

URGENT Modification Report
Exemption from (Mod 414) Zero Tolerance/Energy Incentive for Irish UK Interconnector
Modification Reference Number 0456

Version 2.0

This Modification Report is made pursuant to Rule 9 of the Modification Rules and follows the format required under Rule 8.9.3.

Circumstances Making this Modification Proposal Urgent:

In accordance with Rule 9.1.2 Ofgem has agreed that this Modification Proposal should be treated as Urgent because the reduction of the ITQ and ATQ to a zero percentage is due to be applicable from 1 April 2001. Ofgem considers it prudent to grant this Modification Proposal Urgent status, so that a decision can be made in advance of the reduction of these tolerances.

Procedures Followed:

Transco agreed with OFGEM (and has followed) the following procedures for this Proposal:

Issued to Ofgem for decision on urgency	27 February 2001
Proposal agreed as urgent	2 March 2001
Proposal issued for consultation	2 March 2001
Close out for representations	16 March 2001
Final report to Ofgem	22 March 2001
Ofgem decision expected	27 March 2001

1. The Modification Proposal

"The Interconnector between Ireland and the UK at Moffat is administered by an Agency Agreement between Irish and UK Shippers. The Agency handles various Nominations and Renominations between Shippers in Ireland, Northern Ireland and the UK. It also provides an Offtake Profile requirement for the Irish Transporter and Transco. It is also not possible for Irish Shippers to improve on the management the offtake at Moffat any more than is already in place. The Moffat interconnector is different in many ways to any other Interconnector due to the dependence on this source of gas by customers in Ireland both North and South, these customers include the residential market. This Zero Tolerance would only cause Irish Shippers to pay additional penal charges for gas from the UK. This effectively increases the costs of gas to Irish End users."

2. Transco's Opinion

From the 1 April 2001 both the ATQ and the ITQ will have an Applicable Imbalance Percentage of zero, this effectively reduces the imbalance tolerance for all shippers to zero. Provisions for the NDM Forecast deviation will remain unchanged (Network Code section F paragraph 2.2.3).

Bord Gais Eireanns modification proposes several options that essentially attribute a unique exemption from the zero tolerance to the Irish system entry point, the Moffat UK/Ireland

interconnector. Bord Gais consider that its proposal may help to mitigate any consequential imbalance risk, caused by uncertainty in respect of Irish domestic market loads. Furthermore Bord Gais consider that they are discriminated against in respect of the Irish domestic market, in that the Mainland UK domestic market will retain a variable tolerance based on the forecast deviation.

The forecast deviation is intended to mitigate any shipper risk of being placed in an imbalance position as a consequence of the forecasted NDM nomination, provided by Transco, varying from the subsequent NDM demand attribution. An adjustment will be made to the imbalance tolerance to compensate for any variance in the forecast. The tolerance adjustment for forecast deviation is considered to be small (if any) and variable. Additionally it is only relevant to a shippers imbalance position if the imbalance falls in the same direction as the forecast deviation. The purpose of the forecast deviation was to promote shipper delivery of gas for NDMs based on Transco NDM forecasted nominations.

Transco considers that Bord Gais Eireanns proposal does not recognise the potentially small tolerance value that the forecast deviation holds. Furthermore Transco would argue the forecast deviation is only relevant to domestic supply points deemed to be within the mainland UK. The reasoning behind this is that Transco holds the necessary data to determine the forecasted NDM nomination for mainland domestic customers only, and therefore it would only be appropriate to apply a forecast deviation to those sites. Transco does not consider it appropriate to attribute a forecast deviation to Moffat based on Irish NDM end users.

An option raised in the modification proposal is the introduction of an OBA at the Moffat interconnector. Bord Gais Eireann discuss this option further in its response to the modification proposal. An OBA would offer the Moffat Agent the opportunity to carry over a percentage imbalance. This carry-over would be based on the entire throughput and not focused on the Irish domestic market offtake, which is considered to be a small percentage of the entire offtake.

Transco would not support this option as it argues that the CSEP ancillary agreement and the Connected System Agreements offer adequate balancing provisions. Additionally Transco would highlight that there are no other instances within mainland UK transportation system where an exit point has OBA arrangements, therefore this option would again be discriminatory in nature.

