

CODE MODIFICATION PROPOSAL No xxxx
<Revision of the Post-emergency Claims Arrangements>
Version x.x

Date: 31/05/2009

Proposed Implementation Date: October 2009

Urgency: Non Urgent

1 The Modification Proposal

Nature and Purpose of this Proposal

a)

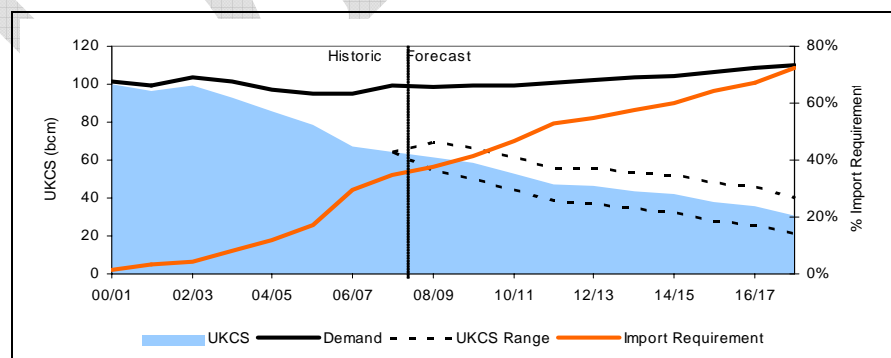
Background to the Proposal

Over the past few years, the gas emergency arrangements within the Uniform Network Code (UNC) have been the subject of much industry debate. This has included discussion associated to the projected reduction of the gas supplies sourced from the UK Continental Shelf (UKCS) with the consequence that the GB market will become more dependent on gas imports from Norway, continental Europe and the global Liquefied Natural Gas (LNG) markets; collectively known in this Proposal as non-UKCS gas supplies.

A related issue raised by the industry relates to the increased GB dependence on non-UKCS gas supplies and the effects this might have should a Network Gas Supply Emergency/Gas Deficit Emergency be declared. It is worth noting that in the event a Gas Deficit Emergency is declared, neither the Network Emergency Co-ordinator (NEC) nor HM Government (including DECC or Ofgem) have any legal vires to direct non-UKCS gas supplies into the GB market.

The extent to which the GB gas market will become dependent on the future importation of non-UKCS gas supplies is demonstrated by Graph 1 – UKCS Annual Supplies and Demands, and is based on the historic and forecast utilisation of proven UKCS supplies

Graph 1 – UKCS Annual Supplies & Demands (2008 Annual 10 Year Statement)



In the event of a Gas Deficit Emergency, Users do however have legal obligations under their Shipper Licences and ostensibly, the Gas Safety (Management) Regulations (GSMR) to maximise their UKCS gas flows and, where directed, reduce their firm demand-side flows when instructed to do so by the Transporter (NEC). These safety obligations are reflected within the UNC insofar as Users must comply where directed by the Transporter to maximise UKCS flows and/or reduce demand offtakes and that the Users' (and the Transporter) business interests are subordinate in the event of a Gas Deficit Emergency.

In February 2009, National Grid NTS, in conjunction with the wider industry, initiated a review of the UNC emergency arrangements with the primary objective of developing, and implementing, robust and well defined revisions that;

Facilitate:

- New and enhanced commercial arrangements so that Users might mitigate the onset or, reduce the potential length and/or severity of a Gas Deficit Emergency and;
- Improved alignment between the Users' Licence/GSMR safety obligations and those of the UNC emergency arrangements.

Recognise Users that:

- Put in place commercial arrangements prior to a Gas Deficit Emergency occurring;
- Provide additional non-UKCS gas supplies into the GB market during a Gas Deficit Emergency; giving confidence to those Users that they will receive an appropriate level of financial recompense based on a market value of the gas supplied;
- Contract for further self-interruption of demand prior to a Gas Deficit Emergency (up to Stage 3); giving confidence to those Users that they will receive an appropriate level of financial recompense based on a market value of the gas interrupted and;
- Seek to address their imbalance.

Introduce:

- Full market transparency and auditability (of costs and prices) through the use of On-the-day Commodity Market (OCM) Physical Market Offers during a Gas Deficit Emergency.
- The ring-fencing of the costs of providing additional supplies/self-interruption of demand during a Gas Deficit Emergency.
- A dampened cost apportionment as a result of revised post-emergency claims arrangements.

We consider this Proposal might encourage additional non-UKCS supply and/or demand-side response during a Gas Deficit Emergency however, this Proposal is not intended to (and cannot) mitigate the issues associated to the future national security of supply e.g. the GB market's increased dependence on gas importation. On balance, we believe that this Proposal (should it be implemented) would represent an incremental step to enhance the existing commercial framework and that it might be considered in a wider, HM Government-initiated review of the UK Security of gas Supply arrangements.

Associated Industry Concerns – User risks

Debates relating to UNC emergency arrangements have resulted in numerous Proposals¹ being raised over the years. During the development of these Proposals, Users have raised several common concerns which they believed should be considered and addressed within any future revisions to the emergency arrangements.

