

URGENT Modification Report
Changes to Commercial Arrangements for a Network Gas Supply Emergency
Modification Reference Number 0582

Version 4.0

This Modification Report is made pursuant to Rule 9 of the Modification Rules and follows the format required under Rule 8.9.3.

Circumstances Making this Modification Proposal Urgent:

In accordance with Rule 9.1.2 Ofgem has agreed that this Modification Proposal should be treated as Urgent because Transco is planning to conduct an exercise to simulate the response to a Network Gas Supply Emergency incorporating the various emergency types in the week commencing 22 September.

Procedures Followed:

Transco agreed with Ofgem (and has followed) the following procedures for this Proposal:

Issued to Ofgem for decision on urgency	03 September 2002
Proposal agreed as urgent	04 September 2002
Proposal issued for consultation	04 September 2002
Close out for representations	12 September 2002
Final report to Ofgem	16 September 2002
Ofgem decision expected	20 September 2002

1. The Modification Proposal

The original Modification Proposal was:

"It is proposed that for the two types of Network Gas Supply Emergency now defined in the Network Emergency Co-ordinator's Safety Case, different Network Code arrangements would apply:

- For a Network Gas Supply Emergency Gas Deficit Emergency (GDE), the present provisions of Section Q 4.1 would continue. These include suspension of gas trading on the On the Day Commodity Market (OCM).
- For a Network Gas Supply Emergency Critical Transportation Constraint Emergency (CTCE), commercial system and User balancing arrangements such as OCM trading would continue to apply throughout the emergency.

In respect of the relevant cash-out prices applied to Users' imbalances, it is proposed that no change be made to the current cash-out arrangements if the daily commercial balancing regime were suspended. This addresses a concern expressed by Ofgem in its decision letter on Modification Proposals 0502 and 0568. This related to the prospect of setting the cash-out price

in the event of a Gas Deficit Emergency to twice the arithmetic mean of the System Average Prices for the immediately preceding 30 days.

In respect of claims for financial loss it is proposed that:

- In the event of a GDE, claims for financial loss (existing paragraph Q4.2.5) would be subject to the following principles:

Allowed costs should be based on an appellant's total costs and not the cost of an individual source;

Intra-group transfers should be deemed to be made at market price;

“Windfall gains” should be netted off wherever possible;

Reasonable administrative/legal costs of making a claim should be allowed, but subsequent costs of pursuing a claim should not be; and

These costs should be limited to 5% of the net claim;

- In the event of a CTCE, the same principles would apply but, in addition, claims would only be considered in respect of gas withdrawn from storage as a result of NEC actions."

In view of the concerns raised, Transco believes it would be appropriate to reconsider the basis for claims for financial loss through a further Modification Proposal at a future stage and therefore this aspect of the Proposal has been withdrawn.

2. Transco's Opinion

Transco supports implementation of this Modification Proposal as the current emergency arrangements are most relevant to a Network Gas Supply Emergency Gas Deficit Emergency and not to a Critical Transportation Constraint Emergency.

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

Transco believes that implementation of this Modification Proposal would be consistent with the efficient operation of its pipe-line system as it would allow commercial balancing arrangements to remain in force throughout a CTCE. Retaining normal commercial arrangements would also be consistent with securing effective competition between relevant shippers and suppliers.

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

Transco, in its role as Network Emergency Co-ordinator, is already required to identify and notify shippers of the category of Network Gas Supply Emergency. However, if this Modification Proposal were implemented, Transco would no longer suspend commercial arrangements in the event of a CTCE.

b) development and capital cost and operating cost implications:

Transco is not aware of any development costs required to implement this Modification Proposal or of any implications for operating costs.

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 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 is not aware of any consequences 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 does not anticipate that there would be any consequences on the level of contractual risk to Transco under the Network Code as a result of implementation of this Modification Proposal.

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

Transco does not anticipate any development implications for its computer systems or the related systems of Users.

7. The implications of implementing the Modification Proposal for Users

Users are less likely to suffer financial loss due to better definition of the type of Network Gas Supply Emergency and subsequent financial impact.

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 such implications of implementing this Modification Proposal.

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 does not anticipate any consequences on the legislative and regulatory obligations and contractual relationships of each User and non-Network Code Party of implementing the Modification Proposal.

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

Advantages: Clearer and more effective rules and procedures for dealing with emergencies.
 Disadvantages: Transco has not identified any disadvantages.

