

Modification Report
Price change notification periods
Modification Reference Number 0655
Version 1.0

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

Transco should be obliged to publish price changes at least 3 months ahead to provide greater certainty to the market. It should also be required to publish indicative prices 3 months prior to this (ie 6 months before implementation). Furthermore, after the publication of indicative prices and before the publication of final prices, Transco should use its best endeavours to ensure that it informs Users as soon as practicable of any change to its assumptions / data that it becomes aware of that could have a material effect on the final prices published.

2. Transco's Opinion

At present, Transco's Gas Transporter Licence contains provisions governing its level of allowed revenue, the process by which it reports on performance against its revenue controls, and the process to be followed when amending the level of transportation charges. This is consistent with the regulatory frameworks of other UK network operators. However, while the Licence requires one month's notice, two is actually given in accordance with the provisions of the Network Code.

The setting of prices is not a straightforward scientific task and considerable uncertainty surrounds the estimates used of allowed and collected revenue. The two months notice period has worked well in the past as a good compromise between an adequate period of notice and getting the price changes as accurate as possible in order to keep collected and allowed revenue aligned. Transco believes that increasing the notice period to three months from two months could prove to be counter-productive, as giving earlier notice could mean that the price changes are less appropriate when they do take effect, and then further price changes may be required to correct the errors.

Rather than increase the notice period, for the reasons explained, Transco could undertake to provide to Users indicative notice of changes with more consistency than in the recent past. The Licence already requires Transco to use reasonable endeavours to give 150 days notice to Ofgem when considering any changes to the charges and these notices could automatically be made available to Users.

Transco also believes that increasing the period for indicative notice to 6 months from 150 days would not serve any useful purpose as it would make the indicative notice less accurate and therefore of far less value. Instead, Transco could undertake, on a reasonable endeavours basis, to inform Shippers of any material change to the content of the 150 day notice before the issuing of the two month's notice.

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

The proposer states that the proposal will better facilitate the Relevant Objectives of the Network Code by furthering effective competition between Shippers and Suppliers and by ensuring efficient operation of the pipe-line.

**4. The implications for Transco of implementing the Modification Proposal , including
a) implications for the operation of the System:**

If implemented, this proposal would have no impact upon the operation of the System.

b) development and capital cost and operating cost implications:

There are no development, capital or operating cost implications as a result of implementing this proposal.

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:

Not applicable.

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

If this proposal were implemented it could lead to more frequent price changes because the extended notice period would mean price changes were less appropriate by the time they came to be implemented. This could lead to greater price volatility than at present.

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

It is not anticipated that there will be a change to the level of contractual risk to Transco as a consequence of this proposal.

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

No development implications on the computer systems of Transco or on the related computer systems of Users are anticipated.

7. The implications of implementing the Modification Proposal for Users

Users would have three months notice of price changes, but price changes might be more frequent and price levels more volatile.

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

No implications are anticipated.

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

No significant consequences on the legislative and regulatory obligations and contractual relationships of Transco and each User and Non-Network Code Party are anticipated as a result of the implementation of this proposal.

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

Advantages.

- Users would have an additional months notice of price changes and increased notice of indicative changes.

Disadvantages.

- Increasing the notice period to three months from two months could prove to be counter-productive, as giving earlier notice could mean that the price changes are less appropriate when they do take effect, necessitating further price changes to correct any errors.
- An increase in the notice period could lead to greater volatility in price levels.
- Increasing the period for indicative notice to 6 months from 150 days is likely to make the information in the indicative notice less accurate and therefore of less value.

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

Transco received a total of 10 responses to this Modification Proposal :

British Gas Trading Ltd (BGT)
Scottish Power (SP)
Statoil UK Ltd (STA)
Corona Energy (CE)
Powergen UK plc (POW)
Total Gas & Power Ltd (TGP)
EDF Energy (EDF)
Association of Electricity Producers (AEP)
RWE Innogy (RWE)
Shell Gas Direct (SGD)

Eight of the ten respondents support implementation of the proposal, with the other two (RWE and EDF) offering qualified support. Of these (RWE) stated, “We do not agree that the notice period for indicative changes needs to be extended to 6 months as proposed. Instead we support Transco’s suggestion to automatically make available to Shippers any notification of changes they anticipate making, at the same time as these are provided to Ofgem under special condition 4.2.a of their Transporter Licence.” The other (EDF) questioned “whether this proposal would provide greater certainty to the market... there could be more frequent price changes to correct errors because prices are published earlier.”

Proposal to publish charges at least three months ahead

All respondents, apart from the EDF qualification (above), supported extending the notice period required from 2 to 3 months. Their view was that this would provide greater certainty in the market and hopefully reduce the associated risk premium.