Common concerns that have been expressed by Users include:

- Market manipulation (of prices)
- High System Marginal Price (SMP) could excessively penalise Users that are unable to respond to an emergency cash-out price.
- The ‘domino effect’ associated with credit and securities during an emergency and the potential for multiple User failures.

Emergency Cashout Prices

The industry has previously highlighted concerns that any revisions to the UNC emergency arrangements should not subject Users to disproportionately inflated gas prices during a Gas Deficit Emergency, and that any proposals should consider how the industry exposure to the likelihood of extreme cashout prices for additional gas supplies could be appropriately managed.

National Grid NTS believes that any enhancements to the UNC emergency arrangements are mindful of the balance between providing a cashout price that does not excessively penalise Users who are unable to respond, whilst encouraging additional non-UKCS gas into the GB and/or further demand-side reductions during a Gas Deficit Emergency.

A common view expressed by Users is that there is a potential conflict between the UNC commercial arrangements at a time where ‘physical’ Users are obliged to operate in accordance with their GSMR Licence obligations, particularly where such commercial arrangements have had no particular alignment to their legal safety obligations.

Some Users have concerns associated with risk of the exposure to potentially spiralling cashout prices that might be over-inflated as a result of market behaviours on the OCM during a Gas Deficit Emergency i.e. not all Users carry the same level of risk to spiralling prices. It was highlighted that it is those ‘physical’ Users that are subject to Balancing Neutrality which carry the greater risk of being exposed to the potential costs of Users defaulting as a consequence of a Gas Deficit Emergency and that such costs may have been caused by spiralling emergency cashout prices.

There is a consensus within the industry that the greatest risk of exposure to the costs incurred as a result of imbalance positions arising from a Gas Deficit Emergency is largely attributed to those predominantly physical ‘demand-side’ Users. National Grid NTS has however undertaken analysis (Graphs 2a/2b) that indicates it might be more appropriate to attribute the greater risk of imbalance cost exposure to the predominantly physical ‘supply-side’ Users who sell the majority of their supplies into the NBP.

¹ 044 "Revised Emergency Cash-out & Curtailment Arrangements" (ECQ); 061 "Facilitating further demand-side response in the event that a Gas Balancing Alert is triggered" (GBA); 0149/a "Gas Emergency Cashout Arrangements: Keeping the OCM open during a Gas Deficit Emergency (GDE)"

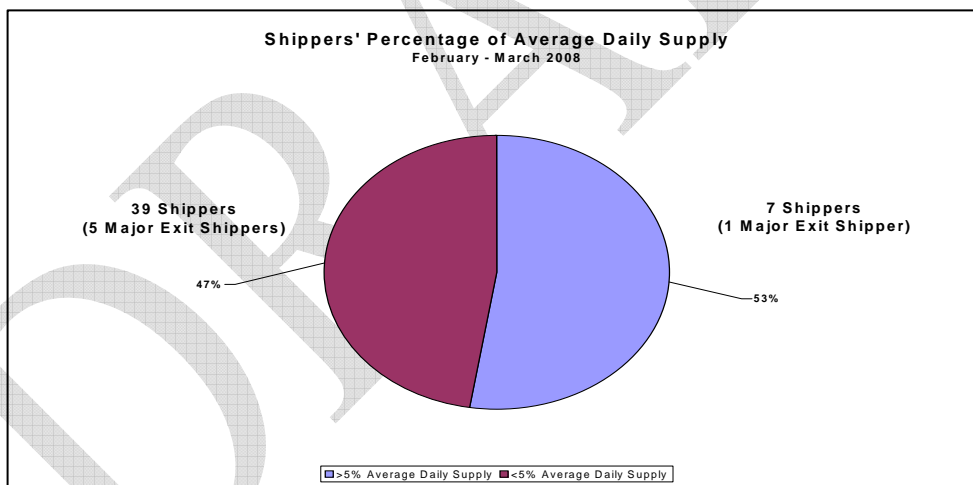
As can be determined from the analysis, 5 Users account for approximately 75% of physical demand but are included within 39 Users that provide approximately 47% of physical gas supplies to meet UK demand.

National Grid NTS understands that those predominantly 'demand-side' Users acquire a greater proportion of their supply requirements through the use of trading and bilateral contracts at the NBP. We are also aware that for the purposes of NBP gas trading through the standard NBP '97 contract, trading parties cannot claim 'Force Majeure' in the event of a National Gas Supply Emergency.

