

Draft Modification Report
Publication of Shrinkage Provider gas procurement and disposal information
Modification Reference Number 0618
Version 1.0

This Draft 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

The Proposal raised requires:

"For each gas day where the Shrinkage Provider has contracted to buy or sell gas for Shrinkage purposes, Transco should publish before the gas day the following information in respect of that gas day:

- Their unbiased estimate of Shrinkage gas requirements for the next gas day in kwh/therms;
- The volume of Shrinkage gas purchased and sold before the day;
- The number of buys and sells trades executed in respect of that gas day;
- The delivery point of all Shrinkage gas bought and sold, whether at the NBP or at the beach.

For each gas day, Transco should publish after the gas day the following information in respect of the day before:

- Their final net Shrinkage position in kwh/therms
- The volume of Shrinkage gas purchased and sold on the day;
- The total number of buys and sells trades executed in respect of that gas day;
- The weighted average price of all buys and sells
- The delivery point of all Shrinkage gas bought and sold, whether at the NBP or at the beach.
- The minimum price at which the shrinkage gas was bought
- The maximum price at which the shrinkage gas was bought
- The minimum price at which the shrinkage gas was sold
- The maximum price at which the shrinkage gas was sold"

2. Transco's Opinion

Transco does not support implementation of this Modification Proposal.

In particular Transco has concerns in relation to:

- Day ahead and after the day (D+1)information revealing the trading position and strategy of the Shrinkage Provider (SP), as this may detract from efficient trading by the SP.
- The asymmetric nature of the Proposal whereby the SP account would be the only User account on the system required to publish such data.
- The size of the SP account is insignificant in comparison to other trading accounts and therefore it is likely to have limited impact on market liquidity

- The publication of information may require resource commitment every day including bank holidays and weekends and may therefore be inefficient.
- Transco already provides a substantial amount of information relating to the SP account to Users and Ofgem.
- Transco concludes that the implementation of the Proposal would neither better facilitate the economic and efficient operation of the system or competition between Users.

The following articulates the rationale behind the above statements:

Shrinkage gas comprises that used by Transco in connection with the operation of the system (such as compressor use) and that which is unaccounted for as offtaken from the system. It comprises two elements: LDZ and NTS shrinkage.

LDZ shrinkage comprises own use gas; that which is used for pre-heating and that which is vented and unaccounted for gas consisting of unidentified theft, leakage and metering error. For 2003/04 using the same unit cost of gas at the NBP that is used in the NTS reference price defined in the Licence would imply an LDZ shrinkage gas cost of £47.8m representing 0.85% of LDZ aggregate demand. LDZ shrinkage was allowed for by Ofgem when setting Transco's LDZ price control. Hence LDZ shrinkage is an OPEX cost to Transco, with any variation borne by Transco.

NTS shrinkage comprises own use gas for compressor use and unaccounted for gas through CV loss and meter measurement variabilities/errors. For 2003/04 it has a target cost for incentive performance purposes of £60.7m representing 0.72% of NTS throughput. NTS shrinkage is subject to an SO incentive scheme whereby Users receive 75% (upto a cap of £4m) of any upside savings on shrinkage and 80% (upto a collar of £3m) of any downside costs. The incentive sharing factor for NTS shrinkage therefore already aligns User and Transco interests in minimising costs.

Transco believes in the context of managing the shrinkage incentives in the LDZ price control and SO incentive arrangements within the Licence and Regulatory framework it should have the freedom to determine how it responds to the SO incentives. Transco does not believe that further provision of information in respect of the SP daily trading activity would deliver better performance. Additional information provision would divert management focus and at the same time increases the level of trading counter-party risk which undermines that same incentive. The Proposal requires Transco to publish data for each gas day before the day and immediately after that gas day which implies a seven day reporting service and therefore employment of additional resource to process and ensure robust data provision. This is in addition to the costs associated with developing the processes and publication media. Transco would be interested in respondents views as to how these additional costs would benefit the regime to enable a cost/benefit assessment to be made against an economic and efficient outcome.

In relation to provision of trading information ahead of and within day the SP is no different to any other trading party on the system and in terms of trading size measured by individual User input and offtake allocations plus NBP trades the SP is a minor player in the market, being ranked as 52nd in terms of trading activity in December 2002. Transco is therefore unclear as to how releasing information relating to the SP account alone ahead of the gas day will increase liquidity and competition in the gas market. If such ex ante trading information would genuinely improve liquidity then Transco would consider that all Users, including the SP as a User should have similar obligations to ensure non-discrimination.

