

Modification Report
Termination of User who seeks or becomes subject to the appointment of an administrator, liquidator, conservator, trustee or similar official for it or for all or substantially all of its assets.
Modification Reference Number 0525
Version 3.0

This Modification Report is made pursuant to Rule 8.9 of the Modification Rules and follows the format required under Rule 8.9.3.

1. The Modification Proposal

It is proposed that if a User seeks or becomes subject to the appointment of a receiver, administrator, liquidator, conservator, trustee or similar official, unless a written commitment is provided that is satisfactory to the Energy Balancing Credit Committee (EBCC), Transco will be obliged, unless directed otherwise by the EBCC, to issue a Termination Notice to a User. This written commitment represents an assurance from the receiver, administrator, conservator, trustee, liquidator or similar official that it will pay Transco all the energy balancing debt accrued since the date of appointment. It further seeks to ensure that the Termination Notice will not be issued in less than two business days of Transco being notified of any such appointment.

2. Transco's Opinion

Whilst Transco is essentially neutral in respect of energy balancing it acts in the interests of Users as a whole and recognises that this Modification Proposal may be considered likely to introduce additional benefits to Users, in the event of the appointment of an administrator, liquidator, conservator, trustee or similar official.

The recent implementation of Modification 0475 "Termination of User in Receivership" was an initial step towards protecting the community from increasing debt exposure once a receiver is appointed by introducing the requirement for the receiver to provide adequate assurances to Transco in respect of all Energy Balancing debt accruing from and including the date of appointment. This proposal widens the scope of Modification 0475 to include assurances from an "administrator, conservator, trustee, liquidator or similar official" in addition to a receiver, requiring that they should also provide adequate assurance that they will pay all monies due relating to Energy Balancing debts accruing from the date of their appointment.

In widening the scope of Modification 0475 the proposer has specified the circumstances in which Transco's discretion to issue a Termination Notice would be removed, there are however two circumstances (i.e. the appointment of a conservator or trustee) that are not currently included within the scope of Section V 4.3. Transco proposes to extend the scope of Section V 4.3.1 (e) to accommodate individual bankruptcy scenarios by making reference to the appointment of a Trustee. Transco intends to exclude a specific reference to the appointment of a conservator as such

official is not appointed under English law, and instead suggests the inclusion of a clause that envisages insolvency events in foreign jurisdictions. In addition, Transco suggests that a reference to "a liquidator" is not included within Section V4.3.3. While it is possible that an administrator, receiver and trustee could continue operating the Defaulting User's business as a going concern, a liquidator is more likely to sell the assets and accordingly it is not appropriate to request a liquidator to provide an undertaking in respect of ongoing debt.

Transco agrees that the EBCC would be the appropriate body to review the written assurances provided by such party in order to ensure compliance with the Energy Balancing Credit Rules.

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

The proposer has highlighted the fact that the community will continue to be burdened with risks associated with a User being unable to fulfil its obligations regarding the payment of Energy Balancing Debt, stating "... the smearing of these uncontrolled costs may seriously jeopardise an individual Users ability to operate in the UK Gas Market". This potential debt burden could be viewed as a form of subsidy, it could further be considered that such subsidies are symptoms of inefficient or uneconomic operation, therefore the implementation of this Modification Proposal could be viewed as enhancing efficient and economic operation of the system.

Additionally as implementation may reduce the risk of exposure to financial loss for all Users by reducing the potential debt burden via the balancing neutrality mechanism it could further be viewed that implementation of this Modification would facilitate the securing of effective competition between relevant shippers and suppliers reducing the potential debt burden that may act as a barrier to entry.

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

a) implications for the operation of the System:

Operation of the system could be affected if the likelihood of issuing of a Termination Notice to a User were to increase. Under current arrangements it may be possible that supply may be discontinued to certain individual supply points until such time that there is certainty surrounding the appointment of a Supplier of Last Resort (SOLR).

b) development and capital cost and operating cost implications:

Transco is not aware of any capital cost or operating cost implications as a result of implementation of this modification.

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 does not believe it is appropriate to put in place any cost recovery measures as a result of implementation of the Modification.

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

Transco is unaware of any such consequences

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 degree of contractual risk is dependant on the prevailing circumstances upon appointment of a SOLR, but in general this may be expected to have a neutral effect on Transco.