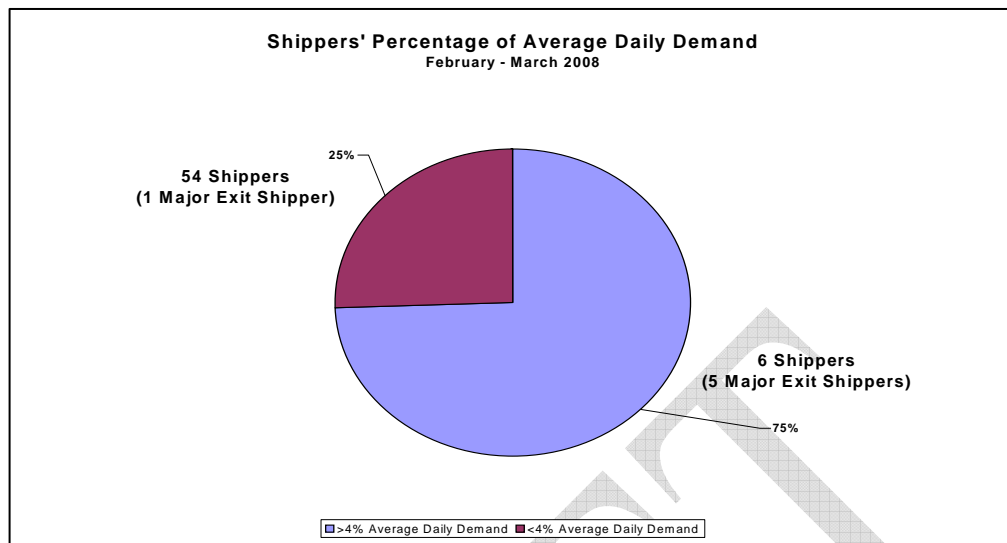
From the analysis (Graphs 2a/2b) and the terms of the NBP '97 contract, it might be inferred that where a Gas Deficit Emergency is the result of a supply-side failure, for example, a beach terminal failure, then an affected 'supply-side User' might have greater exposure to significant energy imbalance costs.

We believe that in the event of a Gas Deficit Emergency, those predominantly 'demand-side Users' that source supplies through NBP gas trade contracts may have less risk of exposure to imbalance costs. This risk might be further mitigated through the contracting of self-interruption of demand prior to the NEC declaring a Gas Deficit Emergency Stage 3 (Firm Load Shedding)

Graph 2a - Determination of the Users - Entry/Exit Split;



Graph 2b - Determination of the Users - Entry/Exit Split;



Energy Balancing Credit Cover during a Gas Deficit Emergency

National Grid NTS considers that the proposed improvements in the transparency of the prevailing emergency claims arrangements with the provision of *potential* 'emergency claims' information (prices and quantities) to the market *during* a Gas Deficit Emergency may facilitate improvements in the management of Energy Balancing security cover.

Following discussions with xoserve, we understand the availability of potential 'emergency claims' information during a Gas Deficit Emergency may afford the Energy Balancing Credit Manager (EBCM) with an opportunity to enhance its monitoring and management of credit and security assessments; this may mitigate the likelihood of the 'domino effect' in respect of User defaults that might arise as a consequence of a Gas Deficit Emergency.

Prevailing Emergency Claim Arrangements

During a Gas Deficit Emergency 2+, Users are required to maximise supplies into the Total System. The emergency claim arrangements were introduced in recognition of concerns regarding possible financial loss that Users may suffer associated with the requirement to maximise beach supply over-and-above that required to fulfil their demand.

Once the NEC has declared a Gas Deficit Emergency Stage 2+ and should the User subsequently have a surplus Daily Imbalance, this surplus is cashed-out at the frozen System Average Price (SAP) for that Gas Day. This price may not reflect the market value paid on the Gas Day for increased supplies.

From its inception, Users that are able to help the Total System by providing supply during an emergency over-and-above that which is required for their supply and demand balancing purposes, have raised concerns associated with the lack of clarity and certainty associated with the post-emergency claims arrangements. These Users believe that under the prevailing arrangements, there is a risk that any supply (or self-interruption of demand) provided to help the Total System during an emergency, may leave them facing financial loss.

This was considered by Ofgem in its decision letter for; *Modification Proposal 0149 dated 19th October 2007- 'Gas Emergency Cashout Arrangements: Keeping the On the Day Commodity Market open during a Gas Deficit Emergency'*

in which Ofgem indicated that;

“We do not consider that the UNC Section Q post emergency claims procedure provides sufficient economic incentive for Users to buy gas not already contracted above the frozen cash-out price, since at best they can only recover their costs, whilst exposing themselves to uncertainties surrounding the outcome of the claims process.”

National Grid NTS concurs with the views that prevailing post-emergency claims arrangements should provide the requisite definition, clarity and certainty that are required to facilitate User confidence that costs for providing additional supply and/or self-interruption of demand during a Gas Deficit Emergency will be settled in a clearly defined and timely manner.

