

Dear Colleague,

Please be advised that the amended gas quality specification will be implemented upon execution of the Network Entry Agreement between Transco and the Delivery Facility Operator.

It is the intention of both parties that this should be signed in readiness for a 1 October 2004 implementation.

An update will be provided in due course.

Please note that a completely 'random' date of 01/01/9999 has been inserted to enable generation of this Implementation Notice.

**NOTICE OF REVISED IMPLEMENTATION
MODIFICATION PROPOSAL No: 0707**

"Amendment of Network Entry Provisions at Total E&P UK sub-terminal at St. Fergus"

Please note that Modification Proposal No 0707 will be implemented with effect from 06:00 hours on 01/01/9999. The Final Modification Report, Version 2.0, was signed by Ofgem on 13/08/2004.

The new Network Code text resulting from this Modification follows.

Modified Text:

Revised Network Code legal text is not required as implementation would be achieved via execution of the NEA.

Annex – Transco note on costs as circulated on 22nd July 2004

Network Code Modification Proposal 0707: Amendment to Network Entry Provisions at Total E&P UK sub-terminal at St. Fergus - cost implications

Background

As indicated in Ofgem's letter of 14 July 2004 granting urgent status to Modification Proposal 0707, Transco has been asked to set out its views of potential cost implications on its system were Modification Proposal 0707 to be implemented. In the Modification Proposal, the proposer indicates a requirement for amendment of Network Entry Provisions by way of a Network Code Modification once Transco and the Delivery Facility Operator have agreed to change the Network Entry Provisions and to incorporate these in a Network Entry Agreement. When considering the potential costs associated with implementation of the Proposal, Transco has therefore assumed that the proposed Network Entry Provisions are implemented in a Network Entry Agreement.

Cost implications

The financial impact across Transco's system of any change to the gas quality specifications at a System Entry Point would be expected to reflect the resulting change in the quantity and quality of gas entering the system at that System Entry Point. However, any change in gas flow at one System Entry Point will, given no change in demand, be offset by equal and opposite flow changes elsewhere. It is difficult to accurately predict the likely change in gas flows over time at either St. Fergus or other entry points which might be anticipated were this Modification Proposal to be implemented.

This note focuses on the potential cost impact associated with Transco's operation of the NTS. However, perhaps the largest potential cost impact would arise as a result of any change in the gas price as a result of implementing this Modification Proposal. Views on the likely scale of such an impact would be welcome, but Transco would observe that, if implementation of the Modification Proposal were to lead to a change in the pattern of gas supplies entering the NTS, it would be reasonable to assume that this would be because lower cost supplies were available. Other things being equal, it would be expected that the highest cost supplies would be displaced, such that the marginal cost of gas should be expected to fall. If competition in the market is effective, the availability of lower cost supplies should lead to reduced gas prices and a potential benefit for all gas consumers.

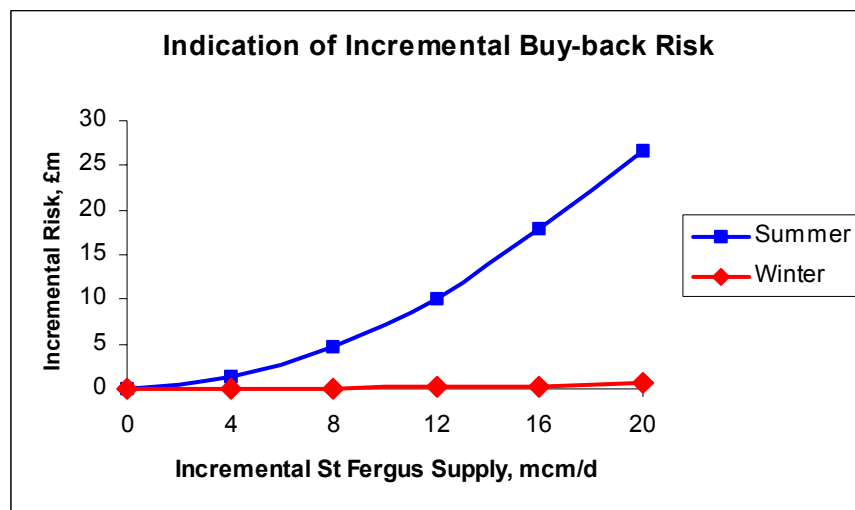
Transco has also considered the likelihood that implementation of the Modification Proposal would impact its NTS investment plans. At this stage, Transco would not anticipate changing its investment plans were the Modification Proposal to be implemented. This may change, however, if future auction signals reveal that the release of incremental entry capacity is justified.

System Operation Cost Impacts

Entry Capacity Buy-Back Costs

If the consequence of implementing this Modification Proposal is that the proportion of demand met by supplies from St. Fergus is higher than would otherwise be the case, there would be a potential increase in the cost of managing entry capacity constraints at St. Fergus. Transco would not anticipate any offsetting saving in buy-back costs at other entry terminals in the immediate future.

