

URGENT Modification Report
Operational Linepack service
Modification Reference Number 0457
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 removal of the ATQ and ITQ is due to take place from 1 April 2001, Ofgem believes that it is prudent to grant this Modification Proposal urgent status, so that a decision can be made in advance of the removal 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	13 March 2001
Proposal agreed as urgent	14 March 2001
Proposal issued for consultation	14 March 2001
Close out for Representations	23 March 2001
Final report to Ofgem	28 March 2001
Ofgem decision expected	30 March 2001

1. The Modification Proposal

Cinergy Global Trading has raised Modification Proposal - 0457 'Operational Linepack Service'. The proposal seeks to create a surrogate balancing tolerance by providing for a small proportion of system linepack to individual shippers for each day. Shippers with imbalances within their allocation of linepack will be able to avoid cash-out exposure and carry imbalance over to the next gas day. The proposal is intended to provide shippers with some protection from cash-out exposure with respect to 'unavoidable' small imbalances.

The Modification proposes an operational linepack service as follows;

'Where the sum of a user's UDQOs and UDQIs is greater than zero the user will have a linepack quantity calculated as follows, subject to a cap and collar, where any imbalance within this amount is not cashed out within day but have the imbalance carried over to the next day.

The Imbalance Linepack quantity for a User for a Day shall be determined as the sum of the following, subject to a maximum and minimum quantity:

- (i) the inner tolerance applicable for the User's UDQOs in respect of DM supply Point Components, including VLDMC Supply Point Components, as specified in the "Network Code Validation Rules" (referred to in section M1.5)
- (ii) 1% of the User's UDQOs in respect of relevant Connected System Exit points and
- (iii) 1% of the User's UDQIs in respect of System entry points

Where the linepack quantity is greater than zero, the linepack will be the greater of:

- (i) the amount calculated above
 - (ii) 117,228 kWh
- and the lessor of
- (i) the amount calculated above
 - (ii) 293,071 kWh'

2. Transco's Opinion

The industry has discussed for the past year and subsequently agreed a number of proposals that have resulted in the phased removal of all balancing tolerances. The latest proposal on the subject, Modification Proposal 0421, 'Temporary Extension of Absolute Tolerance Quantity' had the effect of removing the absolute tolerance quantity (ATQ) from 1 April 2001. ATQs provide shippers who are out of balance by an absolute value of less than 7500 therms with protection from system marginal price (SMP) cash-out exposure. Transco's view is that this Modification Proposal (0457) effectively reintroduces a tolerance of a similar magnitude, albeit in the guise of a linepack service.

Transco is not in support of this Modification Proposal primarily because it is inconsistent with recent developments in the balancing/tolerance regime. Transco argues that Ofgem, in its document 'Further reform to the gas balancing regime', has indicated that it believes that the true commercial value of imbalances may be shown by a Linepack service. Transco considers that the present proposal equates to offering shippers free linepack which may undermine the Ofgem principles and be construed as inconsistent with recent developments.

Furthermore, Transco considers that the introduction of an operational linepack service cannot be supported with system changes necessary to deliver the proposal for 1 April 2001. Transco System Support has highlighted concerns that Modification Proposal 0457 would involve extensive reprogramming of AT Link or extensive and high risk offline transactions. These transactions would be for all shippers that have input and offtaken gas on any day on, or after, the proposed implementation date. Transco observes that the proposed tolerance ranges are very small and considers that the administrative complexities involved would far outweigh any benefit, particularly in the light of the risk from the carry-over effect between days.

The Modification Proposal discusses the carry over of imbalances from the preceding day. Transco has concerns at the implications and risks involved in an, effectively, rolling imbalance, where the individual shipper is not responsible for the purchase and management of its linepack quantity. Additionally Transco observes that the carry over effect of line pack between gas days implies that any allocation amendment may potentially have the effect of changing energy balancing charges, for the shipper, for each day forward. This could rapidly bring the regime into disrepute.

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

Transco considers that the Modification Proposal does not better facilitate the relevant objectives in that it compromises the efficiency and economic operation of the pipeline.

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

a) implications for the operation of the System:

System changes to support this Modification Proposal are understood to involve complex reprogramming that cannot be delivered for 1 April 2001. Therefore high risk and complex offline transactions for all shipper input and oftaken gas will be required. Transco cannot deliver these manual processes in the prescribed timescale.

b) development and capital cost and operating cost implications:

Development and cost is considered to be significant, but cannot be accurately assessed in the timescale available.

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

If implemented this proposal would increase Transco's contractual risk due to operating via complex and unproven offline processes.

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

Transco and Shippers would be required to modify their systems to accommodate the proposed linepack service. This is not achievable for Transco in such short timescales, therefore high risk offline processes would be required.

7. The implications of implementing the Modification Proposal for Users

Transco is not aware of the full implications for Users but considers that implementing offline processing to support this change at short notice would increase the risk to users.

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

Transco is not aware of any such implications.

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 is not aware of any legislative or regulatory consequences.

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

Advantages :

The Modification Proposal offers some protection against true operational uncertainty.

Disadvantages :

The Modification Proposal is inconsistent with recent developments in the balancing regime.

Due to the short implementation timescales high risk offline processes would be required.