The prevailing arrangements associated with the derivation of the Emergency Cash Out Price and the Post-Emergency Claim Arrangements are as follows:

Emergency Cashout Prices

- Users’ Daily Imbalances are cashed-out utilising the *frozen* prices (Stage 2) on the following basis;
 - deficit imbalance – shippers cashed-out @ SMP Buy
 - surplus imbalance – shippers cashed-out @ SAP

Post-emergency arrangements - Claims

- UNC section Q section 4.2.6 states; *Where a User (the "claimant") believes that it will suffer a financial loss by reason of being paid only the relevant price in respect of any gas delivered to the Total System on a Day during a Gas Deficit Emergency (at Stage 2 and higher) (but not in respect of a quantity of gas which exceeds the amount of the claimant's Daily Imbalance if any under paragraph 4.2.2(a)).”*
- The Claimant is required to submit a claim
- Provide details regarding the basis for the claim
- Claim (s) only relevant to gas over-delivered by that shipper during the Gas Deficit Emergency (surplus Daily Imbalance)
- National Grid NTS will appoint an independent claims reviewer
- The Claimant will make available information and cooperate with the claims reviewer
- Recommendations of the independent claims agent will require oversight and subsequent approval by the Authority
- Payment to claimant and recovery of costs
- Following consultation with Authority, and the Claimant, Under Condition A11(18) the Authority may approve the claim, National Grid NTS will pay the Claimant the amount advised by the Claims reviewer.

- National Grid NTS will recover any cost for claims as if it were a Market Balancing Action Charge payable to National Grid NTS, recovered through neutrality (ref Q4.2.5), therefore smeared over User throughputs on the relevant Gas Day (within the Gas Deficit Emergency).
- National Grid NTS will recover the fees and costs of the claims reviewer through Monthly Adjustment Neutrality Costs.

Nature of the Proposal

This Proposal considers the introduction of improvements that will bring greater clarity and definition to the UNC post-emergency claims arrangements. This is of benefit to the wider community by providing greater transparency of the potential costs to the industry and, allowing Users to assess and manage their commercial exposure that might arise from a Gas Deficit Emergency, in a timely manner.

This Proposal seeks to introduce the following changes:-

Emergency Cashout Prices

- *No changes* are proposed to the derivation of the emergency cashout prices (remain frozen at Stage 2)

Post-emergency Arrangements - Claims

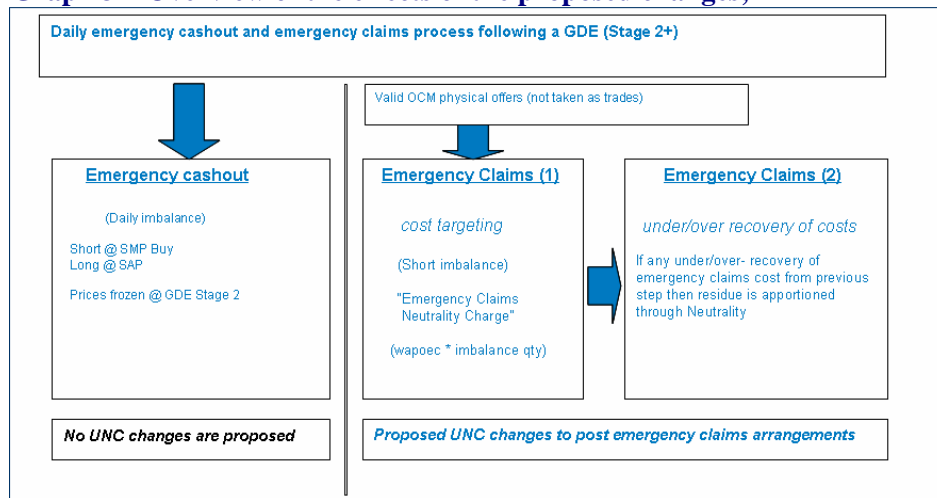
In addition to UNC Section Q 4.2.6:

- In order to submit a post-emergency claim, a User will be required to have posted additional supplies and/or demand-side reduction (quantity and price) as offers to sell on the OCM physical market during the Gas Deficit Emergency.
- These Physical Market Offers might be accepted as trades by Users that have a deficit imbalance in which case, the offer will be cleared through existing OCM rules and therefore, would not be eligible for progression through the revised claims arrangements.
- Any Physical Market Offers remaining on the OCM at the end of each Gas Day of the Gas Deficit Emergency may be submitted as potential claims. However, only the quantity of gas over-delivered by that User for each Gas Day (within the Gas Deficit Emergency), may be claimed e.g. the User's surplus Daily Imbalance.
- Users that incurred a deficit Daily Imbalance will be initially apportioned the costs of valid post-emergency claims to the extent of their imbalance quantity; based on the weighted average price (p/kWh) of all valid emergency claims (wapoc) multiplied by the User's deficit Daily Imbalance quantity (kWh).

Please note: *the full costs of all valid emergency claims will not be smeared over those Users with deficit Daily Imbalances on the day(s) of the Gas Deficit Emergency but such targeted costs will be recovered based on the weighted average price of those emergency claims multiplied by the extent of a User's imbalance quantity.*

- Any under-over recovery of emergency claims costs will be smeared across all Users, based on throughput on the Gas Day(s) of the Gas Deficit Emergency through the Balancing Neutrality adjustment process.

Graph 3 – Overview of the effects of the proposed changes;



Note: For examples of the cash-flows (under-recovery and over-recovery) associated with the proposed changes to the post-emergency claims arrangements, please see Appendix 1 (1a/1b).

Use of the OCM as a 'potential emergency-claims' bulletin board

National Grid NTS believes that during a Gas Deficit Emergency, it should be assumed that all those Physical Market Offers posted on the OCM *will/are* being 'delivered' to the Total System. In this situation, we believe that the OCM should be considered as a 'potential emergency-claims' bulletin board.

