

**Modification Report**  
**Expand Definition of Restricted User to include other Licenced Parties**  
**Modification Reference Number 0528**

Version 1.0

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**

The Modification proposes that the definition of Restricted User contained in Section V2.5.1 of the Network Code be expanded to also include other Clearing Houses licenced by the Financial Services Authority or licenced under the Financial Services Act.

**2. Transco's Opinion**

This Modification Proposal would permit admittance to the Network Code of an additional type of Clearing House body recognised by the Financial Services Authority (FSA) to register trade nominations, onto Transco systems, that have arisen from an independent markets clearing activities.

The FSA recognises two types of body that may offer clearing facilities appropriate for admittance as a Restricted User under section V of the Network Code. The first is a Recognised Clearing House (RCH) which is already provided for under section V and the second is a Recognised Investment Exchange (RIE). Although the two are distinct (but very similar) types of body under the FSA and the Financial Services & Markets Act (FSMA) it appears that the current provisions of the Network Code would not permit an RIE to be admitted as a Restricted User.

Transco has no reason to object to the proposed addition of RIEs to section V2.5.1, since RIEs and RCHs may be viewed as materially equivalent. In respect of the FSA there is considerable overlap between a RCH and RIE in regard to the recognition requirements and both must meet and maintain their recognised status.

Under FSA the RIE is obliged to ensure that satisfactory arrangements are made for securing the timely discharge of the rights and liabilities of the parties to transactions effected on the exchange. The FSA accepts that an RIE may satisfy this requirement either by making its own arrangements for clearing transactions or by appointing a RCH to do so. Where an exchange conducts its own clearing arrangements it will be subject to FSA supervision equivalent in that respect to the FSA supervision of RCHs.

Transco would suggest that facilitation of this proposal may be achieved by modifying section V2.5.1 of the Network Code to admit a body which is declared by Order of the Secretary Of State to be a RIE for the purposes of the FSA.

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

The Proposer states that although this Modification Proposal may not necessarily further the Transporter's relevant objectives, it is to the general benefit of Network Code Users in that it will extend the potential of competition in energy trades.

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

**a) implications for the operation of the System:**

Transco does not anticipate any such implications.

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

Transco does not anticipate any such 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:**

Transco anticipates that the implementation of this Modification Proposal would not lead to an increase in costs.

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

Transco does not anticipate any such consequences.

**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 consequences.

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

Transco does not anticipate any such consequences

**7. The implications of implementing the Modification Proposal for Users**

Transco does not anticipate any such implications.

**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 unaware of any such implications.

**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 unaware of any such consequences.

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

Advantages:

Implementation may increase the number of independent Market Operators offering secure and cleared services. This may benefit market participant by reducing risk from counterparty default.

Implementation may encourage the development of third-party markets for additional products available within the gas industry.

Disadvantages:

Where an existing independent Market Operator appoints an RIE to clear it's market, therefore providing an additional service, costs to the Market Participant may increase.

**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 six respondents.

Dynegy UK Limited	Dynegy
Shell Gas Direct Ltd	SGDL
EnMO	EnMO
Accord Energy Ltd	Accord
Conoco(UK) Ltd	Conoco
Southern and Scottish Energy Plc	SSE

Four respondents express support for the Modification Proposal.

Dynegy and SGDL are not in support of the Modification Proposal on the grounds that the proposer provides too little information on the reasons which motivate this Proposal and that this does not facilitate proper consultation. SGDL notes that it would have preferred that the Modification Proposal had not had such a short consultation period.

Dynegy states that it supports the principle of additional clearing houses. However, it is of the view that there are sufficient implications to warrant discussions within an industry workstream. Dynegy recommends rejection of this Modification Proposal, proposing that a new Modification Proposal be raised which would allow the industry to discuss the issues within an open forum.

SGDL expresses the opinion that as the Modification Proposal presently stands, it cannot be demonstrated that it furthers the relevant objectives of the Network Code. EnMO expresses the view that implementation of the Proposal would benefit Users in that the Network Code may then facilitate a cleared and regulated solution to trading markets and that this in turn may 'better the relevant objectives'. SSE considers that implementation of this Modification Proposal would encourage both the development of and participation in screen based cleared market to the benefit of competition in shipping and supply. SSE adds that the use of cleared markets by shippers reduces the risk of counterparty default and therefore believes that the implementation of the Modification Proposal would better facilitate the relevant objectives.

Accord states that the narrow definition currently drafted within the Network Code prevents the development of further competition by the entry of parties which could otherwise compete in this area of activity. Conoco notes that provisions in the Network Code fail to recognise that clearing houses can operate in the UK and under the supervision of the FSA without holding RCH status. It observes that consequently the development of the OTC clearing service for gas markets has been halted, to the detriment of gas traders.

Conoco believes that the Modification Proposal will bring a much greater degree of security from counterparty default, and could prevent systematic risk arising from defaults spreading through the market. Conoco notes that recent experiences demonstrated the benefits of such a service.

Conoco suggests that it would be anticipated that greater security and anonymity offered by centrally cleared trades may promote liquidity and price transparency while reducing discriminatory trading in gas and power markets. Conoco advises that such a service is required as soon as possible, particularly if trading volumes are to continue to grow.

Transco welcomes the views expressed by the respondents and notes that the majority of respondents support the proposed implementation of the Modification Proposal. Transco maintains its position in respect of the Modification Proposal as expressed in section 1 above. Transco also recognises the issues raised regarding the shortened timescale for consultation, but would observe that this was not a Transco decision but was determined by the Network Code Modification Panel on behalf of the industry.

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

Transco is unaware of any such requirements.

**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**

Transco is unaware of any such requirements.

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

Transco does not anticipate that a program of works will be required for the implementation of this Modification Proposal.

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

If Ofgem direct implementation, Transco recommends that this should take immediate effect.

**16. Recommendation concerning the implementation of the Modification Proposal**

Transco's opinion is neutral in respect of any such recommendation to implement this Modification Proposal.

**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 V:

#### Paragraph 2.5

Amended to read:-

#### 2.5 Restricted User

2.5.1 A person which is for the time being either:

(i) {designated by the Director for the purposes of standard condition 7.4A of the Transco Licence}, or

(ii) a body which is declared by an Order of the Secretary of State to be a Recognised Clearing House for the purposes of the Financial Services Act 1986 (as amended), or

(iii) a body which is declared by an Order of the Secretary of State to be a Recognised Investment Exchange for the purposes of the Financial Services Act 1986 (as amended) and which makes its own arrangements for clearing transactions effected on its exchange,

may be admitted as a User for the purposes only of making Trade Nominations pursuant to Section C6."

Signed for and on behalf of Transco.

Signature:

**Tim Davis**  
**Head of Regulation NT&T**

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 **0528**, version **1.0** dated **19/02/2002**) 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 **1.0**.

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 appropriateprovided 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.