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

Transco is not aware of any implications for the development of Transco or Users' computer systems

7. The implications of implementing the Modification Proposal for Users

Implementation of this Modification Proposal could be expected to have favourable implications as it is intended to reduce the risk of financial exposure on Users through the balancing neutrality mechanism

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

In the circumstances outlined within this Modification Proposal there is a potential effect on a number of parties, including suppliers and consumers. Implementation of this Modification Proposal, linked with robust SOLR provisions, should limit the period of uncertainty for these parties and with it any ongoing debt exposure. Implementation of this proposal in conjunction with certainty regarding the appointment of a SOLR could therefore be considered to be of benefit to all parties.

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 consequences on the legislative, regulatory obligations or contractual relationships of Transco, Users or Non-Network Code Parties as a consequence of implementing this Modification Proposal

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

Advantages of implementing this Modification Proposal;

- May increase the leverage which Transco has on the receiver, administrator, trustee or similar official to provide a commitment to cover ongoing debts
- May reduce the exposure of Users as a whole to costs arising through balancing neutrality as a result of non-recovery of energy balancing debt
- Strengthens the role of the EBCC in assessing whether satisfactory ongoing debt commitments have been made.

Disadvantages of implementing this Modification Proposal are that it would:

- May increase the likelihood of serving a Notice of Termination.
- May increase the likelihood of a Notice of Termination being issued and no SOLR being appointed therefore, unsecured debts might continue to accrue for an extended period.
- May lead to some classes of customers supply being discontinued in the event of termination without SOLR arrangements being in place.

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

Six representations have been received in respect of this Modification Proposal, all are supportive of its objectives and agree that the benefits gained from the implementation of Modification 0475 have been eroded due to the unintentional restrictions that Section V4.3 of the Network Code currently imposes on Transco in respect of its Termination obligations.

Total Fina Elf (the proposer) states 'the recent termination of a User's licences by Transco, (sic) not specifically associated with the appointment of a receiver, highlighted an unintentional limitation to Transco's termination obligations that was not envisaged during the development of mod 0475. The limitation arises from the network code legal text used to implement mod 0475. This specifies that termination obligations are restricted exclusively to the appointment of a receiver. If this limitation is not addressed, it would seriously undermine the wider safeguards and benefits envisaged and intended via the introduction of mod 0475, if, in the

future a User became subject to the appointment of anyone other than a receiver.' and goes on to say that 'implementation of this mod will remove an undesirable and unintentional restriction to Transco's termination obligations that would otherwise continue to seriously undermine the intended safeguards and benefits gained by the implementation of mod 0475. TFEG & P therefore see no reason to delay the implementation of this proposal.'

Powergen Uk Plc concurs with this view stating 'events with Enron have shown that the wording in the original modification needs better definition in that there are circumstances where it is not a receiver but some other such official appointed' and go on to say ' we would like to see more robust credit arrangements in the gas regime, and a clear definition of responsibilities helps towards this, thus we reiterate our support for this proposal.'

Innogy agrees that the definition within the legal drafting of Modification 0475 is too narrow, and states 'We believe that extending the scope of the definition of "receiver" contained within modification 0475 affords the community extra protection against accumulating energy balancing debt. This modification proposal 0525 simply makes more explicit the intent underlying proposals 0475.'

Transco agrees that the legal drafting of Modification 0475 has imposed unintended restrictions and supports the scope of the definition being extended.

British Gas Trading also supports the implementation of this Modification Proposal and states 'We concur that the terminology used when Modification Proposal 0475 was implemented was too narrowly defined and that this Modification seeks to expand this definition to encompass any party acting in the role of administering the affairs of a Company as a result of insolvency.' Transco supports this view. By inclusion of Trustee and Conservator the scope of this Modification Proposal does not restrict to corporate failure.

Scottish and Southern Energy Plc (SSE) agrees that there is a need to update the Energy Balancing Credit Rules and extend the benefits gained from the implementation of Modification 0475 as highlighted by recent events, in order to minimise the risk of financial loss to Users as a result of a User's default. Scottish and Southern acknowledges that this Proposal seeks to extend the principles introduced under Modification 0475 and states 'SSE saw this as the first step towards the introduction of more robust procedures to protect shippers from accrual of debt that is ultimately unrecoverable.' and concludes by agreeing that the EBCC is the correct forum for such matters to be referred to stating 'SSE agree that the Energy Balancing Credit Committee should have the ability to review any assurances and provide Transco with guidance as to appropriate action it should take.'

