

**Modification Report**  
**End of Year Reconciliation of Specific Categories of Smaller Supply Points**  
**Modification Reference Number 0640**

Version 2.0

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**

Following discussion within the Supply Point and Billing Workstream this Modification Proposal has been descoped to remove elements which proposed an 'end of year' reconciliation methodology with respect to Annual Quantity (AQ) amendments.

Section 2 of this Modification Proposal explains the Workstream's rationale.

### **Events within scope.**

- Where a Smaller Supply Point ("SSP") becomes a Larger Supply Point ("LSP") at an AQ review, and the AQ increases by more than 15,000 kWh and 20%.

### **Events outside scope.**

- Supply Points meeting the above criteria which transfer to another User during the year
- Normal annual fluctuations in AQs within the Smaller Supply Point category
- Normal annual fluctuations in AQs resulting in the Supply Point becoming a Larger Supply Point, but the AQ increasing by less than 15,000 kWh or 20%.

### ***Upward Threshold Crossers – “Reconciliation” Methodology.***

Where a Smaller Supply Point becomes a Larger Supply Point as a result of the AQ Review in Year 2, the Year 2 AQ would be used to reconcile the Supply Point for Year 1.

Note that if the AQ increases to a value greater than the LSP threshold by an appeal before Transco performs the AQ calculation for the following year, no reconciliation would be made. If the AQ is moved above the LSP threshold by an appeal after that date, the reconciliation period would be reduced to equal the effective period of the original Year 1 AQ.

A: Year 1 AQ

B: Year 2 AQ

C: Appealed above LSP threshold - before Year 2 AQ calculation - no reconciliation

D: Appealed above LSP threshold - after Year 2 AQ calculation - reconcile to Date D only

Test 1: Is A below 73,200 kWh and B above 73,200 kWh?

Test 2: Is B-A more than 15,000 kWh?

Test 3: Is B more than 120% of A?

The User would be charged for the difference in allocation between A and B for the relevant End User Category (EUC) for Year 1 (or to live date of new AQ if appealed after the calculation of Year 2 AQs). Transportation commodity charges would be at the applicable Smaller Supply Point Rates and the associated energy costs will be at System Average Price. The charges would be issued as TRE (transportation) and GRE (energy).

No amendment will be made to capacity charges for the relevant year.

**Timing:** the calculation would be performed and invoices issued after the end of the relevant Gas Year.

**RbD Treatment:** the opposite impact of the transportation commodity and associated energy costs will be processed through RbD on the next available reconciliation invoice, based on the duration of the error, namely in the Domestic Portfolio Adjustment (Annual) sector.

No amendment would be made to RbD Market Shares for the change in AQ.

## 2. Transco's Opinion

It is Transco's opinion that this Modification Proposal should be implemented.

The measures contained within this Modification Proposal have been developed within the Supply Point & Billing Workstream, RbD sub-group and Billing Operations Forum.

Following exhaustive analysis and discussion, the Supply Point & Billing Workstream concluded that the scope of the Modification Proposal should be reduced to incorporate 'Upward Threshold Crossers' only. It was determined that the reconciliation methodology for AQ amendments originally identified within this Modification Proposal should be dispensed with as being superfluous and having little material benefit. The Workstream's rationale was that the need for an 'end of year' reconciliation associated with AQ amendments had not been substantiated. Members cited the effectiveness of Modification 0624 'Changes to the 2003 Annual Quantity (AQ) amendment process' which introduced specific provisions to the Network Code governing AQ amendment activity. Workstream members identified that there was currently no evidence of the problems experienced in previous years with regard to inappropriate AQ amendments.

Workstream members acknowledged that the inappropriate use of a SSP AQ where a site is consuming at Larger Supply Point ('LSP') levels (commonly termed 'threshold crossers') remained a concern given that under the current Reconciliation by Difference ('RbD') mechanism for invoicing Smaller Supply Points ('SSPs'), the RbD community can be adversely affected by the mis-statement of a User's total SSP portfolio Annual Quantity ('AQ').