The market may not be able to distinguish those Physical Market Offers (other than through price) that will provide additional (non-UKCS) supplies and/or self-interruption to say, those extra UKCS supplies (or demand-side reduction) being provided under NEC instruction.

We do not consider however that the requirement to distinguish Physical Market Offers in this manner is necessary. One objective of this Proposal is to encourage those Users, with a physical capability, to register any available 'surplus' gas as Physical Market Offers on the OCM for those Users who might wish to address their deficit imbalance.

During a Gas Deficit Emergency, a Physical Market Offer may either be accepted by a User that has made a commercial decision to address its deficit imbalance position or, where such offers are not accepted, they may form the basis of a post-emergency claim. In the latter case, the cost of a post-emergency claim would, in the first instance, be recovered from Users that had incurred deficit Daily Imbalance positions.

We believe that notwithstanding a Physical Market Offer is cleared through the OCM as a trade or, becomes a potential post-emergency claim; the use of the OCM in this manner may result in a timely restoration of the Total System.

Price Discovery

We note that in its decision letter to Modification Proposal 0149, Ofgem responded to several Users' concerns relating to gaming issues and instances where monitoring of such activity would be difficult to identify or prove;

“Ofgem has powers under the Competition Act to investigate and take action against anti-competitive conduct. We think that the current focus of attention should be on putting in place arrangements that provide appropriate commercial incentives under emergency arrangements on the assumption that Users do not behave in this way and seek to game the rules, in the knowledge that Ofgem has the necessary powers to intervene, if necessary.”

We believe the changes contained within this Proposal will facilitate greater transparency of prices and potential costs associated with the value of gas during a Gas Deficit Emergency.

We also consider that this Proposal may afford the community and Ofgem with an ability to monitor any potential post-emergency claims on an 'ex-ante' basis and thus enable the industry, not only to calculate exposure to after-the-day costs associated with a Gas Deficit Emergency, but it also to ensure that any concerns associated with 'gaming' may be addressed in a timely manner.

As previously suggested, we consider that greater transparency of the prices and potential costs during a Gas Deficit Emergency may facilitate improvements in the Energy Balancing Credit Manager's ability to improve the efficiency of managing and monitoring the wider community's credit risk exposure.

Appointment of a Claims Reviewer

This Proposal seeks to appoint the Transporters' Agent as the Claims Reviewer; to become responsible for the 'mechanistic' elements of the post-emergency claims validation process. We note that xoserve has indicated that it welcome such an undertaking as the post-emergency claims validation process will enhance the monitoring and management of Energy Balancing Credit exposure that might arise as a consequence of a Gas Deficit Emergency.

Claims Validation Process

We propose that the claims validation element of the post-emergency arrangements is undertaken on a 'mechanistic' basis with the validation rules clearly defined, agreed and transparent. To achieve this we believe that the claims validation rules and the claims submission requirements are defined within the UNC [*Claims submission requirements may be defined within Guidelines referenced in within the UNC*].

The proposed changes will require the Claimant to provide specific data with each claim submitted, the requirements of which are detailed within Section 3.3 of the Business Rules (see Appendix 3). As part of this specified information the Claimant will be required, where relevant, to provide details of a Market Reference to which the Market Offer Price relates, together with a justification for the level of the Market Offer Price where it significantly varies from other Market Reference price(s) that occurred during the Gas Deficit Emergency.

It is recognised that there may be instances where a post-emergency claim might be queried as the price appears to notably differ to other post-emergency claims relating to

the same day during a Gas Deficit Emergency. In these circumstances, additional 'economic validation' may be required however, we believe that this would only be considered where Ofgem had instructed such economic validation to be undertaken.

We consider that the proposed changes to the post-emergency claims arrangements will provide sufficient time for any 'price/economic' issues and auditing of such post-emergency claims to be resolved, and for Ofgem to direct a decision regarding the validity of such a Claim, prior to the required settlement of all valid Claims through the Emergency Claim Neutrality process.

Cost-targeting of Post Emergency Claims

We believe that the introduction of the proposed arrangements puts in place appropriate incentives for Users to appropriately manage their imbalance position. Where a User fails to make appropriate arrangements, an additional cashout price will be applied that reflects the costs of the post-emergency claims associated with additional gas 'supplied' during the Gas Deficit Emergency.

This Proposal seeks to apply a weighted average price, derived from all valid post-emergency claims prices associated to each Gas Day within a Gas Deficit Emergency, and multiplied by the extent to which any User incurred a deficit Daily Imbalance for that Gas Day.

We anticipate there may be instances (see Appendix 1a/b) where the costs for the post-emergency claims may initially be under-recovered or over-recovered from those Users that incurred a deficit Daily Imbalance. We propose that any under-recovery or over-recovery of the costs of post-emergency claims is cleared through the Neutrality Adjustment mechanism, across all Users as defined within the TPD Sections Q4.2.4 and F4.