Transco is not minded to oppose this view, but would point out that experience has shown that Transco has acted in the best interests of community in such situations with a view to minimising Users' exposure to financial loss.

Shell Gas Direct, whilst supporting the proposal highlights the benefits that the Proposal would bring in better facilitating the 'Relevant Objectives' and states ' We agree with the proposer's view that the current arrangements can be viewed as a form of cross-subsidy. Furthermore, its implementation would facilitate competition between shippers as it removes potential uncontrollable debt burdens which may act as a barrier to entry. Transco concurs with this view.

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

Transco is not aware 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

Transco is not aware of any such requirement

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

Transco is not aware of any works required to facilitate the implementation of this Modification Proposal. Changes proposed would be in the area of operational controls for the Credit & Risk Management functions within Transco. Such changes would be discussed and agreed with members of the EBCC.

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

If the decision was taken to implement this Modification Proposal, Transco believes that the authority should focus discussions surrounding the appointment of a SOLR to provide certainty, further that the implementation date should be agreed following the EBCC's satisfactory conclusion of discussions on changes required to the Energy Balancing Credit Rules and or the Network Code Supplement. This would allow all relevant changes to take effect simultaneously.

16. Recommendation concerning the implementation of the Modification Proposal

In view of the recent implementation of Modification Proposals 0474 "Revision to Indebtedness cash - Call Trigger" and 0475 "Termination of User in Receivership"

having a similar scope and given the support received through consultation for this proposal Transco recommends implementation 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 to modify the Network Code and Transco now seeks direction from the Gas & Electricity Markets Authority in accordance with this report.

19. Text

SECTION V - INSERT NEW PARAGRAPHS V4.3.1(e) (vi) and (vii) AS FOLLOWS

- "(vi) the Defaulting User becomes subject to a bankruptcy order; or
- (vii) the Defaulting User becomes subject to an event made in a jurisdiction outside England and Wales, equivalent or analogous to any one or more of those events listed in paragraphs 4.3.1(e)(i) to (vi) above; or....

SECTION V - DELETE V4.3.3(c)(i) & (ii) AND INSERT NEW PARAGRAPHS V4.3.3(c)(i) & (ii) AS FOLLOWS:

- (i) a User Default occurs by reason of the circumstances set out in any one or more of paragraphs 4.3.1(e)(ii), (iii) or (vi), or 4.3.1(e)(vii) to the extent that a person, analagous or equivalent to those persons appointed pursuant to paragraphs V4.3.1(e)(ii), (iii) or (vi) is appointed in a jurisdiction outside England and Wales ("**foreign insolvency practitioner**") in respect of the User; and
- (ii) the receiver, administrator, trustee-in-bankruptcy or foreign insolvency practitioner (as appropriate) fails to provide adequate assurances to Transco in compliance with the principles established in the Energy Balancing Credit Management Supplement and Energy Balancing Credit Rules (such assurances not to exceed a legal and binding commitment by the receiver, administrator, trustee-in-bankruptcy or foreign insolvency practitioner (as appropriate), to pay to Transco all Energy Balancing Debt accruing from (and including) the date of appointment of the receiver, administrator, trustee-in-bankruptcy or foreign insolvency practitioner (as appropriate)), as soon as reasonably practicable after being appointed (but for the avoidance of doubt not within two Business Days of its appointment).

THE SUPPLEMENT TO NETWORK CODE (SECTION X) - AMEND PARAGRAPH X4.2.1 AS FOLLOWS:

- 4.2.1 Before Transco shall take the action envisaged by paragraph 4.1, Transco shall convene a meeting of the Energy Balancing Credit Committee as soon as reasonably practicable following the ~~receiver's failure~~ of the receiver, administrator, trustee-in-bankruptcy or foreign insolvency practitioner (as appropriate) to provide those assurances referred to in Section V4.3.3(b) and shall consult with the Energy Balancing Credit Committee to determine whether Transco should be obliged to issue the Termination Notice, pursuant to paragraph 4.1, or whether Transco should defer taking such step.

Signed for and on behalf of Transco.

Signature:

Steve R Phillips
Director of Shipper 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 **0525**, version **3.0** dated **08/03/2002**) 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 **3.0**.

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.