Transco considers that there are more appropriate means by which Bord Gais may reduce imbalance risk caused as a consequence of flow uncertainty for the Irish domestic market. These measures would have no detrimental effect on Transco relevant objectives and would not discriminate against other system users.

* In accordance with the CSEP ancillary agreement and Connected System Agreement, nominations through the UK/Irish interconnector can be amended to reflect the changing profiles of the offtake in the domestic market.

* Bord Gais argue that it is not in a position to manage its flows for the Irish domestic market. Transco would suggest that Bord Gais may wish to consider using linepack within the interconnector and the Irish transportation system to support its end users.

* Bord Gais may wish to consider the merits of applying a forecasting mechanism to determine greater accuracy of demand for its NDM end users. Possibly mirroring the forecasting mechanism in Mainland UK.

In conclusion Transco is not in support of Modification Proposal 0456. Transco is of the opinion that the Bord Gais Eireann modification proposal conflicts with Transcos relevant objectives in that it proposes transportation arrangements that are generally viewed to be preferential. Transco views the application of a unique zero tolerance exemption for any CSEP, or exit point, as discriminatory to other system users. It considers that the discriminatory nature of the proposal may lead to the inefficient and uneconomic operation of the gas pipeline. Additionally Transco argues that efficient and economic operation may be further compromised should similar dispensations be considered for other exit points.

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

This modification proposes discriminatory transportation arrangements. It therefore does not meet the relevant objectives in that it compromises the Gas Act section 9 and PGT License Condition 11 (1), which state that the Transporter must avoid undue preference or discrimination.

**4. The implications for Transco of implementing the Modification Proposal , including
a) implications for the operation of the System:**

For a start date of 1 April Transco systems could only support the implementation of a delay to the reduction of the zero tolerance in its entirety. Transco could not support the unique application of a tolerance to an individual shipper or exit point. Complex manual processes would be required.

b) development and capital cost and operating cost implications:

As Transco recommends rejection of the Modification Proposal no detailed analysis has been carried out. However it is likely to be significant.

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:

Not considered.

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

Not considered.

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

Transco is unaware of any such consequence.

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

Transco system cannot support the modification proposals option to uniquely exclude the Moffat interconnector from zero tolerance by April 2001. Transco systems could only support the option to delay the 1 April implementation for the reduction of tolerance percentage for all system users.

This modification proposal will have a system impact on both Transco and Bord Gais Eireanns computer systems.

7. The implications of implementing the Modification Proposal for Users

The Modification proposal is viewed as potentially discriminatory against other System Users and may increase costs.

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

Irish Shippers and Transporter would benefit from the proposal and this may have the consequential effect of benefiting the end user in Ireland. Mainland shippers will have no benefit and may in fact bear some increased cost. Other Connected System Operator may seek similar dispensations.

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

Transco would not be acting in accordance with section 9 of the Gas Act or section 11 of its licence, which state that the Transporter must avoid undue preference or discrimination.

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

Adv - Potential lower prices for the Irish domestic market.

Disadv - Potential for higher prices in the UK.

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

Representation have been received from 10 respondents. These are Northern Electric & Gas Limited, Bord Gais Eireann, Powergen, Scottish & Southern Energy, Associates of Electricity Producers, Yorkshire Energy Limited, British Gas Trading, Alliance Gas Ltd, Dynegy and Innogy. All the respondents express the view that they were not in support of the modification proposal.

A number of respondents express a degree of sympathy with Bord Gais Eireanns position however they view the imbalance risk, from the reduction of tolerances, as one that is borne at all CSEPs and exit points. Associated Electricity Producers articulated the view of a number of the responses. It argues that although it has some sympathy for the concerns raised by the proposer it does not believe that being unable to perfectly match allocations to nominations justifies different treatment for the UK/Ireland interconnector. Adding that it would be concerned that this proposal could set a precedent for future modifications.