Transco, therefore, believes that there should be a mechanism to address the AQ related anomaly described above to ensure appropriateness of transportation billing. There are mechanisms for retrospective adjustment which have been developed within RbD billing, but these can only presently be used for errors of portfolio completeness or existence, rather than mis-statement of AQ.

Transco's view is that an advantage of the methodology identified within this Modification Proposal is that it encourages ongoing monitoring and if necessary prompt appealing by Users of inappropriate AQs by Users.

Transco believes that it is appropriate that the 'threshold crosser' mechanism, described above, should be included within the Network Code to rectify potentially adverse effects associated with the AQ review which impact Users with Smaller Supply Points. The activity would enable aggregate commodity & energy corrected positions to be billed to the User and then applied through RbD to adjust each User's annual gas consumption. The procedure would apply to circumstances as defined in the Proposal, but not for normal year on year AQ fluctuations.

Unless the correction mechanism identified within this Modification Proposal is implemented, the opportunity for commercial gain as a consequence of failure by Users to ensure AQs are reflective of actual consumption would remain. Failure to ensure this could have a detrimental effect on Users with portfolios containing Smaller Supply Points.

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

The measures identified within this Modification Proposal minimise risk to RbD Users by ensuring the accuracy and robustness of a key feeder process. The proposed mechanism is consistent with Transco's Licence 'Relevant Objective' to secure effective competition between relevant shippers and between relevant suppliers.

**4. The implications for Transco of implementing the Modification Proposal , including**

**a) implications for the operation of the System:**

No implications for the operation of the system have been identified.

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

No such implications have been identified.

**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:**

Minor administrative costs would be incurred by Transco as a consequence of implementing this Modification Proposal. Transco does not propose any additional cost recovery.

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

No such consequences have been identified.

**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**

Implementation of this Modification Proposal would not increase the level of Transco's contractual risk.

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

No changes would be required to Transco's UK-Link system to facilitate implementation of this Modification Proposal. Transco proposes to calculate the relevant 'end of year' reconciliation 'off-line' and utilise existing 'ad-hoc' invoicing functionality. Transco has been informed via representation to this Modification Proposal that development of Users systems may be required in order to monitor and appeal upward threshold crossers on an ongoing basis.

**7. The implications of implementing the Modification Proposal for Users**

It is expected that minor changes to relevant Users' processes would be required to accommodate implementation of this Modification Proposal.

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

No such implications have been identified.

**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 such consequences have been identified.

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

Advantages:

- Ensures that relevant transportation charges are incurred by Users appropriate to the actual offtake of a Supply Point, and that any inappropriate allocation of charges is rectified at the end of the gas year.
- Promotes prompt and timely monitoring and appealing of AQs by Users where an AQ 'threshold crosser' occurs.

Disadvantages:

No disadvantages have been identified.

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

Five representations were received with respect to this Modification Proposal. Four were supportive of its implementation and one was supportive in principle.

Transco notes BGT's comment that it raised a challenge on an element of the legal drafting. Transco agreed with the point made by BGT and has undertaken minor amendments to the text to remove the

concern. The change related to Sections 7.4.5(a) and 7.4.5(b)(i) which determine the 'User Annual Quantity Revision Difference', with respect to AQ appeals.

RWE Innogy commented "in our opinion Transco have yet to demonstrate that the benefits associated with implementing this modification proposal in its revised form are material".

Transco's response is that Users having Smaller Supply Points (SSPs) have the opportunity to receive and review the output from the RbD verification process, which Transco operates to provide additional assurance to the community. By far the largest reconciling items to date are the energy impacts of upward threshold crossers following each SSP AQ Review.

Work has been undertaken within the RbD Sub-group, AQ Sub-group and RbD Technical Sub-group to examine the materiality of the impacts of upward threshold crossers. These industry fora have concluded that the energy and financial impacts are sufficient to merit the implementation of the measures identified within this Proposal.

RWE Innogy comments "Nor do we believe that gaming (whereby shippers deliberately declare sites as small supply points knowing that their AQ exceeds the small supply point threshold) takes place on a large scale basis, particularly since the modification proposal 624 took effect".

Transco acknowledges the view of the respondent and believes that this Modification Proposal is more aimed at ensuring that transportation and energy charges are appropriately borne by the relevant User, rather than addressing inappropriate behaviour. Based on the metrics detailed above, Transco stresses that the volume of 'misplaced' energy is not insignificant.