We note that concerns have been raised associated with the introduction of the targeting of costs in that such arrangements may penalise a User that has been placed in deficit Daily Imbalance position through circumstances which are out its control. In particular, concerns were raised associated with the consequences of a User with a small deficit position, for example, a User with a 1 kWh deficit Daily Imbalance might be targeted with a high proportion of the costs arising from a Gas Deficit Emergency. During a Gas Emergency Arrangements Workshop, we have clarified that in this situation the User would be charged 1 kWh multiplied by the wapoec and not the whole costs arising from all valid post-emergency claims. Any remaining costs after the initial 'targetting' will be apportioned across all Users (based on throughput) through Balancing Neutrality (see Appendix 2).

ECQ interactions - ECQ and Emergency Claims process

The Emergency Arrangements Workshop has discussed concerns associated with the interactions of the Emergency Curtailment Quantity (ECQ) and the proposed changes to the post-emergency claims process. A view was expressed within the Workshop that implementation of both arrangements was not necessary and indeed, the changes contained within this Proposal could replace the ECQ arrangements.

We have carefully considered this view however, on balance we believe that this Proposal would compliment, rather replace, the ECQ arrangements in as much as the Proposal might encourage Users to facilitate additional self-interruption arrangements with their demand-side customers.

Under the prevailing UNC provisions, the ECQ arrangements are applied where a User has been instructed switch a site off either during Stage 1 (interruptible load) or Stage 3 (firm load). Where the User has been instructed to take a site off during Day 1 of a Gas Deficit Emergency, the User will receive an ECQ so that the quantity 'interrupted' maintains the imbalance position.

For Day 2+ of a Gas Deficit Emergency, Users may submit a 'P70' to National Grid NTS that indicates a site has been 'self-interrupted' and thereby avoid an ECQ from being applied for that particular site.

We believe that this Proposal will provide Users and their end consumers with a framework through which they may be appropriately recompensed for the cost of self-interruption, whilst both this Proposal (if implemented) and the ECQ might encourage Users to further contract for self-interruption prior a Gas Deficit Emergency occurring.

Potential requirement for a Regulatory Impact Assessment

Given that this Proposal is seeking to introduce provisions that will initially target the costs associated from valid post-emergency claims against a sub-set of Users i.e. those which incurred a deficit Daily Imbalance, there may be a requirement for Ofgem to undertake a Regulatory Impact Assessment. Any proposed implementation date assigned to this Proposal must be mindful of the scope and duration that any such Regulatory Impact Assessment may require.

b) Justification for Urgency and recommendation on the procedure and timetable to be followed (if applicable)

Not applicable

c) Recommendation on whether this Proposal should proceed to the review procedures, the Development Phase, the Consultation Phase or be referred to a Workstream for discussion.

The changes contained within this Proposal have been discussed within the main Transmission Workstream on several occasions since Summer 2008 and, in a number of Emergency Arrangements 'Workshops' (sub-group of the Transmission Workstream). We therefore recommend that this Proposal should proceed to Consultation.

2 User Pays

a) Classification of the Proposal as User Pays or not and justification for classification

On the basis that this Proposal is seeking to improve and add clarity to the Energy Balancing arrangements both during, and following, a Gas Deficit Emergency; and that such changes may provide a benefit to both Users and Transporter(s), we believe that this Proposal should be classified as a User Pays Modification Proposal.

b) Identification of Users, proposed split of the recovery between Gas Transporters and Users for User Pays costs and justification

We propose that the Users Pays costs, for these proposed changes, are apportioned 50/50 between Users and Transporters as we believe that the benefit of the proposed changes to the Emergency Arrangements mitigate risks borne by all parties equally during/following a Gas Deficit Emergency.

c) Proposed charge(s) for application of Users Pays charges to Shippers

xoserve has determined that the changes required to implement this Proposal are administrative and procedural changes, with no UK Link system changes required. Therefore we expect that any User Pays costs will be minor and relate to operational requirements. xoserve has advised that it believes that these procedural changes may be absorbed through the enhancement of prevailing operational processes in place for Gas Deficit Emergency arrangements.

d) Proposed charge for inclusion in ACS – to be completed upon receipt of cost estimate from xoserve

xoserve does not anticipate any additional costs will be required to facilitate this change.

3 Extent to which implementation of this Modification Proposal would better facilitate the achievement (for the purposes of each Transporter's Licence) of the Relevant Objectives

Standard Special Condition A11. 1 (a) the efficient and economic operation of the pipe-line system to which this licence relates:

If implemented, the proposed changes will provide greater clarity and definition of the post-emergency claims process.

We believe that:

- overall, the introduction of such provisions may provide Users with an enhanced opportunity to better manage their supply and demand balance during an emergency;
- the proposed transparency of the emergency arrangements will afford those Users that have a physical capability, to assist in the mitigation of a Gas Deficit Emergency;
- the changes may further encourage non-UKCS gas supplies into the GB market as a User might have greater confidence that it will receive an appropriate level of financial recompense based on a prevailing market rate and;
- such actions may result in the restoration of the Total System in a timely manner and this may therefore improve the efficient operation of the Total System during a Gas Deficit Emergency.

This Proposal, if implemented, seeks exclusive use of the OCM Physical Market to register offers that are eligible for submission as post-emergency claims. We consider that determining the values of claims in this manner may keep prices from spiralling, as a result

of the improved market transparency and auditability of such prices. National Grid NTS considers that this may demonstrate an improvement in the economic operation of the Total System during a Gas Deficit Emergency.

We believe that the proposed changes might better align the UNC arrangements to those of the Users' legal safety obligations (Shipper Licence/GSMR) during a Gas Deficit Emergency and that this may also demonstrate an improvement in the operation of the Total System during such an emergency.

Standard Special Condition A11.1 (d): so far as is consistent with sub-paragraph (a) to (c) the securing of effective competition between shippers, suppliers and DN operators:

We believe that the proposed changes may demonstrate improvements in competition between Users during a Gas Deficit Emergency. We consider that through the provision of improved transparency of prices, utilising the OCM as a post-emergency claims 'bulletin board' and, with greater clarity in the UNC emergency arrangements, Users might be better placed to manage their financial exposure that might arise as a consequence of a Gas Deficit Emergency.

Users will have an opportunity to utilise a framework to manage their exposure to any costs (prices) arising from a Gas Deficit Emergency in an environment where such commercial arrangements are better aligned to, and may complement, their legal safety obligations (Shipper Licences / GSMR).

We believe that facilitating an improved framework for Users to manage supply/demand imbalance may reduce the occurrence of User-defaults as a consequence of a Gas Deficit Emergency, thereby reducing the cost implications on all Users. This, we consider demonstrates an improvement in competition between Users as it may reduce uncertainties in the costs arising from the Gas Deficit Emergency.

A11.1(f) the promotion of efficiency in the implementation and administration of the network code and/or the uniform network code.

We note that it is generally accepted that the prevailing UNC emergency arrangements lack the definition and clarity required to provide Users with the confidence that will enable them to recover their costs associated to any incurred financial losses. These financial losses might be incurred as a consequence of placing additional gas supply onto the Total System during a Gas Deficit Emergency. We believe that, if implemented, this Proposal provides the definition and clarity required and thus, the Proposal promotes efficiency in the administration of the UNC.

4 The implications of implementing this Modification Proposal on security of supply, operation of the Total System and industry fragmentation

We believe that if implemented this Proposal may provide greater clarity and improvements in the commercial arrangements for the provision of additional gas during an emergency, we anticipate that this may encourage non-UKCS gas into the GB market and, facilitate further self-interruption on demand-side arrangements.

Whilst a potential increase in supply during a Gas Deficit Emergency may demonstrate an enhancement to the safe operation of the Total System, we recognise that such additional supply *may* only be 'on the margins' of the quantities required to alleviate a Gas Deficit Emergency. Nevertheless, National Grid NTS believes that in the event this Proposal is

implemented, it would demonstrate an improvement to the prevailing arrangements.

5 The implications for Transporters and each Transporter of implementing this Modification Proposal, including:

a) The implications for operation of the System:

We believe that if implemented, the Proposal might improve the operation of the Total System during a Gas Deficit Emergency, such that it may encourage greater supply and demand side response. We believe that this may result in the restoration of the Total System in a timely manner.

b) The development and capital cost and operating cost implications:

No development or operational costs implications are anticipated.

c) Whether it is appropriate to recover all or any of the costs and, if so, a proposal for the most appropriate way for these costs to be recovered:

Not applicable

d) The consequence (if any) on the level of contractual risk of each Transporter under the Uniform Network Code of the Individual Network Codes proposed to be modified by this Modification Proposal

We believe that this Proposal might improve the definition and clarity of the emergency claims process provided in Section Q. The improved clarity and definition may mitigate the potential contractual risks of the Transporter under the UNC.

6 The extent to which the implementation is required to enable each Transporter to facilitate compliance with a safety notice from the Health and Safety Executive pursuant to Standard Condition A11 (14) (Transporters Only)

Not applicable

7 The development implications and other implications for the UK Link System of the Transporter, related computer systems of each Transporter and related computer systems of Users

We do not anticipate any system development requirements for the implementation of this Proposal. We understand that the changes required to UK Link system to facilitate this change will be managed through procedural and offline processes, the cost of which may be countered by the enhancement of the prevailing post-emergency arrangements.

If implemented, this Proposal will require the following changes to operational processes/procedures, for example:

- OCM Physical Market Offer data is required to support the post-emergency claims validation process.
- Energy Balancing Credit Management (EBCM) to validate and process all post-

emergency claims.

- EBCM to calculate and credit Claimant for valid post-emergency claims.
- EBCM to calculate and recover Claims costs through Balancing Neutrality in accordance with the proposed rules.
- Provision of reporting, relevant to the revised emergency arrangements.

