



Direct Dial: 0171-932-1669

22 July 1998

Your Ref:

Our Ref: Net/Cod/Mods/244to247

To: Transco, Shippers and other interested parties

Dear Sir or Madam,

Re: Urgent Modification Proposals 244 to 247

Six modification proposals, reference numbers 242 to 247, have been received from Enron for urgent consideration. These proposals have been formulated by AGAS, Alliance Gas, Enron, Dynegy UK (previously NGC) and Shell Gas Direct.

This letter deals only with modifications 244 to 247. For each of these modifications, we have stated whether or not the Director accepts that the network code may require modification as a matter of urgency. The letter also provides Ofgas' initial views on each of the modification proposals. Ofgas will make a final decision having received the relevant modification reports.

Ofgas is still considering whether proposals 242 (Special Storage Deliverability Services), and 243 (revision of Rough Services) should follow the urgent modification route.

Urgent Modification proposal 244, Reduce Overrun Charges

Ofgas accepts that this modification should follow the urgent route so that implementation is possible at the earliest possible opportunity before 1st October when there is likely to be a large change in capacity bookings because of the start of the new gas year. Urgent consideration will also allow modification proposal 230, Changes to System Entry Capacity Rules, to be developed and implemented before 1st October. Transco has agreed that the modification should proceed to the following timetable: -

Modification proposal to be circulated to interested parties	Wednesday 22 July
Consultation responses to Transco	5:00 p.m. Friday 21 August
Final modification report to Ofgas	Friday 28 August
Ofgas decision expected	Friday 4 September
Implementation	ASAP

Ofgas considers that the current level of system entry overrun charges is set too high. As a consequence, beach and stored gas is discouraged from being brought to the market, especially at peak times. There also appears little to justify the differential overrun multipliers between

peak storage connection points and all other points. Furthermore, Ofgas noted in its acceptance of urgent modification 94 (Capacity Overruns 1st March 1996 to 31st September 1996) that the capacity booking and overrun regime would benefit from further consideration. This was especially so in respect of the crude ratchet mechanism which was designed to alleviate consecutive exit overruns occurring whilst overruns continued to be calculated on a calendar month rather than rolling month basis. We note that this modification proposal seeks to remove the need for a ratchet by moving to an overrun applied on a daily basis.

It is Ofgas' initial view that a significant reduction in the overrun multiplier would better facilitate the relevant objectives. However, there are a number of issues that will need to be addressed in the final modification report.

First, it is not clear how the daily overrun multiplier 8, set out in the modification proposal, was arrived at. Doug Wood, Enron, has agreed to make available the derivation of this multiplier.

Second, in a shipper paper submitted to Ofgas supporting these modification proposals¹, a "normal winter load duration curve" was used to produce the multiplier. It is argued that over time the chosen multiplier would ensure that the revenue Transco receives from capacity bookings and/or overruns would be maintained. Even if this were the case, Ofgas is concerned that this could lead to unnecessary volatility in the revenues that Transco receives. This in turn could lead to unnecessary volatility in the prices charged by Transco. This could arise even if shippers were "indifferent between booking lower levels of capacity and paying overrun charges on more frequent occurrences of breach". Transco's revenues from overruns year on year may vary as temperatures deviate from seasonal normal temperatures over time. To avoid this it is likely that the overrun multiplier would need to be higher than would otherwise be the case.

Third, it may be more appropriate to use the load duration curve of the peakiest shipper, for example a domestic-only shipper, rather than an 'average' shipper to formulate the level of the multiplier. Consideration could also be given to producing terminal specific analysis rather than averaging across all terminals. This could also lead to an increase in the level of the multiplier.

To enable issues related to this modification to be addressed, discussions will take place at the Capacity workstream currently scheduled.

Urgent Modification proposal 247, Alignment of Capacity and Flexibility Overrun Charges

Ofgas accepts that this modification should also follow the urgent route so that implementation is possible at the earliest possible opportunity before the start of the new gas year on 1st October. Furthermore, the level to which overruns should align is not covered by this modification. Therefore, this modification should follow the same timetable and be considered in parallel to modification proposal 244, Reduce Overrun Charges. To enable issues related to this

¹ Gas Balancing Regime, 1998 Consultation, Short Term Proposals, 2 July 1998. Produced by AGAS, Alliance Gas, Enron, Dynegy UK and Shell Gas Direct.

modification to be addressed, discussions will take place at the Capacity workstream currently scheduled.

It is Ofgas' initial view that capacity and flexibility overrun charges need to converge, otherwise gas may be channelled to the flexibility mechanism rather than sold to other shippers within day. This change would also facilitate the move to a single market covering shipper-to-Transco and shipper-to-shipper trades. However, the level of overruns to which the two regimes should converge is for consideration under modification proposal 224.

Urgent Modification proposal 245, Remove barriers to On-the-day- Trading

Though Ofgas would welcome less restrictive rules on matching renominations to accompany acquiring and disposing trades at the NBP, we do not believe that the changes proposed in this modification could be introduced in time for this winter. Therefore, Ofgas does not accept that this modification should follow urgent procedures.

Over the last few months, Ofgas and Transco have discussed in detail the current nomination regime. Ofgas hoped that these discussions would lead to proposals to improve the information which Transco receives whilst providing shippers with greater flexibility to meet their own balancing requirements. These discussions have not resulted in any proposals for change.

It is likely that significant changes to the nomination regime for this winter will not be possible because Transco has indicated that these changes require consideration of their safety case. Transco would need to submit any material change to their safety case to the Health and Safety Executive (HSE) for their consideration before changes could be introduced. Any considerations by Transco and the HSE are not likely to be completed quickly.

Following the publication later this month of Ofgas' conclusions document "An on-the-day commodity market for a gas balancing regime", it is our intention to launch a review of the nominations regime. The issues contained in this modification are likely to be considered in that review. We would expect the energy workstream to consider what changes could be made to the nomination regime without materially affecting Transco's safety case so that they could be introduced for this winter.

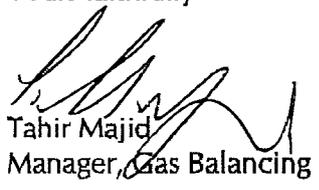
Urgent Modification proposal 246, Remove Constraints costs from Balancing

In addition to removing the recovery of the costs of constraints from neutrality (Transco and not shippers would pay for constraint costs) the modification proposes to better identify and separate from supply/demand matching the costs of constraints. Ofgas welcomes better separation of the costs of constraints. However, Ofgas does not consider that this modification should follow urgent procedures. This modification proposal should be considered at the energy workstream.

It is Ofgas' initial view that Transco should eventually pay for the entire costs of managing transportation constraints. However, though we are still finalising our "On-the-day Commodity Market" conclusions document, we conclude that Transco should be incentivised for the costs

of supply/demand matching and managing transportation constraints at an earlier date than that which was envisaged in the Ofgas consultation document. Provisionally this would occur in April 1999.

Yours faithfully



Tahir Majid
Manager, Gas Balancing