RWE Innogy claimed "Transco have also underestimated the work that may be required by shippers to allow all small supply point AQs to be monitored on an ongoing basis throughout the year". The respondent further commented "Whilst some shippers will be able to easily highlight any upward threshold crossers on an ongoing basis such that they can then promptly appeal the AQ in the event it meets the criteria specified, not all shippers may be geared up to acting in this way. Other shippers having been used to a regime where they have only had to review the AQs of what are presumed to be small supply points on an annual basis, may experience considerable difficulty adapting to a situation where they in effect have to recalculate the AQ of their entire small supply point portfolio each time they receive a meter read".

Transco's response is that it accepts that Users may need to improve their internal processes for monitoring their SSP AQs. This would ensure threshold crossers are identified at an earlier stage. However, Transco believes that Users would have a relatively small number of 'target' sites, these being, for example, 'greenfield start-ups' or premises which have been mothballed/closed for refurbishment. Transco's opinion is that the AQ of the majority of true 'domestic' sites will never come close to the threshold, and most of the sites which tend to oscillate across the threshold on successive years would be excluded by the 20% and 15,000 kWh de minimus limit.

RWE Innogy stated that "With this in mind, we would argue that if this modification proposal were accepted it should not take effect until the AQ Review for 2005. This would ensure that shippers have sufficient time to make the changes to their systems and working practices, so as to allow them to

monitor and appeal upward threshold crossers on an ongoing with effect from gas year 2004". The respondent further comments "Were it to be implemented before then, shippers may find themselves exposed to retrospective reconciliation charges based on meter reads that have already taken place or will take place later in this gas year, which leaves precious little time for them to make any changes needed to mitigate this exposure. This exposure would be compounded the longer it takes to make a decision on whether to accept this modification proposal."

Transco acknowledges and has some sympathy with the above concern expressed by the respondent. There is a view, however, that the significance of prompt appealing of AQs in circumstances reflected in Section G1.6.13(b)(ii) has been well aired in industry fora since 2000 and Users should already have well established measures in place to ensure timely monitoring and appealing of AQs. Transco would also draw attention to the fact that if the Modification Proposal was not implemented in accordance with the timetable detailed within this Modification Report, but was implemented effective in the following gas year, approximately a further 3 tWh of energy would remain inappropriately allocated. Transco however would be prepared to accommodate a later implementation should this be the prevailing industry view. However, another respondent recommended that it was implemented as soon as possible.

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

Implementation of this Modification Proposal is not required to enable Transco 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**

This Proposal is not required to facilitate any such change.

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

No programme of works is required to implement this Modification Proposal.

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

This Modification Proposal could be implemented with immediate effect. Transco would undertake the first reconciliation exercise in the fourth quarter of 2004, following the 2004 AQ Review exercise.

**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

### SECTION E: DAILY QUANTITIES, IMBALANCE AND RECONCILIATION

*The following shall be added as a new paragraph 1.3.8:-*

“1.3.8 **“End of Year AQ Reconciliation”** is a reconciliation and adjustment in respect of gas offtaken from the System and certain Transportation Charges, following a revision of the Annual Quantity, in respect of quantities determined in accordance with paragraph 7.4.

*The heading to paragraph 7.4 shall be amended to read:-*

“Annual Quantity revision and End of Year AQ Reconciliation”

*Add the following as new paragraphs 7.4.3 to 7.4.5:-*

“7.4.3 Where, as a result of the revision of the Annual Quantity of a Smaller Supply Point pursuant to Section G1.6, the Supply Point becomes a Larger Supply Point and:-

- (a) the Annual Quantity is increased by more than:-
  - (i) 20% of the Annual Quantity at the start of the preceding Gas Year; and at least by
  - (ii) 15,000 kWh; and
- (b) there has not been a change in Registered User for the Supply Point since the last revision of the Annual Quantity of the Supply Point pursuant to Section G1.6; and
- (c) the Annual Quantity of the Supply Point was not increased such that the Smaller Supply Point became a Larger Supply Point prior to the Provisional Annual Quantity being calculated by Transco

then paragraph 7.4.4 will apply.