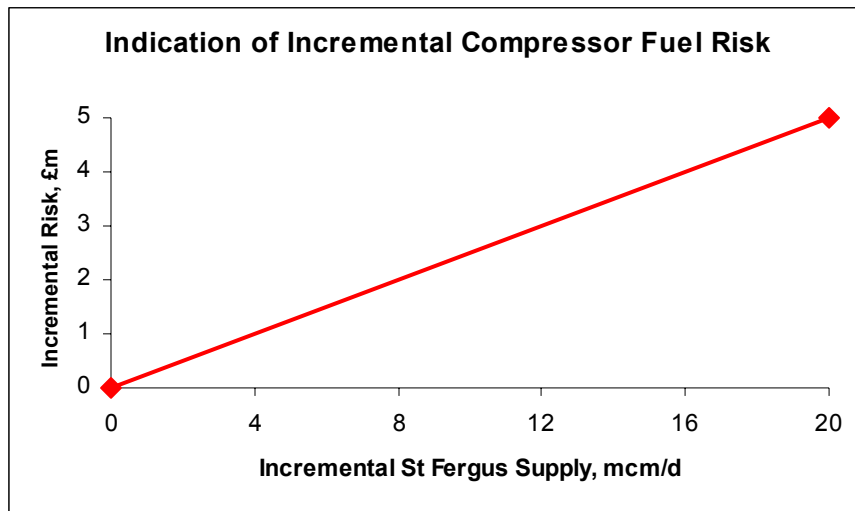
To illustrate the potential change in buy-back costs, Transco has considered the potential impact were implementation of the Modification Proposal to lead to a sustained increase (i.e. increased on each and every day) in desired flows at St. Fergus. As an indication of the possible impact, Transco has modelled, based on 2004 data, the potential change in spot buy-back costs were Shippers to seek to flow up to an additional 20mcm/d throughout the period April 2004 to March 2005. Buy-back costs tend to be volatile and difficult to accurately predict, and hence any modelling results should be interpreted as no more than indicative of the potential costs assuming no ameliorating action was undertaken – such as investment in additional physical capacity or through commercial actions. The modelled results for differing additional flow levels are summarised in the graph below, which shows the average cost which emerges from a relatively wide modelled range, for Summer and Winter. The results suggest that if Shippers were to seek to deliver a sustained increase in flows from St. Fergus throughout the whole period, above the level seen since March to date this year and above the level Transco presently anticipates for the remainder of the year, potential buy-back costs could increase materially in the Summer. The more limited potential Winter impact is largely a reflection of an assumption that maximum flows would effectively be capped by the level of available entry capacity, whereas in Summer the available capacity rights generally leave significant headroom against which additional flows can be nominated.



NB: The graph illustrates the potential buy-back risk if Shippers desired flows increase on each and every day during the period.

Shrinkage Costs

If flows from St. Fergus increase as a consequence of implementing this Modification Proposal, this would be expected to increase the costs of compression needed to ensure the gas is transported to the remainder of Transco's system. As for entry capacity buy-back costs, Transco has modelled the potential impact of a sustained incremental daily flow at St. Fergus of 20mcm/d, given no change in NTS demand, on the costs of compression for 2005/06. This indicates a potential increased annual compression cost of £5m as a central estimate within a potentially wide range which depends on actual gas costs and the entry points from which flows are displaced. The graph below illustrates the potential incremental costs assuming a linear relationship between compression costs and additional flows at St. Fergus.



NB: The graph illustrates the potential annual compressor fuel risk if flows increase on each and every day.

Other Costs

While Transco would not anticipate other material cost impacts in the immediate future as a result of implementing this Modification proposal, additional costs may arise. For example, if the proportion of demand met by supplies from St. Fergus is higher than would otherwise be the case, there could be an increase in the number and consequently cost of locational OCM buy actions at other system entry points. This could become necessary to secure sufficient security in specific areas of the network, particularly the South.

There may also be a positive financial impact on Transco and Shippers through the entry capacity buy-back incentive scheme as a result of implementing the Modification Proposal. If Shippers seek to increase aggregate flows at St. Fergus and purchase additional entry capacity rights as a consequence, this would increase revenue attributed to Transco's entry capacity buy-back incentive scheme to the extent that the capacity sold was non-obligated, interruptible, or sold within-day – and not offset by a revenue reduction elsewhere.

Transco would also observe that were additional supplies to be available to the system as a result of implementation of the Modification Proposal, this could enable additional demand to be supported, for example in severe Winter conditions. To the extent that this was the case, there may be potential for top-up costs to be avoided.

Yours sincerely,

Julian Majdanski
Modification Panel Secretary