Modification Report
Modification Reference Number - 0017

This modification report is made pursuant to Rule 8.12 of the Modification Rules and follows the format required under Rule 8.12.4.

1. Circumstances Making This Modification Urgent

In accordance with Rule 9.2(a) Ofgas has agreed that this modification should be treated as URGENT because the prices generated by the use of the Flexibility Market to balance supply and demand during March 1996 are seen as non representative and non neutral to be used for imbalance cash-out and reconciliation purposes.

2. Procedures Followed

TransCo agreed with Ofgas (and has followed) the following procedures for this Proposal:

4 April 1996 - Meeting held.
11 April 1996 - The Proposal was circulated.
17 April 1996 - System User representations made.
18 April 1996 - Modification report to OFGAS.
April 1996 - Implementation.

3. The Modification Proposal;

To introduce a single system price for March 1996. i.e. all system average prices, system marginal prices, to be used for Energy Balancing and reconciliation. This is option 1 of the Discussion Document circulated with the proposal.

4. Text provided pursuant to Rule 8.14;

Transition Document Part II, paragraph 8 -

Add a new paragraph F1.2.1 as follows:

"F1.2.1. During March 1996 the System Marginal Buy Price, the System Marginal Sell Price and the System Average Price on each Day shall be 0.6701 p/kWh. (20 p/therm) and accordingly F1.2.2 shall not be deemed to apply during March 1996 so as to produce different prices."

Transition Document Part III -

Add the following at the end of section S1.4.2:

"Provided that the expected date for submission of the first reconciliation invoice is 7th May 1996 (rather than the 18th Business Day above). This shall not be deemed to be a change or delay for the purposes of sections S1.4.2, S1.4.3 and S4.2.6".

increases level of indebtedness to each other.

relates only to CVA

5. TransCo's opinion:

This proposal maintains the treatment of energy quantities in accordance with the Network Code and is relatively easily implemented using existing systems functionality.

6. Extent to which the modification would better facilitate the relevant objectives:

The modification achieves a more equitable treatment of March 1996 imbalances and reconciliation amounts given discrepancies in customer portfolios and data flows within the month. The differences in the daily System Average Price, partly due to the illiquidity of the Flexibility Mechanism, used for reconciliation are neutralised. Shippers following their own view of their demand are treated equitably with those that followed TransCo's view of their demand by making the daily prices for reconciliation the same as the imbalance prices.

7. The implications for TransCo of implementing the Modification Proposal, including:

a) implications for the operation of System and any BG Storage Facility:

None

b) development and capital cost and operating cost implications

None

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 is not seeking to recover additional cost.

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

TransCo is not aware of any impact on price regulation.

8. 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:

Depending on the price option for the single system price, there is an impact on the Phase 1 cap.

9. The development implications and other implications for computer systems of TransCo and related computer systems of Relevant Shippers:

There will be a delay in the submission of reconciliation invoices. It will be necessary to re-format prices and re-run reconciliation programs for UK-LINK.

10. The implications of implementing the modification for Relevant Shippers.

Shipper imbalances will be bought and sold at the same price as generated by the Network Code rules. Shippers will not be penalised by System Marginal prices for daily imbalances and cumulative imbalances, including unauthorised flows. The price will be the same for all daily reconciliation variances for the month of March 1996.

11. The implications of implementing of the modification for terminal operators, suppliers, producers and, any Non-Network Code Party;

Transco has not been informed of any impact on any Non-Network Code Party.

12. Consequences on the legislative and regulatory obligations and contractual relationships of TransCo and each Relevant Shipper and Non-Network Code Party (if any), of the implementation of the Modification Proposal;

TransCo has not been informed of any consequences of the legislation and regulatory obligations and contractual relationships of implementing this proposed modification.

13. Analysis of any advantages or disadvantages of the implementation of the Modification Proposal;

Advantages:- Maintains the treatment of energy quantities under the Network Code and can be implemented with the existing TransCo and Shippers system's functionality. It does not require a parallel data management system to manage the carrying forward of imbalances and the management of reconciliation quantities. The process provides a recognisable audit trail. Imbalances are cashed out at the price generated in accordance with market expectations using a previously agreed methodology. The relatively high price reflects the availability of gas in March. There is no additional smearing of system costs.

Disadvantages:- March reconciliations require re-running to alter prices (not quantities). However, this is minor compared with the systems implications of an alternative option that carries forward imbalance and reconciliation quantities to pre-Code run-off arrangement (option 2) where it would be necessary to determine deemed opening reads for April.