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

Representations have been received from the following:

Respondent	Response
British Gas Trading (BGT)	Support
PowerGen (PG)	Support
Shell Gas Direct (SGD)	Support
TXU Europe Energy (TXU)	Qualified Support
Association of Electricity Producers (AssEP)	Against
Innogy (INN)	Against
Scottish and Southern Energy (SSE)	Against
TotalFinaElf Gas and Power Ltd (TFE)	Against

Cash-out Incentives

BGT and PG supported the Proposal, but expressed disappointment that Ofgem did not feel able to implement the full recommendations of the GIEC Commercial Market Implications Work Group (CMIWG), particularly in relation to providing adequate cash-out incentives. BGT commented that "In the event of a Gas Deficit Emergency, the neutral cash-out proposed will provide weaker signals for shippers to alleviate any shortfalls than the mechanism recommended by GIEC." BGT recommended further industry discussion "to address the unresolved issues of determining an acceptable cash-out regime in the event of a Gas Deficit Emergency."

AssEP, INN and TFE, were unable to support implementation of the Modification Proposal. TFE's principal objection was the lack of adjustment to the existing "cash-out arrangements should the daily commercial balancing regime be suspended." In continuation of its support of the work that was done by the CMIWG, TFE was of the opinion that "the exclusion of the cash-out calculations (originally proposed in Mod 502 and subsequently revised by Mod 568) leaves shippers exposed to an unacceptable commercial risk associated with potentially extreme short term cash out prices generated as a consequence of a network emergency." TFE "strongly oppose Ofgem's views on the arbitrary nature of the mod 502 and mod 568 cash out proposals which were cited in its rejection of both proposals." INN noted that whilst the Proposal "contains no explicit changes to the cash-out prices regime, there is an implicit change due to the different cash-out treatments for the different types of emergency."

Transco Opinion

Transco confirms the different cashout regime would apply in the two types of emergency. It does not, however, believe that Users' behaviour, in a GDE type of emergency would be significantly influenced by the multiplier used in the cashout regime.

Transco notes respondents' views regarding the proposed neutral cashout incentive, together with Ofgem's view that any changes to the existing cashout arrangements would be arbitrary. However, in order to progress this Modification Proposal, which would bring the Network Code emergency definitions in line with the Safety Case, Transco proposes that the debate should be reopened within the appropriate industry forum.

Windfall Gains

INN confirmed that it is still not "wholly comfortable with the arrangements for financial loss and would prefer a clearer definition of "windfall gains"."

SGD referred to the discussion at GIEC on introducing a basis for claims for financial loss, but felt "this approach may create an unacceptably high level of claims."

Transco Opinion

Transco notes INN's and SGD's comments and believes that in view of the concerns raised, it would be appropriate to reconsider this through a further Modification Proposal at a future stage and therefore this aspect of the Proposal has been withdrawn. Transco would welcome further debate of these issues in the appropriate industry forum to inform the content of a future Modification Proposal.

Possible Interaction of the Emergency Regimes in the Gas and Electricity Markets

AssEP did not support implementation of the Modification Proposal. Whilst in support of the definition of the two types of emergency and accepting that different cashout arrangements "may well be an improvement on the current situation", AssEP supported Ofgem's view, in its rejection letter for Modification Proposal 0502 and 0568, in that more consideration should be given to the interactions between the gas and electricity markets in an emergency. TXU expressed a similar view. INN remained in support of the definition of the two types of Network Gas Supply Emergency as detailed in its response to Modification Proposals 0502 and 0568, but reiterated its argument that the interaction between the gas and electricity markets "had not been fully considered." SSE indicated its willingness to participate in further detailed discussions on these issues.

SGD responded to Ofgem's concerns regarding interactions between the gas and electricity markets and commented that this was a "commercial risk about which power station must be aware and is one of the reasons why they have been encouraged to have back-up fuel on site."

Transco Opinion

Transco would welcome further debate on the interaction between the gas and electricity markets during an emergency and proposes that this issue is placed on the agenda of the next

meeting of the appropriate industry forum. Transco would agree that interruptible users might be expected to have back-up fuel supplies available.

As stated above, Transco has withdrawn the appeals definition part of this Modification Proposal and this would allow the market interaction issues to be further explored.

Exercise Jeopardy & Urgent Status

TXU welcomed the differentiation of the two types of emergency, but registered concern over the granting of urgent status to the Modification Proposal and hence offered qualified support. TFE registered concern "at the delays in decisions to reject both of the earlier proposals that have now resulted in urgent procedures for this modification in order to accommodate revised proposals within the scope of the forthcoming emergency simulation exercise." AssEP quoted Ofgem's reasons for the rejection of Modifications 0502 and 0568 and expressed surprise "that modification 582 was raised and granted urgent status" since it only addressed Ofgem's concern regarding the need to increase emergency cashout prices.