Transco is concerned that the publication of quantities, prices and number of trades undertaken by the SP would be inappropriate and might indicate Transco distress when either long or short thereby restricting its ability to efficiently access the market. This might be expected to increase the costs associated with operation of the SP account. Such costs might be expected to increase both Transco and User costs in operation of LDZ shrinkage and SO incentives schemes. Transco does not believe such an outcome could be considered economic or efficient.

Transco would also emphasise that it currently provides frequent and extensive shrinkage information in a variety of formats to Users and Ofgem about the operation of the shrinkage account, full details of which are provided in Appendix A to this report. A brief summary of the information provision is as follows:

INFORMATION PROVIDED TO USERS

- 1. NORM13** - shrinkage quantities supplied for each gas day in each month
- 2. NORM14** - shrinkage by month per year
- 3. SIS** - shrinkage factors
- 4. Special Condition 27 Reporting**
- 5. Shrinkage Forum**

ADDITIONAL INFORMATION SUPPLIED TO OFGEM -

- 6. SORM Reports -**
SORM2B
SORM06A
SORM16 1

- 7. AT Link access to the SP account.**

- 8. Weekly shrinkage reporting**

- 9. Special Condition 33 Reporting**

Most of the data that would be provided at D+1 will necessarily be provisional and as such Transco believes may be misleading given entry and exit close out does not occur until M+15 and D+5 respectively. Transco would therefore welcome respondents views as to how such information release could be considered to lead to better fulfill the relevant objectives.

With regard to the specific requirements of the Proposal, attendees at the NT&T workstream considered that the information categories are sufficiently developed for consultation. To ensure that interpretation of the requested data is consistent, Transco has outlined a definition in brief but does not believe there is

sufficient clarity to ensure a unique interpretation for the purposes of legal text and would therefore welcome detailed clarification from respondents. The information table is attached as Appendix B to this draft modification report.

Transco has considered the possible interactions between the gas and electricity regimes and has concluded that there would be no impact on the electricity regime if this Modification Proposal was implemented. However, respondents' views on any potential interactions with the electricity regime would be welcomed.

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

The Proposer considers that the modification would, if implemented, better facilitate the relevant objectives of the efficient and economic operation of the pipeline system for the following reasons:

- Increase competition between shippers for the provision of Shrinkage gas procurement and disposal contracts;
- Add more liquidity in the market for Shrinkage Gas management services;
- Lead to more efficient and economic Shrinkage gas management whilst lowering costs;
- Enable Shippers to better forecast their NDM/DM demand on a day;
- Enable shippers to better determine system imbalance and to achieve a more effective end-of-day balanced position;
- Enable Shippers to monitor Transco's performance vis-à-vis their Price control and Licence obligations;

With respect to the first three bullets Transco believes that the SP is currently already able to access the liquidity associated with the current gas market in a similar manner to other market participants. Transco does not believe that one player, the SP, having obligations to declare its trading position would enhance market efficiency. Indeed such data release should be expected to lead to less efficient outcomes to any User having such obligations. If that is not the case then Transco would assume that other market participants would voluntarily reveal their position. Thus Transco concludes that implementation of this Proposal would act to the detriment of the SP (and to the User community by virtue of the increased costs that would result from both trading efficiency losses and extra systems and administrative costs).

In the context of the fourth bullet,

The provision of SP trading information will have no effect on shipper NDM and DM forecasting as under current Network Code arrangements, Transco provides the NDM forecast for all Users and DM forecasting by Users should be more reliant on DM meter read history and large End User profiles than shrinkage.

In the context of the fifth bullet,

Transco is unclear as to how provision of the information required by the Proposal will enable shippers to better determine system imbalance and therefore achieve a more effective end of day imbalance.

In the context of the sixth bullet,

Transco believes it is the role of Ofgem to monitor Transco's performance under the Licence. Transco already supplies extensive information to Ofgem to support this monitoring. Transco also provides a substantial amount of shrinkage information to Users after the day and does not consider that further obligations for more information are appropriate, rather that it should have discretion to release information where it considers it would lead to more efficient and economic outcomes.