Changing prices could be seen as setting an unwanted precedent for the future. However the proposal only changes the reconciliation prices and not the imbalance prices. Some feel reconciliation prices should be neutral to balancing.

14. Summary of the representations (to the extent that the import of those representations are not reflected elsewhere in the modification report;

13 shippers in total responded to TransCo's modification proposal 0017.
5 shippers were in favour of option 2 in the discussion document and 8 were in favour of option 1, the modification proposal contained within this report, but with different price recommendations.

Shippers in favour of option 1 cited the following:

- the rules that existed at the time at which decisions were made are the only ones which can truly deemed to be fair.
- this removes the potential for considerable and unpredictable reconciliation costs which shippers are unable to mitigate .
- the cash-out price should be calculated in accordance with the Network Code rules.

Shippers in favour of options 2 cited the following:

- roll over is the correct market signal .
- give time to sort out March problems.
- given data quality problems and uncertainty in the application of the reconciliation process to the broad NDM portfolio this is the most appropriate solution.

Concerns expressed regarding option 1 were:

- the arbitrary setting of prices.
- the setting of a precedent in changing Network Code prices.

Concerns expressed regarding option 2 were:-

- The required system changes, although more detail was requested regarding impact on systems.
- The difficulty in the prediction of reconciliation quantities. The Alliance proposal that 1st April becomes effectively a new start read for Network Code moves March reconciliation variances prospectively into April and beyond.
- Gas is effectively "swapped" between different pricing periods, i.e. March 1996 versus winter 96/97.
- A new and ongoing mechanism would be required to avoid double counting March reconciliation quantities.
- Is not consistent with Modification 0012.

There was no consensus with regard to the price for option 1 although there was a measure of support to use the system generated price of 0.6701 p/kWh. TransCo, having already adjusted prices by agreed Modification 0012, believes that the system price goes some way to reflect the availability of gas during the March period (This view has been expressed by a number of shippers). There is a concern that the spot market was not liquid during March and therefore prices would not be reflective of a value for gas.

15. The extent to which the implementation is required to enable TransCo to facilitate compliance with safety or other legislation;

The modification is not required to facilitate compliance with safety or any other legislation.

16. Having regard to any proposed change in the methodology established under Standard Condition 3(5) or the statement; furnished by TransCo under Standard Condition 3(1) of the Licence;

The proposed modification is not required to comply with the above clause.

17. Programme of works required as a consequence of the implementation of the Modification Proposal;

Not Applicable

18. Proposed implementation timetable;

It is important that the work necessary to implement this modification is undertaken as soon as possible. Reconciliation invoices were due to be run on 1st April 1996 and are being consequently delayed.

19. Recommendation for the implementation of the modification;

TransCo recommends that this modification is implemented as soon as possible.

20. 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.

21. TransCo Proposal

This Modification Report contains TransCos proposal to modify the Network Code which TransCo has already received a direction from the Director General to make in accordance with this report.

Signed for and on behalf of British Gas TransCo.

Signature:

Date:

Name:

Position:

Director General of Gas Supply Response

In accordance with Condition 7 (10) (b) of the Standard Conditions of Public Gas Transporters' Licences dated 21st February 1996 I hereby direct British Gas TransCo that the above proposal be made as a modification to the Network Code.

Signed for and on behalf of the Director General of Gas Supply.

Signature:

Date:

Name:

Position:

ANNEX 1

Any provision contained in this Agreement or in any arrangement of which this Agreement forms part by virtue of which this Agreement or such arrangement is subject to registration under the Restrictive Trade Practices Act 1976, shall not come into effect:

(i) if a copy of the Agreement is not provided to the Director General of Gas Supply ("**the Director**") 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 Director 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 paragraph (2)3 of the Schedule to the Restrictive Trade Practices (Gas Conveyance and Storage) Order 1996;

provided that if the Director does not approve the Agreement as aforesaid then the following clause shall apply:

Any provision contained in this Agreement or in any arrangement of which this Agreement forms part by virtue of which this Agreement or such arrangement is subject to registration under the Restrictive Trade Practices Act 1976 shall not come into effect until the day following the date on which particulars of this Agreement and of any such arrangement have been furnished to the Office of Fair Trading under Section 24 of the Act (or on such later date as may be provided for in relation to any such provision) and the parties hereto agree to furnish such particulars within three months of the date of this Agreement.