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

Representations have been received from nine respondents.

Six respondents express support for the proposal. These are Cinergy Global Trading, Alliance Gas Ltd, Conoco, Shell Gas Direct, Total Fina Elf and EnMO Ltd.

Three respondents were not in support of the Modification Proposal. These are British Gas Trading, Powergen and Aquila.

Respondents that express support for the Modification Proposal generally viewed the proposal as a means by which to mitigate imbalances caused as a consequence of the uncertainty associated with physical delivery of gas into and out of the pipeline system. Shell Gas Direct Ltd articulates the view of a number of supportive respondents. Explaining that to ensure Shippers do not face penal charges as a result of uncertainties, it considers that it would be appropriate to provide Shippers with some protection against System Marginal Prices that would otherwise be applied to these unmanageable imbalances.

Shell Gas Direct discuss the Modification Proposal in the light of Ofgem's latest consultation document. Shell Gas Direct observes that Ofgem in its paper reinforces the expectation that a linepack service should be introduced shortly. It considers that Ofgem is encouraging the industry to adopt new mechanisms by which to manage risks of uncertainty associated with physically delivering gas. British Gas Trading argues that Ofgem has indicated that it believes a linepack service will reveal the true commercial value of imbalance. This Modification Proposal seeks to give shippers free linepack thereby undermining this principle, and in effect renders development of a linepack service redundant. Aquila adds that it believes that the Transco provision of this service, which is not paid for individually by shippers, moves the regime backwards (toward tolerances) rather than forwards (toward a physical linepack service).

Cinergy Global Trading highlights that the current rules will result in added premiums on quantities smaller than the minimum block size tradeable via the OCM. Cinergy Global Trading consider that the premium on these small quantities will disadvantage smaller players and do not provide a market reflective price for such quantities. It suggests that the quantities could be viewed as being a disproportionately large percentage of the small shippers portfolio. Alliance Gas suggests that this Modification Proposal will protect shippers from the penal marginal costs for small imbalances which have a negligible effect on the overall system balance and may create a barrier to entry for smaller shippers.

Total Fina Elf articulate a point observed by a number of respondents in support of the Modification Proposal. It notes that in the absence of an operational linepack service, Ofgem has recognised the need for the provision of limited relief from marginal cashout prices, following the removal of tolerances and the introduction of the revised marginal cashout prices derived from Modification 0433. Additionally, Alliance Gas observes that following the reduction of the ITQ and ATQ to zero from the 1 April 2001, shippers will be exposed to significant additional risk without any means of mitigating that risk. Alliance Gas continues that the risk is particularly pertinent in April, which as a shoulder month can be a time of significant swings. Aquila suggest that the linepack amounts proposed are of very limited financial consequence to participants in the market.

Conoco considers that the proposal would, to a certain extent, encourage shippers to manage their portfolio within a tighter band and having some allowance would enable Shippers to make a judgement on their requirements for a future linepack service.

Powergen and British Gas Trading argue that the proposal is a move to reintroduce an Absolute Tolerance Quantity (ATQ) under another name. Powergen highlights that it has been a long standing objective to remove the ATQ from the Network Code, originally conceived as a transition arrangement. British Gas Trading considers that the incentives for shippers to balance would be weakened by the introduction of an operational linepack service at this stage.

Transco's Opinion

In its response to the Modification Proposal Cinergy Global Trading suggests that the Transco system changes necessary to facilitate this change are minimal due to the similarity with the old regime. This is not the case. Transco systems cannot support this change with existing functionality, as additional variables are required in the proposed linepack service compared with the old regime, and changes would need to be made on where data is sourced from. Transco systems cannot support this change in the short term and therefore complex high risk manual processes would be required that may compromise the efficiency and economic running of the pipeline system.

The Modification proposal discusses the carry over of imbalances to the next day. Transco has concerns over the implications and risk involved in an infinite rolling imbalance where the individual Shipper is not responsible for the purchase or management of its linepack quantities. Furthermore, Transco is concerned that having balances not closed out within the day, or at month end, would run against the principles of the Network Code.

In conclusion Transco has some sympathy with shippers that consider a modest tolerance necessary to protect against true operational uncertainty. However, Transco considers that Modification Proposal 0457 is an inappropriate vehicle by which this may be achieved. At such short notice Transco systems cannot support this proposal for the proposed implementation date. Additionally Transco views the carry over effect of line pack between gas days as meaning that any allocation change would potentially change energy balancing invoicing for that shipper for every day forward, which could rapidly bring the regime into disrepute. Therefore, Transco considers that it cannot support this Modification Proposal.

Transco is of the opinion that should a method to protect shippers against true operational uncertainty be required, then this should be discussed in conjunction with the wider changes to the balancing regime. Alternatively, consideration of a

pragmatic continuation of the ATQ for all shippers with a full daily cashout may be viewed as appropriate.

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

Transco is unaware of any such requirement.

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 linked to any such change.

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 does not propose any implementation timetable.

16. Recommendation concerning the implementation of the Modification Proposal

Transco recommends 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

No legal text is provided as Transco is not in support of this Modification Proposal.

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 **0457**, version **2.0** dated **28/03/2001**) 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 appropriateprovided 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.