7.4.4 In the circumstances set out in sub-paragraph 7.4.3 above:-

- (a) the User Annual Quantity Revision Difference shall be extinguished by a System Clearing Contract in accordance with Section F5;
- (b) for the purposes of Section F5, the Reconciliation Clearing Charge in respect of a System Clearing Contract under paragraph 7.4.4(a) shall be the User Annual Quantity Revision Difference Clearing Value;
- (c) the User Annual Quantity Revision Difference Transportation Charge Adjustment shall be payable by an adjustment in respect of the NTS Commodity Charge, LDZ Commodity Charge and Commodity Variable Components (if any) of the Customer Charges underpaid by the User in respect of gas offtaken by the User in the relevant period;
- (d) the User Annual Quantity Revision Difference Transportation Charge Adjustment shall be payable by the User to Transco.

7.4.5 For the purposes of this paragraph 7.4:-

- (a) **“User Annual Quantity Revision Difference”** is the sum of:-

$$(X - Y)$$



Where:-

X is the Annual Quantity of the Supply Point notified by Transco in respect of the Gas Year following the relevant Gas Year;

Y is the Annual Quantity of the Supply Point notified by Transco in respect of the relevant Gas Year;

- (b) The “**User Annual Quantity Revision Difference Clearing Value**” is the amount established by:-
- (i) Determining the additional NDM Supply Meter Point Demand as a result of the User Annual Quantity Revision Difference for each day in the relevant Gas Year in which Y (as defined in paragraph (a) above) was in effect;
  - (ii) Multiplying the daily additional NDM Supply Meter Point Demand by the System Average Price for such day to determine the daily User Annual Quantity Revision Difference Clearing Value; and
  - (iii) Aggregating the daily User Annual Quantity Revision Clearing Values for all days in the applicable period of the adjustment.
- (c) “**User Annual Quantity Revision Difference Transportation Charge Adjustment**” is the amount established:
- (i) Multiplying the daily additional NDM Supply Meter Point Demand (under 7.4.5 (b) (i)) for each day in the relevant Gas Year in which Y (as defined in paragraph (a) above) was in effect by the Applicable Commodity Rate of the NTS Commodity Charge, the LDZ Commodity Charge and the Commodity Variable Component (if any) of the Customer Charge for such day to determine the daily reconciliation charge adjustment; and
  - (ii) Aggregating the daily reconciliation charge adjustments for all days in the applicable period of the adjustment.

## SECTION F: SYSTEM CLEARING, BALANCING CHARGES AND NEUTRALITY

*Paragraph 5.1.1 shall be amended to read:-*

“5.1.1 Upon each Individual Reconciliation, Aggregate NDM Reconciliation and End of Year AQ Reconciliation, the quantity of gas comprising.....”

*The following shall be added as a new sentence at the end of paragraph 5.2.1:-*

“The Clearing Charge (“**End of Year AQ Reconciliation Clearing Charge**”) in respect of the System Clearing Contract under paragraph 5 shall be the Annual Quantity Revision Difference Clearing Value in accordance with Section E7.4.5.”

*Paragraph 5.2.2 shall be amended to read:-*

“5.2.2 The buyer shall pay the Reconciliation Clearing Charge, the Aggregate Reconciliation Clearing Charge or the End of Year AQ Reconciliation Clearing Charge to the seller.”

*Paragraph 5.2.3 shall be amended to read:-*

“5.2.3 The Reconciliation Clearing Charge, the Aggregate Reconciliation Clearing Charge or the End of Year AQ Reconciliation Clearing Charge shall be invoiced and payable in accordance with Section S.”

*The following shall be added as a new paragraph 5.2.6:-*

“5.2.6 The End of Year AQ Reconciliation Clearing Charge shall be treated as payable for the purposes of End of Year AQ Reconciliation as and when invoiced by Transco in accordance with the provisions of Section S.”

Signed for and on behalf of Transco.

Signature:

**Peter Rayson**  
**Commercial Manager - Customer**

**Support Services**

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 **0640**, version **2.0** dated **21/05/2004**) 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 **2.0**.

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.