AssEP, TXU, SSE and INN confirmed they found it difficult to understand why the Network Code required changing on an urgent basis to accommodate the forthcoming emergency exercise. SSE additionally commented that as the two types of Network Gas Supply Emergency are now defined in the Network Emergency (NEC) Safety Case "Surely the change to the Safety Case alone gives sufficient vires to allow Transco, as NEC, to carry out the simulation?"

Transco Opinion

Exercise Jeopardy has been planned during week commencing 22 September 2002, with the agreement and involvement of the DTI and the industry, to test the effectiveness of the two types of emergency. Transco would not normally expect participation in an exercise unless the underlying operational and commercial regime was consistent with the scenarios being adopted. It would also doubt the validity of the results obtained and how they might be applied to inform the procedures to be followed in an emergency. Transco therefore proposed urgent procedures, which Ofgem accepted was appropriate.

Additional comments

INN advised that it understood that the DTI would shortly be consulting on a revised Fuel Security Code and suggested that "a co-ordinated approach to consider how the gas and power markets interact under emergency conditions would be appropriate. In our view, the conclusions and way forward set out in Ofgem's 0502/0568 decision letter could form a useful starting point for further analysis."

SGD noted that in Ofgem's decision letter on Modification Proposals 0502 and 0568 that reference was made to a report by NGC and Transco. As shippers had no access to this document, SGD drew into question the purpose of the consultation and as to whether "representations can be properly informed if there is substantial information lacking."

Transco Opinion

Transco is not of the opinion that implementation of this Proposal would be inconsistent with any DTI consultation on a revised Fuel Security Code, nor, with any report that has been produced jointly by Transco and NGC.

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 requirement.

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 requirement.

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

Material changes would be required to NEC and GT procedures.

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

Transco recommends implementation of this Modification Proposal as soon as possible in order to bring its Safety Case and Network Code into alignment, and to validate the results of an emergency exercise scheduled for week commencing 22 September 2002. This exercise will include simulation of the two proposed emergency types.

16. Recommendation concerning the implementation of the Modification Proposal

Transco recommends that this Modification Proposal be implemented.

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

Amend paragraph 1.2.3 to read as follows:

“1.2.3 For the purposes of the Code:

- (a) a “**Network Gas Supply Emergency**” is a network gas supply emergency (as referred to in the NEC Safety Case), namely a Gas Supply Emergency which involves or may involve a loss of pressure in the NTS;
- (b) a “**Network Gas Supply Emergency Gas Deficit Emergency**” is a Network Gas Supply Emergency which arises as a result of:
 - (i) deliveries of gas to the System being insufficient for the purpose of meeting demand for gas on the System;
 - (ii) or a Transportation Constraint affecting the deliveries of gas to the System;
 - (iii) or a Transportation Constraint on the System which does not prejudice the ability of Users to offtake gas from the System;
- (c) a “**Network Gas Supply Emergency Critical Transportation Constraint Emergency**” is a Network Gas Supply Emergency which is not a Network Gas Supply Emergency Gas Deficit Emergency; and
- (d) any other Gas Supply Emergency is a “**Local Gas Supply Emergency**” (that is, local gas supply emergency as referred to in the NEC Safety Case).”

Amend paragraph 3.1.1 to read as follows:

- “(i) . . . whether it is a Potential Network Gas Supply Emergency or of the Stage thereof, and (in the case of a Network Gas Supply Emergency which is not a Potential Network Gas Supply Emergency) whether it is a Network Gas Supply Emergency Gas Deficit Emergency or a Network Gas Supply Emergency Critical Transportation Constraint Emergency, and (in the case of any Gas Supply Emergency), in so far as reasonably practicable, of the nature, extent and expected duration . . .
- (ii) . . . and material developments in respect of the Gas Supply Emergency (including, without limitation, any determination made by Transco pursuant to paragraph 3.5.1); and
- (iii)”

Amend paragraph 3.2.2 to read as follows:

“In a Network Gas Supply Emergency Gas Deficit Emergency the application of Section D . . . from the time the Network Gas Supply Emergency Gas Deficit Emergency was declared . . . duration of a Network Gas Supply Emergency Gas Deficit Emergency, Transco will not take . . .”

Amend paragraph 3.3.2 to read as follows:

"In a Network Gas Supply Emergency Gas Deficit Emergency each User shall comply . . ."

Amend paragraph 3.3.3 to read as follows:

“In any Network Gas Supply Emergency Transco may (where appropriate, in lieu of applying...”

