Modification Report
Removal of Output Unauthorised Gas Flow Charges from the Network Code
Modification Reference Number 0448

Version 8.0

This Modification Report is made pursuant to Rule 7.3 of the Modification Rules and follows the format required under Rule 8.9.3.

1. The Modification Proposal

British Gas Trading suggested that:

The removal of output UGF from the Network Code has been repeatedly raised as an issue since Modification Proposal 069 was raised in 1996.

The original intention of UGF charges was to encourage shippers to make nominations at entry and exit points, which would provide valuable information to Transco to enable both accurate system scheduling and NDM demand forecasts to be produced.

However, a shipper can avoid UGF charges by entering a zero against the relevant activity on AT-LINK. This can be administratively burdensome for shippers and dependent on the number of nominations that have to be entered, can lead to oversights. Such an oversight would result in a UGF charge at SMP. The level of this charge is inconsistent with the negligible impact on Transco's ability to correctly schedule outputs on the system.

Modification 232 - Removal of Input UGF at Sub-Terminals was implemented in August 1998 and resulted in Transco entering zeros at all sub-terminals for all shippers. In the letter accompanying the implementation of this change, Ofgem made it clear that they expected the issue of output UGF to be dealt with at the energy workstream.

Despite repeated attempts by shippers there has been reluctance by Transco to progress this issue. This proposal is intended to facilitate the removal of output UGF

2. Transco's Opinion

Unauthorised Gas Flows (UGFs) have been a feature of the balancing regime since Network Code began on 1 March 1996. A number of Modification Proposals were raised from August 1996 onward, aimed at either addressing the impact or removing the concept of UGF from the Network Code. Whilst Modification Proposal 0069, which addressed the removal of both entry and exit UGFs, was rejected, Modification Proposal 0232 for removal of entry UGF was implemented in September 1998. At that time, Ofgem was of the view that exit UGF should be debated further.

Exit UGF has remained a discussion topic at the Energy and Capacity Workstream for some time.

Shipper charges associated with exit UGF only arise if shippers fail to insert output nominations. Charges are based on the quantity of unauthorised energy flowed multiplied by SMPbuy price. In addition, scheduling charges apply as normal. The shipper exposure

however, depends on the SMPbuy-SAP or SMPbuy-SMPsell price differential, depending on the extent of shipper imbalance and the scheduling charge. This is because exit UGF charges at SMPbuy would be offset by changes in imbalance charges at SAP and/or SMPsell had nominations been entered. Shippers can however,avoid exit UGF charges by inserting zero exit nominations, a process which Transco understand can be cumbersome for shippers with a relatively large number of exit meters.

Transco has been of the view that the exit UGF regime has a beneficial influence on shipper nomination accuracy thereby enhancing the efficiency of balancing decisions, interruption management and NDM demand estimation. For this reason, Transco has been seeking a solution that, whilst removing exit UGF charges, might improve the scheduling regime. In order to further the relevant objectives, Transco is of the opinion that exit UGF charges could be removed whilst pursuing provision of high quality nomination information separately.

The methodology for removal of exit UGF charges suggested by British Gas Trading constitutes automated insertion of zero output nominations. The number of exit meters is significantly larger than the number of entry meters and a manual solution (as is currently the case for entry meters) may be an inefficient way of removing exit UGF charges. Transco has some reservations about the proposed solution to automatically insert zero nominations as this would generate a large volume of unnecessary default data points that might have an adverse effect on other processes. Transco is therefore considering an alternative approach that might suppress exit UGF charges. Such an approach might be developed such that exit gas flows generate exit allocations in the same manner, independent of whether a shipper has made a corresponding exit nomination. Such an approach might ensure that Energy Balancing and Neutrality processes could function in the normal way and generate appropriate effects although some minor changes to ensure that scheduling charges are applied correctly may be required.

For the purpose of Output Nominations, Network Code treats different types of Exit Points differently. Such treatment is directly influenced by relevant provisions of specific contractual arrangements for Connected System Exit Points and Interconnectors. The impact of these arrangements on any potential solution may be significant and must be considered carefully in determining a robust solution.

Transco therefore supports the objective underlying the Modification Proposal but believes that there may be alternative approaches that might better facilitate the relevant objectives.

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

BGT suggests that "the particular objectives of running an economic and efficient pipeline system will be furthered.....".

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

a) implications for the operation of the System:

Exit UGF charges have the potential to encourage accurate DM nominations. Removal of such charges may reduce nomination accuracy which may impact Transco's energy balancing decision making and interruption management processes.

b) development and capital cost and operating cost implications:

Transco is currently undertaking system impact assessment, and assessing the cost implications.

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 of system development would be met from allowed revenue for such purposes.

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

Transco is not aware of any impact on price regulation.

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 not aware of any consequence for contractual risk as a result of implementing this Modification Proposal.

