

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 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

1.1 The Original Proposal

The Original Modification Proposal 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.

1.2 Methodology Development

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 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. As a result of these discussions the following conclusions were reached:

1.3 Billing Methodology

The Billing Methodology, which would be followed were this Modification Proposal to be accepted, is attached to this report as Appendix 1. This assumes separate billing adjustments for each Gas Year and the period from 1 February 1998 (the first day of RbD) to 30 September 1998. The 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. As part of Transco's ongoing operational controls, the application of the underlying methodology of RbD adjustments has been audited and found to be in conformance with the Network Code. It should be recognised that contrary to the belief of one shipper, this methodology would not require the creation of any special "RbD pot".

1.4 Assessment Methodology

In addition to the routine adjustments already provided under the existing Network Code, this Modification Proposal would give Transco the obligation of calculating and invoicing for adjustments as a result of the Domestic Meter Temperature Surveys (DMTS) and as a result of the domestic internal vs external metering point survey.

There are therefore three potentially separate adjustments that could be made:

(1) 1999 and 2000 DMTS, available July 2000

(2) Internal vs external split, available late 2000

(3) 2001 DMTS, available July 2001

No decision has been made to date to carry out any further surveys following the completion of (3)

Gas Year Adjustments	Original Data	Routine Adjustments	One-off
RbD to end September 98	I&C 1996/1997	None	(1), (2) and (3)
1998/1999	I&C 1996/1997	None	(1), (2) and (3)
1999/2000	I&C 1996/1997	(1)	(2) and (3)
2000/2001	(1)	(2) and (3)	None

Transco has calculated by LDZ the range of adjustment quantities relating to the 1999 and 2000 DMTS and has detailed them in Appendix 2. From these adjustments, their market shares and System Average Prices (SAPs), shippers could estimate their own credit or debit positions. Information on market share and SAPs is already available to shippers through Transco's routine billing and information service processes.

Particularly with the one-off adjustments (1), (2) and (3), for billing purposes Transco would have the option of bundling all these together, bundling two of them together or invoicing them separately. This point has been debated but as this is a methodology issue, the legal text does not need to specify this level of adjustment detail. This debate has continued within the representations and a compromise suggestion has been made and supported by Transco that adjustments (2) and (3) should be bundled together but adjustment (1) should proceed as soon as practicable

1.4 Close-Out

The present programme of domestic meter point surveys does not extend past the 2001 DMTS. There is a lack of consensus within the community whether it would then be appropriate to carry out a final adjustment on the initial RbD periods and effectively close-out that period. To make progress, the legal text of this Modification Proposal is limited to the adjustments required as result of the surveys already executed or planned and will effectively close-out the initial RbD period. If it became necessary to re-open this period, a further Network Code Modification would be required.

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 would 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 would be made, other than those already covered within the main body of the Network Code. This would not prevent any party to the Network Code proposing a Modification if it became 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, implementation of 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)

Representations following the Draft Modification Report were received from British Gas Trading (BGT), Eastern Energy part of TXU Europe Energy Trading Ltd (TXU), Scottish and Southern Energy plc (SSE), Scottish Power (SP) and Yorkshire Energy Limited (YE). BGT, SSE and YE wrote in support of the modification. TXU and SP supported the basic principle behind the Modification Proposal but had reservations over the detailed proposals for its implementation. The principal issues raised were close out, number of adjustments and suitability of relevant data.

Close Out

BGT stated: "We have some reservations about the need to 'close out' a shrinkage period. However, we are happy to go along with the proposal in the belief that it will almost certainly be a case of diminishing returns from further refinements after the already planned corrections for the internal/external meter split and the results from the DMTS with its improved sample."

TXU stated that it "...would also appreciate clarity in respect of what is proposed for 'close out'. Our belief is that if the DMTS is insufficiently robust to change the regulations it is inadequate to close out on." This comment should be viewed in the context of a previous representation by TXU that "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."

SSE stated: "We are therefore pleased to see a close out date following the assessment of the 2000/2001 shrinkage year."

SP stated that it "...had concerns over the open-ended period for which adjustments will be made. We feel that it is appropriate to state when adjustments will cease for historic periods to give Shippers comfort that they do not have an unlimited period of liability"

Transco's Response

Transco has sympathy with Shippers' views that a close-out date should be set and therefore proposes that, following completion of the 2001 DMTS and the consequent adjustments, future adjustments would only cover the preceding Gas Year. This is in accordance with N3.4 of the Network Code.

Number of Adjustments

BGT stated that "the Mod as drafted allows for multiple changes (if required) as and when improved domestic temperature data becomes available. It therefore fulfils the commitment given at the time of RbD implementation to adjust to domestic temperatures once they become available from a suitable survey to be undertaken by Transco." BGT also stated that "The case against delaying until a final set of domestic temperatures is agreed is driven by the fact that the incorrect allocation between LDZs has been in place for a considerable time, and insofar as any shippers have suffered should be corrected as soon as possible."

SP stated: "In addition, we would prefer to see a single adjustment being made for each gas year reflective of all new information obtained. This may delay the process of reconciliation of Shippers, but would serve to keep uncertainty and administrative costs to a minimum, both for Transco and Shippers alike."

TXU referred to a previous representation from them which stated "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."