Transco's Response

Transco is currently required to give two months notice to the shipping community under Section B1.8.2 of the Network Code. To increase the notice period would increase the probability that price changes might not be appropriate by the time they are introduced, especially during winter months, making further remedial changes necessary.

Proposal to publish indicative prices 6 months before implementation

All respondents, except RWE and EDF, supported the proposal to introduce an obligation on Transco to provide indicative prices 6 months before implementation. Their view was that this would extend the period of price stability, reduce the impact of price shocks, and facilitate the planning for adopting price changes for both Shippers and end consumers.

Transco's Response

Transco's GT Licence requires it to use reasonable endeavours to inform Ofgem of any proposals it is considering to change charges 150 days before the proposed date of implementation. Transco will also make available to Shippers any notices it provides to Ofgem under this Licence condition. It is difficult to see how providing indicative charges six months ahead rather than five will improve the quality of information available to Shippers. Even five months in advance it is often possible only to be clear about the direction of a price change but not about its size. In many cases even the need for a price change does not emerge until less than 150 days from the required date of implementation. In these circumstances notice would be provided as soon as possible. As a general rule the longer the notice period the less robust will be the information provided.

Proposal to publish updates between the proposed 6 months and 3 months announcements

If Transco were to publish indicative charges 6 months ahead of implementation, respondents wished to see updates to the forecast changes and explanations of the drivers behind the changes - for example, colder weather leads to over-recovery which equates to a reduction in prices.

Transco's Response

Where Transco provides 150 days indicative notice of a price change it could provide updates when it became possible to provide greater clarity.

Frequency of price changes

A number of respondents expressed concern about the perceived frequency of price changes and suggested that Transco should be limited to a small number of changes per annum. Also it was suggested that to avoid uncertainty Transco should change charges just once a year.

Transco's Response

This is not part of the original proposal and is more suited to a Licence modification. However Transco offers the following explanations. Given the separate forms of control (TO, SO and LDZ) introduced with effect from April 2002 it is inevitable that there will be more frequent changes to charges. Transco does

not consider the number of changes to be excessive. The picture has become more complex with separate controls so that now there may be three notices of changes and three implementation dates, whereas there would have been just one of each in the past. Moreover, the number of changes to each form of control tends not to currently average more than one change per formula year as the following table showing changes to the core (non-auction) prices illustrates:

	Exit		NTS Comm			LDZ Charges	
2002/03	Apr02	Provisional interpretation of new control	Apr02	0.0089	Provisional interpretation of new control	Apr02	New form of control introduced
2002/03	Jul02	Final interpretation of new control	Jul02	0.0150	Final interpretation of new control		
2002/03			Jan03	0.0177			
2003/04	Apr03	+2%				Oct03	+5%
2003/04	Dec03	Indication of increase notified					
2003/04	Apr04	Increase to be applied				Apr04	Possible reduction

Transco also proposes to introduce an NTS TO commodity charge, which would allow NTS exit capacity charges to be maintained at levels consistent with the recovery of 50% of allowed NTS TO revenue. Transco will shortly be publishing its Consultation Report for PC77, in which the NTS TO commodity charge was proposed. In this report, Transco will set out the circumstances under which it would expect to use the charge, which it is hoped will provide greater certainty and clarity for Shippers regarding the potential level of the prospective TO commodity charge.

Discussion paper

A number of respondents have suggested that a Pricing Discussion paper should be issued to take forward discussion on the whole process of price setting and related information disclosure.

Transco's Response

Transco was pleased to receive formal written opinions on this Modification Proposal as a means of initiating discussions. Transco is happy to proceed to a Discussion Paper in the New Year.

Transportation charging workgroup on price setting process

A number of respondents have suggested that they would like to see some form of transportation charging workgroup to look at the wider issues surrounding price setting and to give them a better understanding of the drivers behind collected and allowed revenue so that they can better interpret the likelihood of changes and hence lessen uncertainty and risk.

Transco's Response

Ofgem set the price controls and monitor compliance with them, however Transco would be happy to participate in such a group in the interests of spreading knowledge.

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

Implementation 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 is not required with regard to any proposed change in the methodology established under Standard Condition 4(5) of the Statement; furnished by Transco under Standard Condition 4(1) of the Licence.

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

There are no modifications required to the UK-Link Systems and therefore a programme of works will not be required as a result of implementing the Modification Proposal.

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

Transco does not recommend implementation.

16. Recommendation concerning the implementation of the Modification Proposal

Transco does not recommend implementation.

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 not to modify the Network Code and Transco now seeks agreement from the Gas & Electricity Markets Authority in accordance with this report.

19. Text

Transco does not recommend implementation of this Modification Proposal. Legal text has therefore not been provided.

Signed for and on behalf of Transco.

Signature:

Simon Griew
Charging & Forecasting Manager
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 **0655**, version **1.0** dated **23/12/2003**) 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 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.