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

Transco's computer systems would need to ensure that the allocations are correctly attributed and appropriate charges, including imbalance charges and scheduling charges, are correctly calculated and invoiced.

Insertion of zero nominations might have an impact on shipper systems (even if only at the margin) because of increased data volumes.

7. The implications of implementing the Modification Proposal for Users

If the Modification Proposal is implemented, Users would not face exit UGF charges. Since UGF charges are based on System Marginal Price (buy), Users might face reduced exposure to SMP (buy).

Removal of exit UGF charges would result in 'UGF volume' contributing to the User UDQO and hence would have an impact on User imbalance.

Users would also avoid administrative effort for entering zero exit nominations.

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

Transco is not aware of any implications for terminal operators, consumers, connected system operators, storage operators, suppliers, producers or any non-Network Code party.

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

Advantages:

- Transco would incur reduced administration costs associated with invoicing processes.
- Users would not face UGF charges and might avoid exposure to SMP (buy).
- Users would avoid administrative effort entering zero exit nominations.

Disadvantages:

- User exit nomination performance may deteriorate.
- Lack of accurate nomination information may have an adverse effect on Transco's energy balancing decision making, interruption management and NDM demand estimation.

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

Representations were received from BP Gas Marketing Limited, TXU, Northern Electric & Gas Supply, Shell Gas Direct Limited, Yorkshire Energy Limited, British Gas Trading (BGT), Cinergy Global Trading Limited, TotalFinaElf Gas and Power Limited, Aquila Energy Limited and Powergen.

Nine Shippers expressed support for the Proposal whilst one was against.

Northern Electric & Gas Supply is not supportive of the Modification Proposal on the basis that Transco will actively seek to develop an alternative solution that will not only remove exit UGF charges but also ensure that there is no deterioration in the scheduling regime.

Shell Gas Direct is supportive of the Proposal as it addresses issues similar to those raised and implemented via Modification 0232 for removal of entry UGF charges. It considers the process of inserting zero nominations by Shippers as burdensome and UGF charges as penal costs for administrative errors.

Yorkshire Energy supports the Proposal in principle, provided that the AT Link system remains robust and that there are no adverse implications for its users.

Cinergy supports immediate implementation of the Proposal as Transco's alternative solution that removes UGF charges at a more fundamental level could take a long time. It considers that Transco could still provide a more efficient solution at a later date. With regard to the information provision, it believes that blank or zero nominations are no different and that the charges associated with one action over the other are neither reflective nor necessary. It also suggests that, in relation to the allocation mechanism at Shared Supply Meter Points, if all parties have zero output nominations, then the current default allocation rules for blank nominations should apply.

TotalFinaElf is supportive of the Proposal as it has been concerned and frustrated by delays in resolving this problem. However, it noted Transco's concerns about possible complications with the implementation of the methodology proposed in the Proposal. It also noted that Transco's approach of suppressing UGF charges, outlined at a recent Energy and Capacity Workstream, appeared to offer an alternative that is acceptable to both Transco and the community. TotalFinaElf would wish Transco to clarify the timing of raising an alternative proposal as the Modification Rules might not allow an alternative proposal to proceed until the outcome of BGT's Proposal has been determined.

Powergen is in support of the Proposal as the removal of exit UGF charges would remove shipper exposure to these penalties. It also believes that exit UGF charges result from occasional errors and these are unlikely to affect Transco's demand estimation, balancing actions and interruption decisions.

BGT, the proposer, supports implementation of the Proposal as soon as possible. It makes several comments on the draft Modification Report and these are summarised in the following paragraphs.

BGT describes the sequence of events that led to raising the Proposal, including lack of progress by Transco for more than twelve months.

Whilst it welcomes the exploration of alternative approaches by Transco, it does not consider that a large volume of unnecessary default data points, created by BGT's proposed solution, could have an adverse effect on other processes, unless Transco could demonstrate this quantitatively. Furthermore, it does not accept Transco's argument that insertion of zero output nominations would cause problems for default allocations at CSEPs and SSMPs as shippers are already able to insert zero exit nominations in order to avoid exit UGF charges. Nor does it accept that invoking of default allocation rules at Entry is a real cause for concern as insertion of zero input nominations has been carried out for over two and half years without any reported problems.

BGT acknowledges that the Proposal did not contain a specific section on relevant objectives that would be facilitated by this Proposal. For clarity, it states that "the particular objectives of running an economic and efficient pipeline system will be furthered.....".

BGT does not agree with Transco that the removal of exit UGF charges might reduce nomination accuracy. It believes that scheduling charges provide sufficient incentive for shippers to ensure accurate output nominations, and hence there should not be any impact on Transco's balancing decisions or interruption management.