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

a) implications for the operation of the System:

Transco does not believe that implementation of this Proposal will have any implications for operation of the system

b) development and capital cost and operating cost implications:

Transco believes that development costs for setting up additional web pages and data transfers could be in excess of £50,000 and ongoing reporting support for 7 day a week operation could be around £50,000 per annum.

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:

Any additional costs arising from implementation of the Proposal would be shared with Users in accordance with the SO incentive scheme, although costs applying to LDZ shrinkage would have a direct bottom line impact on Transco.

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

Transco is unaware of any impact this Proposal would have 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 believes this Proposal increases the price risk for the SP as it's trading strategy will be exposed to all market participants

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

Transco will have to develop new web pages for publication and mechanisms to download and verify trading information from the SP

7. The implications of implementing the Modification Proposal for Users

Transco is unaware of any implications for Users in relation to this Proposal

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 implications for such Parties

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 believes it may need to advise counter parties, particularly for the NBP 1997 contract of data publication but that no other consequences are envisaged.

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

Advantages

Increased competition between shippers for the provision of shrinkage gas contracts

Increased liquidity in the shrinkage gas market

More efficient and economic shrinkage gas management

Enable shippers to better forecast their NDM and DM demand

Enable shippers to better determine system imbalance

Enable shippers to monitor Transco performance under the Licence and Price Control.

Disadvantages

Additional costs to provide the information

Transparency of trading information may lead to higher trading costs

Higher costs to Users and Transco through the SO incentive and LDZ price control

Asymmetric information provision in respect of the SP User account compared with other User accounts.

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

Representations are now sought as part of this Draft Modification Report

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

No such requirement exists in respect of this Modification Proposal

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

No such requirement exists in respect of this Modification Proposal

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

A programme of works will need to be developed to implement the reporting requirements

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

Development of a timetable will be subject to any Ofgem decision with regard to the Proposal

16. Recommendation concerning the implementation of the Modification Proposal

Transco does not recommend implementation of the Proposal

17. Text

Representations are now sought in respect of this Draft Report and prior to Transco finalising the Report

Signed for and on behalf of Transco.

Signature:

Nigel Sisman
Manager Commercial Development
NT & T

Date:

APPENDIX A - CURRENT INFORMATION PROVISION IN RESPECT OF SHRINKAGE ACTIVITY

INFORMATION PROVIDED TO USERS (full details of which are appended to this report)

1. NORM13 (quantities supplied for each gas day in each month)

Forecast shrinkage quantity - Forecast demand multiplied by the shrinkage factor
Actual shrinkage - Actual demand multiplied by the shrinkage factors for NTS, LDZ and storage
Assessed total shrinkage - Sum of the daily quantities for NTS, LDZ and storage
Assessed NTS shrinkage - Assessed shrinkage quantity

2. NORM14 (by month per year)

Forecast shrinkage quantity - Average forecast demand for a month multiplied by the shrinkage factor
Actual shrinkage - Average actual demand for a month multiplied by the shrinkage factor
Assessed total shrinkage - Average sum of the months daily quantities for NTS, LDZ's and Storage
Assessed NTS shrinkage - Average of the months daily quantities for NTS shrinkage

3. SIS

Shrinkage factor by day for NTS and LDZ's published ahead of 13.00 demand run. In addition the Information exchange website publishes the shrinkage factors and quantities after the day for the NTS and LDZ's.

4. Special Condition 27 Reporting

Under special condition 27 of its Licence, Transco is obliged to provide information on procurement activity including shrinkage which is due to be published in April 2003 for the formula year 2002 -3. This will enable Users to examine SP trading activity over the year broken down on a monthly basis. The information that Transco is proposing to publish through the Procurement Guidelines report is:

The number of trades
 The number of parties
 The quantities traded
 The unit cost of those trades (p/kwh)

5. Shrinkage Forum

Transco provides regular reporting on Shrinkage activities through the monthly Shrinkage Forum and any specific concerns Users may have in relation to SP actions as they arise can be addressed either with Transco, Ofgem or the relevant industry workstream. Furthermore Ofgem can at anytime examine SP trading activity to monitor compliance with the Licence.

ADDITIONAL INFORMATION SUPPLIED TO OFGEM -

In addition to the above, Ofgem have access to:

6. SORM Reports - Ofgem receive copies of the following reports for the SP account. Reports are provided in respect of each calendar month and provide data in respect of each gas day within the month.