The general consensus of the proposal is that it discriminates against other system users and proposes preferential transportation agreements for the Moffat UK/ Irish interconnector. Scottish & Southern Energy highlight that not only would this proposal discriminate against all other shippers it is also conflicts with the intentions behind the introduction of the zero tolerance. Dynegy concurred with this view explaining that it does not consider that Transcos relevant objectives would be furthered by the implementation of this modification. It views that the discriminatory nature of this proposal would result in inefficient and less economic operation of the pipeline, adding that this may be replicated with other exit points seeking similar dispensations. Alliance Gas raised concerns that if the Bord Gais Eireann modification proposal is accepted similar principles could be considered for the Bacton interconnector. It suggests that this may give rise to further gaming opportunities from the European markets leaving the UK sandwiched between Europe and Ireland, with the UK consumers covering the cost that may arise.

Two respondents consider that the proposal would go against the Ofgem reform objectives of targeting costs to those participants that have caused them and shippers balancing their portfolios.

A common view that ran through the responses was that of Moffat Interconnector being no different to any other interconnector or system offtake. Yorkshire Energy Ltd highlight concerns that the implementation of this proposal would result in shippers in the UK mainland incurring extra costs for the failure of other parties to balance gas flows. British Gas Trading highlight that nominations through the UK/Ireland interconnector are independent of the end customers. It adds that nominations through the interconnector can, also in accordance with the CSEP ancillary agreement and Connected System Agreement for UK/Ireland interconnector, be changed in order to reflect the changing profile of offtake in the domestic and industrial market.

Northern Electric & Gas suggested that it is not the responsibility of Transco to provide non-daily meter demand forecasts for Irish end users and hence it would be inappropriate to apply a forecast deviation tolerance to such users.

The response from Alliance Gas discusses observations it has made in respect of the Irish gas transportation system. Alliance Gas states that it believes that the domestic market in Ireland only represents approx 12% of the total market. It suggests that this is able to be supported by indigenous supplies which are under the control of BGE Trading. Alliance Gas continues that BGE's ability to meet domestic variation will be further augmented by its storage project, which is due to come on stream in 2002, and supplies from Corrib field in 2003. The remainder of the Irish market is either power generation or process load which should be capable of being forecasted to the same degree of accuracy as in the UK. To permit an exemption would provide an absolute tolerance equivalent to the total throughput at Moffat whilst only a small fraction is domestic.

Alliance Gas goes on to explain that Moffat is continuously monitored and rarely exceeds a 1% imbalance between nomination and actual delivery. Alliance Gas suggest that exemption from a zero tolerance regime may present opportunities to arbitrage tolerance between the two connected systems.

A number of respondents discuss alternative means by which Bord gas Eireann can better mitigate its imbalance risk, caused as a consequence of uncertainty within the Irish domestic market offtakes. British Gas Trading considers that the establishment of an Agency at Moffat to ensure correct allocation of the gas should mean that there is even less need for tolerances in the interconnector. Any errors made in matching allocations and nominations fall under the agreement Shippers have with the Moffat Agency and are independent of tolerances on the NTS.

British Gas Trading view the argument that end users of the interconnector are not in a position to manage their flow from the UK as flawed, to the extent that the transportation company for UK/Ireland interconnector should use its own linepack to support its end users. The NTS should not be seen to be subsidising end users in Ireland.

British Gas Trading conclude that it does not consider any of the options proposed in the modification as acceptable.

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

Transco is unaware of such requirement

13. The extent to which the implementation is required 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

Transco is unaware of any such requirement.

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

Transco is recommending rejection of this proposal and has not therefore constructed such a programme.

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

Transco does not recommend implementation and therefore has not proposed a implementation timetable.

16. Recommendation concerning the implementation of the Modification Proposal

Due to the respondent unanimous opposition to the Modification Proposal, and based on the arguments discussed in this report, Transco would recommend rejection of this Modification Proposal.

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 not to modify the Network Code and Transco now seeks agreement from the Gas & Electricity Markets Authority in accordance with this report.

19. Text

Signed for and on behalf of Transco.

Signature:

Tim Davis
Manager, Network Code

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 **0456**, version **2.0** dated **22/03/2001**) 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.