Renumber paragraph 3.5 as paragraph 3.6 and insert a new paragraph 3.5 as follows:

“Network Gas Supply Emergency Critical Transportation Constraint Emergency”

3.5.1 If, in the event of a Network Gas Supply Emergency Critical Transportation Constraint Emergency, Transco determines at any time that the application of Section D may have a detrimental effect on Transco’s immediate ability to take Emergency Steps in accordance with paragraph 1.3.1 above, then the application of Section D (other than paragraph 2.4 thereof) will be suspended with effect from such time as may be determined by Transco and notified to Users pursuant to paragraph 3.1.1(ii) and in respect of any later Gas Flow Day falling within the duration of a Network Gas Supply Emergency Critical Transportation Constraint Emergency. Transco will not take any Market Balancing Actions from such time and (in lieu thereof) the Emergency Procedures will apply and Transco’s decisions as to the delivery and offtake of gas to and from the System will be implemented pursuant to paragraphs 3.3 and 3.4.

3.5.2 In the event that paragraph 3.5.1 applies, the provisions of paragraphs 3.3.2, 4.1.1 and 4.2 shall, from the time determined by Transco pursuant to paragraph 3.5.1, apply mutatis mutandis to the Network Gas Supply Emergency Critical Transportation Constraint Emergency as if all references in such paragraphs to a Network Gas Supply Emergency Gas Deficit Emergency were to the Network Gas Supply Emergency Critical Transportation Constraint Emergency.

Amend paragraph 4.1.1 to read as follows:

“In respect of each Day or part of a Day during a Network Gas Supply Emergency Gas Deficit Emergency:

- (i) . . . Daily System Entry Capacity . . . ;

...

(viii) . . .; and

(ix) . . . provisions of Section G.”

Amend the title of paragraph 4.2 to read as follows:

“Clearing of gas balances following a Network Gas Supply Emergency Gas Deficit Emergency”

Amend paragraph 4.2.1 to read as follows:

“In a Network Gas Supply Emergency Gas Deficit Emergency Section F2 will apply . . .”

Amend paragraph 4.2.2 to read as follows:

“In respect of each Day during a Network Gas Supply Emergency Gas Deficit Emergency:

(i) . . . ;

(ii)”

Amend paragraph 4.2.3 to read as follows:

“...by reference to the 30 Days preceding the Day on which the Network Gas Supply Emergency Gas Deficit Emergency started.”

Amend paragraph 4.2.4 to read as follows:

“In applying Section F4 in respect of Days during a Network Gas Supply Emergency Gas Deficit Emergency amounts payable by Transco . . . (for the purposes of Section F4.4.3).”

Amend paragraph 4.2.5 to read as follows:

“ . . . in respect of any gas delivered to the System on a Day during a Network Gas Supply Emergency Gas Deficit Emergency (but not in respect of . . .

Renumber existing paragraph 4.3 as 4.4 and add new paragraph 4.3 to read as follows:

"4.3 Consequences of Network Gas Supply Emergency Critical Transportation Constraint Emergency

4.3.1 Save where paragraph 3.5.1 applies (in which event this paragraph 4.3 shall be of no effect), where a User (the “claimant”) believes that it will suffer a financial loss in

respect of any gas delivered to the System on a Day during a Network Gas Supply Emergency Critical Transportation Constraint Emergency in accordance with Transco's instructions to the operator of a Storage Facility (in which the User had gas-in-storage) pursuant to paragraph 3.3.3:

- (a) the claimant may within such time as Transco shall reasonably require submit to Transco a claim in respect of such financial loss together with details of the basis on which it believes it will suffer such loss and the amount thereof;
- (b) Transco will appoint an independent accountant or other appropriately qualified person as "claims reviewer" to review each claimant's claim and advise Transco of whether the claim appears to the claims reviewer to be justified and the amount which (in the claims reviewer's opinion) the claimant should be paid so that it will not suffer such financial loss;
- (c) the claimant shall be required (as a condition to its claim being considered, but subject to the claims reviewer accepting a reasonable obligation of confidence) to provide such information, access to records and cooperation as the claims reviewer shall reasonably require;
- (d) the fees and costs of the claims reviewer shall be paid by Transco and shall be additional Monthly Adjustment Neutrality Costs for the month in which they are paid; and
- (e) Transco will (after consultation with the claimant and the Director) pay to the claimant the amount advised by the claims reviewer (unless on Transco's application after consultation with the claimant the Director shall give Condition 7(4) Approval to Transco's paying a different amount).

4.3.2 Save where paragraph 3.5.1 applies, in applying Section F4 in respect of Days during a Network Gas Supply Emergency Critical Transportation Constraint Emergency:

- (a) amounts payable by Transco to Users pursuant to paragraph 4.3.1; and
- (b) all such costs as Transco may reasonably incur pursuant to paragraph 3.4,

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 **0582**, version **4.0** dated **18/09/2002**) 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 **4.0**.

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.