SORM2B -	Input scheduling by ASEP by Gas day Final renomination quantity Allocation quantity Scheduling quantity and charge
SORM06A -	Daily cashout quantity by gas day Imbalance quantity Cashout charge/payment Industry total cashout charge/payment
SORM16 -	Monthly financial position by Gas Day Imbalance charge/payment entry scheduling exit scheduling DMA exit PRI charges Net total

7. AT Link

Ofgem has access to AT Link to monitor any User account including the SP and within day can monitor SP trades and flows by counter party, as well as measurements, allocations and charges.

Data Tables - Imbalance Clearing Table by User by day

UDQI & UDQO
Trade buys & Trade sells
Net imbalance
Imbalance charges and cashout rates

8. Weekly shrinkage reporting

Transco provides Ofgem with a daily breakdown of shrinkage trade information one week after the week to which the trades relate to. This information consists of:

Gas quantity bought at the beach	Gas quantity sold at the beach
Gas quantity bought at the NBP	Gas quantity sold at the NBP
Beach purchase WAP	Beach sells WAP
NBP purchase WAP	NBP sells WAP
Overall purchase WAP	Overall sells WAP

9. Special Condition 33 Reporting

By month, Transco provides gas cost incentive performance measures as specified in this Licence requirement.

APPENDIX B - INFORMATION REQUIREMENTS TABLE

INFORMATION REQUIREMENT	DEFINITION
DAY AHEAD - by 18.00 D-1	
Unbiased estimate of shrinkage gas requirements for the next gas day in kwh/therms Volume of shrinkage gas purchased and sold before the day	Aggregate estimate of LDZ and NTS shrinkage gas expressed in kwh as defined by section N 1.5 Notwithstanding the dates when the gas was bought and sold - the quantity (kwh) of shrinkage gas bought and the quantity (kwh) of shrinkage gas sold for all trades as defined by section N4.2.2
Number of buys and sell trades executed in respect of that gas day	Notwithstanding the dates when the gas was bought and sold the number of buy trades and the number of sell trades (as defined in section C6.)expressed separately (not including trades associated with movement of shrinkage for constraint management purposes as defined by section N4.2.2
The delivery point of all shrinkage gas bought and sold, whether at the NBP or at the beach	Notwithstanding the dates when the gas was bought and sold: 1. the quantity (kwh) of gas sold other than at the NBP 2. the quantity (kwh) of gas bought other than at the NBP 3. the quantity (kwh) of gas sold at the NBP 4. the quantity (kwh) of gas bought at the NBP.
AFTER THE DAY - by 18.00 D+1	
The final net shrinkage position in kwh/therms	The provisional net imbalance quantity of the shrinkage provider (kwh)
The volume of shrinkage gas purchased and sold on the day	Notwithstanding the dates when the gas was bought and sold - the quantity (kwh) of shrinkage gas bought and the quantity (kwh) of shrinkage gas sold for all trades as defined by N4.2.2.
The total number of buy and sell trades executed in respect of that gas day	Notwithstanding the dates when the gas was bought and sold the number of buy trades and the number of sell trades expressed separately (not including trades associated with movement of shrinkage for constraint management purposes) as defined by N4.2.2
The weighted average price of all buys and sells	Notwithstanding the dates when the gas was bought and sold - the weighted average price of all of shrinkage gas bought and the weighted average price of all shrinkage gas sold expressed separately as defined by N4.2.2.
The delivery point of all shrinkage gas bought and sold, whether at the NBP or at the beach	Notwithstanding the dates when the gas was bought and sold: 1. the quantity (kwh) of gas sold other than at the

	NBP
	2. the quantity (kwh) of gas bought other than at the NBP
	3. the quantity (kwh) of gas sold at the NBP
	4. the quantity (kwh) of gas bought at the NBP.
The minimum price at which shrinkage gas was bought	Not withstanding the dates when the gas was bought , the minimum price (p/kwh) of shrinkage gas bought under N4.2.2.
The maximum price at which shrinkage gas was bought	Not withstanding the dates when the gas was bought , the maximum price (p/kwh) of shrinkage gas bought under N4.2.2.
The minimum price at which shrinkage gas was sold	Not withstanding the dates when the gas was sold, the minimum price (p/kwh) of shrinkage gas bought under N4.2.2.
The maximum price at which shrinkage gas was sold	Not withstanding the dates when the gas was sold , the maximum price (p/kwh) of shrinkage gas bought under N4.2.2.