. Proposed implementation timetable:

Further clarification is required before a Timetable is finalised.

18. Recommendation for the implementation of the modification:

Transco recommends that these proposals (205/205a) should not be implemented and suggest that a formal review is carried out for the 1998/9 winter.

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 Proposal:

This Modification Report contains a recommendation not to modify the Network Code and Transco now seeks a direction from the Director General in accordance with this report.

21. Text Provided pursuant to Rule 9:

Transco does not consider it appropriate to provide legal text at this stage.

It will not be possible to draft legal text until the allocation method between bid options is clarified. The drafting is expected to be complicated for Modification 205.

Signed for and on behalf of Transco.

Signature:

John Lockett
Manager, Network Code

Date:

5.1.98

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 205/205a, version 1.0 dated 06/01/98) 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:

The Network Code is hereby modified, with effect from _____, in accordance with the above proposal.

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.