8 The implications for Users of implementing the Modification Proposal, including:

a) The administrative and operational implications (including impact upon manual processes and procedures)

We anticipate that Users may need to review amend their Emergency Arrangements to align with the changes that are outlined within this Proposal.

b) The development and capital cost and operating cost implications

We are unaware of any development and capital/operational costs and would request that respondents advise of such in due course.

c) The consequence (if any) on the level of contractual risk of Users under the Uniform Network Code of the Individual Network Codes proposed to be modified by this Modification Proposal

We believe that providing greater clarity and definition of the post-emergency claims arrangements may mitigate some of the uncertainties associated with payment for any financial loss incurred by Users for providing additional gas to the Total System during a Gas Deficit Emergency.

We consider this may mitigate some of the Users' contractual risks associated with such uncertainty that might arise as a consequence of a Gas Deficit Emergency.

9 The implications of the implementation for other relevant persons (including, but without limitation, Users, Connected System Operators, Consumers, Terminal Operators, Storage Operators, Suppliers and producers and, to the extent not so otherwise addressed, any Non-Code Party)

If implemented this Proposal would require the OCM Market Operator (APX Gas Ltd) to support certain elements;

- The provision of certain Physical Market Offer data
- Provision of indicative WAP prices during the Gas Deficit Emergency

APX Gas Ltd believes the required changes to implement this Proposal can be achieved without the need for system changes and therefore, do not anticipate any development or capital cost implications.

APX Gas Ltd has indicated that the provision of Physical Market Offer data (as outlined

within this Proposal) to National Grid NTS/Transporter Agent will require a 1 month consultation with its Members to discuss an amendment to their OCM Market Rules. APX Gas Ltd considers there would be no significant issues (if any) arising from this consultation.

10 Consequences on the legislative and regulatory obligations and contractual relationships of the Transporters

We note that this Proposal, if implemented, does not require any material changes to the NEC Safety Case nor, impinge on Users' safety obligations to comply with their Licence / GSMR (NEC instructions) in the event of a Network Gas Supply Emergency.

11 Analysis of any advantages or disadvantages of implementation of the Modification Proposal not otherwise identified in paragraphs 2 to 10 above

Advantages

- The prevailing emergency cashout prices remain unchanged – frozen at Stage 2.
- Addresses those expressed concerns of, and improves, the clarity and definition of the UNC post-emergency arrangements.
- May encourage additional non-UKCS gas supplies and/or promote further self-interruption of demand to be delivered to the Total System during a Gas Deficit Emergency. Provides Users with greater confidence that they will receive payment, which appropriately reflects the cost of such gas.
- Where appropriate, enables User's to recover their costs of providing additional supplies/self-interruption of demand with a linkage to a transparent 'market value', for example, price referenced to an adjacent European gas/LNG market.
- Enhances the existing incentives for Users to put in place commercial arrangements that might address a deficit imbalance prior to, and during, a Gas Deficit Emergency.
- Utilisation of the OCM as a 'bulletin board' in this manner will provide greater market transparency and price discovery as Users are able to assess their potential exposure to costs prior to any post-emergency claims being submitted.
- May increase the likelihood that a User, with its additional gas registered as a Physical Market Offer during a Gas Deficit Emergency, has the offer accepted and cleared through the APX Gas Ltd – rather than have the offer progressed as a post-emergency claim through Balancing Neutrality.
- 'Ring-fences any costs that might arise as a consequence of a Gas Deficit Emergency
- Spreads the risks associated with credit issues across the 'normal' daily cashout mechanism (frozen cashout prices at Stage 2) and the revised post-emergency claims arrangements (Balancing Neutrality up to three months after a Gas Deficit Emergency has occurred).
- Enables the Energy Balancing Credit Management to better monitor and manage credit/security provisions during a Gas Deficit Emergency.

- No changes are required to the NEC Safety Case, nor does this Proposal impinge on the Users' ability to comply with their safety obligations (Shipper Licence/GSMR (NEC Instructions)).

Disadvantages

- The initial cost-targeting of post-emergency claims against Users who may not be in control of events might be deemed punitive.
- Utilisation of the OCM Physical Market during a Gas Deficit Emergency in this manner may be viewed by some Users as discriminatory.

12 Summary of representations received as a result of consultation by the Proposer (to the extent that the import of those representations are not reflected elsewhere in this Proposal)

None yet received

13 Detail of all other representations received and considered by the Proposer

None yet received

14 Any other matter the Proposer considers needs to be addressed

None

15 Recommendations on the time scale for the implementation of the whole or any part of this Modification Proposal

Draft Proposal to 18 June 2009 Modification Panel - recommend to consultation

Final Mod report to 16 July 2009 Modification Panel

Ofgem decision August 2009

Implementation 1st October 2009

16 Comments on Suggested Text

17 Suggested Text

Code Concerned, sections and paragraphs

Uniform Network Code

Transportation Principal Document Section Q 4.2.4

Section(s)

Proposer's Representative

Steve Pownall (National Grid NTS)

Proposer

National Grid NTS

Appendices

Appendix 1 – Cashflows and over-recovery / under-recovery examples

Appendix 2 – '1 kWh' deficit imbalance example

Appendix 3 – Proposed business rules

DRAFT