Finally, BGT suggests that, in the absence of timescales for implementation of Transco's alternative solution, this Proposal should,be implemented, and in the meantime, Transco should bring forward its more efficient solution in the form of a Modification Proposal.

Transco's Response:

With regard to provision of accurate information, Transco agrees with Cinergy that insertion of a zero, as opposed to a blank entry, provides no added information to Transco. Furthermore, Transco shares Northern Electric & Gas Supply's concern about possible deterioration in scheduling performance as a consequence of removal of exit UGF charges. At the Energy and Capacity Workstream in January 2000 and February 2000, Transco

presented several options to the community for improving scheduling performance whilst simultaneously removing exit UGF charges. However, at that time, Transco received no support for any of these options, contributing to delays in resolving this issue.

Transco agrees with Shell Gas Direct and Powergen that the process of inserting zero nominations can be burdensome, particularly for shippers with a large number of exit meters. However, Transco is also mindful of Yorkshire Energy's concern that the removal of exit UGF charges should not adversely affect robustness of AT Link. At the Energy and Capacity Workstream on 1 February 2001, Transco demonstrated that, whilst BGT's solution would remove exit UGF charges, efficient operation of Transco's computer system could not be guaranteed as this solution would generate a large volume of unnecessary data. Whilst Transco welcomes BGT's clarification of the relevant objectives that would be furthered by the Proposal, Transco does not believe that the inefficiencies in the proposed solution would facilitate efficient running of the pipeline system.

At Workstream meeting, Transco also highlighted the differences between inserting zero nominations at entry points and the impact of repeating a similar exercise at exit points. These differences included the relatively large number of exit meters, additional validation checks for the status and type of exit meter, and consideration of both firm and interruptible exit nominations. All these differences led to Transco's conclusion that an 'entry-type' solution involving insertion of zero input nominations would be inefficient for removal of output UGF charges. Whilst there may be similarities, as noted by Shell Gas Direct, between the issues raised by this Proposal and those addressed by Modification 0232 (for entry), the additional considerations outlined by Transco demonstrate that replication of a simple 'entry-type' solution for exit may not be the best way forward.

Transco identified the potential impact of inserting zero output nominations on the existing Network Code rules and illustrated at the Workstream that specific default allocation rules, particularly those concerning CSEPS, might become inapplicable. Transco also pointed out that a similar problem could occur on the entry side even though Transco had been inserting zero input nominations on behalf of shippers without any reported problems. Whilst BGT does not agree with Transco on this issue, Transco welcomes Cinergy's suggestion that where all output nominations are zero, current default allocation rules for blank nominations could apply.

Transco shares BGT and Cinergy's concerns for prompt resolution of this issue and early removal of exit UGF charges. However, Transco would wish to ensure that any potential solution is not only as efficient as possible but also does not inadvertently create anomalies in the existing Network Code rules. Transco is also of the opinion that immediate implementation of this Proposal, and subsequent implementation of a more efficient solution, is not the most efficient way of achieving the desired outcome. Transco, therefore, does not recommend immediate implementation of a proposal that, in Transco's opinion, does not facilitate the relevant objectives.

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 directly linked to Transco's compliance with any 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 to comply with the above clauses.

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

User exit allocations and subsequent User charges would need to be adjusted to account for exit 'UGF volume'.

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

Transco would wish to implement a solution as soon as reasonably practicable.

16. Recommendation concerning the implementation of the Modification Proposal

Transco does not recommend implementation of this Modification Proposal. However, Transco would wish to build on BGT's Proposal and develop a more efficient solution that could achieve the same desired outcome.

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

This Modification Report contains Transco's proposal to modify the Network Code and Transco now seeks direction from the Gas & Electricity Markets Authority in accordance with this report.

19. Text

Section C: Nominations

Insert new paragraph 2.2.6 to read:

"2.2.6 If in respect of a System Exit Point, a User has not made a DM Output Nomination in respect of the Gas Flow Day, the User shall be deemed to have made a DM Output Nomination of zero at the Relevant Output Nomination Time."

Section E: Daily Quantities, Imbalance and Reconciliation

Amend Paragraph 3.2.8 to read:

"3.2.8 If no User made an Output Nomination for the Connected System Exit Point for the Gas Flow Day (and accordingly C2.2.6 applies), or where all the Output Nominations for the Connected System Exit Point for the Gas Flow Day are submitted as zero, and gas was offtaken from the System at the point:

(i) each User who was (whether or not by virtue of this paragraph 3.2.8) an Offtaking CSEP User on the Preceding Day shall be an Offtaking CSEP User; and

(ii) the CSEP Daily Quantity Offtaken shall be allocated to the Offtaking CSEP Users in the proportions in which the equivalent quantity was (whether or not by virtue of this paragraph 3.2.8) allocated on the Preceding Day."

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 **0448**, version **8.0** dated **21/09/2001**) 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 **8.0**.

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.