Transco's Response

Whilst Transco's own administrative costs would be lower if there were a single adjustment, the necessary systems and processes are in place to allow several adjustments. However, in light of representations, Transco proposes having two sets of adjustments. The first would implement the results of the 1999 and 2000 DMTSs and the second would implement the 2001 DMTS and the survey of external vs internal meters.

Data Suitability

BGT stated that the data available from the 1999 DMTS and 2000 DMTS: "...fulfils the commitment given at the time of RbD implementation to adjust to domestic temperatures once they become available from a suitable survey to be undertaken by Transco." This statement was made notwithstanding, "a few minor reservations about those results"

SSE stated: "The Domestic Temperature Survey represents a significant improvement in the robustness of the data used to derive LDZ specific shrinkage factors. This work has been undertaken with industry agreement and has been the subject of lengthy debate." SSE subsequently confirmed by telephone that references to the "Domestic Temperature Survey" or "DMTS" include the survey of internal vs external meters.

SP stated: "At the present time we cannot comment on the details derived from the DMTS 2000 and their effect on Shrinkage Factors, as discussions and analysis of this information has not yet been carried out by the sub-group. We do however hope to gain more confidence in this information through discussion with Transco, BG Technology and Ofgem Technical Directorate." It further stated: "With regard to carrying out temperature surveys into the future, Scottish Power feel that it may be worthwhile developing this area together with the Demand Estimation Process, currently carried out by Transco. It has been

the ultimate goal of the Shrinkage subgroup that the sample obtained in respect of temperatures should be robust enough to allow Ofgem to assess the suitability of the inherent Gas Regulations for customer billing. Continuing focus on this issue may lead to this goal being met."

TXU referred to a previous response from them which stated: " We share 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."

Transco's Response

Transco concurs with the view that the series of DMTSs together with the internal vs external meter survey fulfils the commitment given at the time of RbD implementation. Summaries of this data have been presented to the LDZ Shrinkage Forum which concurs that it should be used for the purpose of LDZ Shrinkage Factor adjustment. Transco has therefore followed the agreed consultation process in this.

Transco has no plans at present to carry out a 2002 DMTS so the potential option of development of a combined survey with Demand Estimation does not need to be considered at present.

Other Comments

TXU believed that a special pot may be required for the retrospective adjustment but Transco confirmed that this was not necessary. BGT concurred with Transco's view.

SSE registered a concern "over the lack of formal consultation or 'sign-off' with regards to the LDZ Shrinkage Assessment in general. Although this adjustment has been well represented it provides no future guarantees". Transco's response to this comment is that it intends to continue with the consultation process it has set up with the industry and generally maintain industry consultation within the appropriate forum.

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

Implementation of 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

Implementation of 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 the 1999 DMTS and 2000 DMTS are available and carry out the consequent billing adjustments
Repeat this process when the results of the 2001 DMTS and the internal vs external survey are complete.

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. 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.

18. Transco's Proposal

19. Text

Transition Document II

8.11.3 N3.4 *Delete existing text and replace with*

“For the purposes of Gas Year(s) 1999/2000 and 2000/2001 reference to the Preceding Year in Section N3.4.1 shall be deemed to be a reference to the period from the Reconciliation by Difference Date to 30th September 1999 and 30th September 2000 respectively”

Signed for and on behalf of Transco.

Signature:

Tim Davis
Manager, Network Code

Date:

Gas and Electricity Markets Authority Response:

In accordance with Condition 9 of the Standard Conditions of the Gas Transporters' Licences dated 21st February 1996 I hereby direct Transco that the above proposal (as contained in Modification Report Reference **0396**, version **2.0** dated **04/08/2000**) be made as a modification to the Network Code.

Signed for and on Behalf of the Gas and Electricity Markets Authority.

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

1. Any provision contained in this Agreement or in any arrangement of which this Agreement forms part by virtue of which The Restrictive Trade Practices Act 1976 ("the RTPA"), had it not been repealed, would apply to this Agreement or such arrangement shall not come into effect:
 - (i) if a copy of the Agreement is not provided to the Gas and Electricity Markets Authority ("the Authority") 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 Authority 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 paragraphs 1(6) or 2(3) of the Schedule to The Restrictive Trade Practices (Gas Conveyance and Storage) Order 1996 ("the Order") as appropriate

provided that if the Authority does not so approve the Agreement then Clause 3 shall apply.
2. If the Authority does so approve this Agreement in accordance with the terms of the Order (whether such approval is actual or deemed by effluxion of time) any provision contained in this Agreement or in any arrangement of which this Agreement forms part by virtue of which the RTPA, had it not been repealed, would apply this Agreement or such arrangement shall come into full force and effect on the date of such approval.
3. If the Authority does not approve this Agreement in accordance with the terms of the Order the parties agree to use their best endeavours to discuss with Ofgem any provision (or provisions) contained in this Agreement by virtue of which the RTPA, had it not been repealed, would apply to this Agreement or any arrangement of which this Agreement forms part with a view to modifying such provision (or provisions) as may be necessary to ensure that the Authority would not exercise his right to give notice pursuant to paragraph 1(5)(d)(ii) or 2(2)(b)(ii) of the Order in respect of the Agreement as amended. Such modification having been made, the parties shall provide a copy of the Agreement as modified to the Authority pursuant to Clause 1(i) above for approval in accordance with the terms of the Order.
4. For the purposes of this Clause, "Agreement" includes a variation of or an amendment to an agreement to which any provision of paragraphs 1(1) to (4) in the Schedule to the Order applies.