

**Draft Modification Report**  
**Removal of Energy Balancing Incentives from the Network Code**  
**Modification Reference Number 0519**

Version 4.0

This Draft 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**

If implemented this Modification Proposal would remove existing provisions that relate to Transco's energy balancing incentive from the Network Code. This Modification Proposal would facilitate Ofgem's proposals, i.e. the migration of Transco's energy balancing incentive from the Network Code into Transco's Gas Transporters (GT) Licence and enable Transco to manage NTS SO energy balancing incentive amounts via the proposed NTS SO Commodity charge.

It would be necessary to ensure that the proposed amendments to the Network Code are coordinated with any relevant amendments to Transco's GT Licence to avoid any conflict between the terms of the two documents.

The Network Code provisions which relate to and underpin the energy balancing neutrality process are outside the scope of this Modification Proposal.

**2. Transco's Opinion**

Transco believes that this Modification Proposal is required to facilitate Ofgem's proposals to revise the structure of Transco's NTS System Operator (SO) incentives. Ofgem's proposals would result in the definition of Transco's incentives, incentive parameters and provisions for the calculation of incentive amounts being contained within Transco's GT Licence.

Transco believes this Modification Proposal would facilitate Ofgem's proposals by enabling the migration of Transco's energy balancing incentive scheme from the Network Code into Transco's GT Licence. This migration would result in the NTS SO energy balancing incentive being defined through Transco's GT Licence and included as part of the calculation of Transco's NTS SO allowed revenue.

Transco believes that failure to implement this Modification Proposal might lead to inconsistency, duplication and conflict between the provisions of the Network Code and the proposed Transco GT Licence conditions.

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

In the event that Transco's energy balancing incentives are incorporated into Transco's GT Licence, Transco believes that it would be necessary to remove the existing provisions that relate to energy balancing incentives from the Network Code to mitigate the risk of a conflict arising between the terms of the Network Code and Transco's GT Licence.

Therefore, Transco believes that implementation of this Modification Proposal would better facilitate adherence to the relevant objective contained in Standard Condition 9 of its GT Licence, i.e. the efficient discharge of Transco's obligations under its GT Licence.

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

If this Modification Proposal is implemented there would not be any implications for the operation of Transco's System.

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

Transco is not aware of any development, capital or operating cost implications that would arise from the implementation of this Modification Proposal.

**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 applicable.

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

This Modification Proposal does not propose any changes to Transco's allowed revenue or the way in which it is recovered.

**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**

The effect of this Modification Proposal would be to marginally reduce Transco's contractual risk under the Network Code through the removal of the energy balancing Incentive scheme. However, it is envisaged that this affect would be offset by the inclusion of Transco's energy balancing Incentive scheme in Transco's GT Licence.

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

Transco's computer systems would be unaffected if this Modification Proposal is implemented. Transco is unaware of any impact upon Users' systems.

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

If this Modification Proposal is implemented Users would no longer receive ad-hoc invoices in respect of energy balancing incentive amounts.

**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 unaware 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**

The contractual obligations faced by Transco and Users in relation to Transco's energy balancing Incentive would cease to be defined by the Network Code.

The regulatory obligations which would arise from the potential amendments to Transco's GT Licence are not the subject of this Modification Proposal.

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

The advantages of implementing this Modification Proposal are:

- facilitating the implementation of Ofgem's proposed governance structure;
- prevention of a potential conflict of terms between the Network Code and Transco's GT Licence in respect of Transco's NTS SO incentive schemes;
- facilitation of an appropriate governance structure and a stable regulatory regime within which Transco may respond to its incentives.

The stated advantages are consistent with Ofgem's view that "...those aspects of the new incentive arrangements that have the potential to materially affect Transco's financial position should be included in its licence. We consider that this is necessary to provide Transco with a sufficient degree of certainty in order to allow it to respond to its incentives." (paragraph 11.6: Transco's NTS SO incentives 2002-07, Final Proposals).

The disadvantage of this Modification Proposal is that the Network Code may be considered to be more flexible than Transco's GT Licence in respect of the ease with which it may be amended to respond to regime changes. However, Ofgem has adopted the view that this disadvantage is offset by the need to balance "...the flexibility offered by the Code against the need for stability and certainty." in determining the appropriate governance structure for Transco's incentives. (paragraph 11.5: Transco's NTS SO incentives 2002-7, Final Proposals).

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

Representations are now sought in respect of this Modification Proposal.

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

Not Applicable.

**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**

Implementation of this Modification Proposal is not required in relation to any proposed change in the methodology established under Standard Condition 4(5) of the statement.

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

A program of works would not be required as a consequence of implementing this Modification Proposal.

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

It is proposed that the implementation of this Modification Proposal be aligned with the potential modifications to Transco's GT Licence and be implemented no earlier than 1 April 2002.

**16. Recommendation concerning the implementation of the Modification Proposal**

Transco recommends implementation of this Modification Proposal is aligned with, and subject to, modification of Transco's GT Licence.

**17. Text**

SECTION D: OPERATIONAL BALANCING, TRADING ARRANGEMENTS AND ENERGY BALANCING INCENTIVES

*Rename Section D as 'OPERATIONAL BALANCING AND TRADING ARRANGEMENTS'.*

*Delete paragraph 3.*

TRANSITION DOCUMENT PART II

*Delete text at paragraph 8.2.1 and insert new text and new paragraph 8.2.2 to read as follows:*

"8.2.1 In respect of the application of Section D3 in the period from 1 October 2001 up to (and including) the Day preceding the date of implementation of the Modification to the Code giving effect to this paragraph ("**relevant period**") (and by which modification Section D3 ceased to apply):

- (a) a reference to a Gas Year shall be treated as a reference to the relevant period;
- (b) amounts payable in respect of the relevant period by way of User Daily Incentive Amounts, User Annual Incentive Interest Amounts and User Annual Incentive Adjustment Amounts (under the Price Incentive Arrangement and the Linepack Incentive Arrangement collectively) shall continue to be invoiced and payable in accordance with Section S notwithstanding that such amounts are invoiced and payable after the relevant period; and
- (c) amounts payable under paragraph (b) shall be calculated in accordance with Section D3 as it applied immediately prior to the end of the relevant period.

8.2.2 For the purposes of paragraph 8.2.1 terms used therein shall have the meaning attributed thereto in Section D3 as it applied immediately prior to the date of implementation of the Modification to the Code giving effect to this paragraph."

***Representations are now sought in respect of this Draft Report and prior to Transco finalising the Report***

Signed for and on behalf of Transco.

Signature:

**Tim Davis**  
**Manager, Network Code**

Date: