

Modification Report
Cessation of Invoicing for Terminated and Discontinued Users
Modification Reference Number 0633
Version 1.0

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

This proposal is intended to apply only in the case of a User being Terminated or requesting Voluntary Discontinuance, i.e. where the User is exiting the market and does not have any Supply Points registered, does not hold any Capacity of any type and does not hold any open trading positions. It is not intended to impact in any way on the invoicing relationship between Transco and Users in the ordinary course of business.

The proposal seeks to link the date of the invoicing position becoming final to the cessation of activity by the User and the change in User Status, but with a minimum 3 month notice period.

Given that Users operate differently under the Network Code according to the nature of their business, there are two parts to this proposal:

1. In the case of a User who has operated in the NDM market as well as the DM, it is proposed that the invoicing position becomes final 18 months from the end of the month in which the last NDM supply point left the portfolio, the last Capacity holding expired or the last Trade was completed whichever is the later. For example, if the last supply point left on 13th March 2003 and Capacity was held until 31st March 2003, the invoicing position would close on 30th September 2004.
2. In the case of a User who has operated exclusively in the DM Market and/or as a Trader, it is proposed that the invoicing position becomes final 6 months from the end of the month in which the last DM supply point left the portfolio, the last Capacity holding expired or the last Trade was completed whichever is the later. Continuing the example above, if the last supply point left on 13th March 2003, but the User held Capacity until 30th April 2003 and had Trades up to 31st May 2003, the invoicing position would close on 30th November 2003. This reflects the different treatment of reconciliation in the two markets.

Once a User has been Terminated or requested Voluntary Discontinuance, Transco and the User will review the circumstances applicable to the User's portfolio(s) in the light of (1) & (2) above and the required minimum 3 month notice period proposed and confirm the Invoice Position Completion Date (IPCD). Again, using the examples above, if the User was Terminated or requested Voluntary Discontinuance on 30th June 2003, in both cases the IPCD would remain as above.

If however, the User was Terminated or requested Voluntary Discontinuance on 30th September 2003, whilst the IPCD in case (1) would remain unchanged, in case (2) it would move to 31st December 2003.

It is further proposed that as the IPCD will be known in advance, neither Transco nor the User should be able to raise any new disputes or queries in the final month leading to the IPCD to ensure Transco has time to process adjustments due.

It is believed that these periods should give Transco sufficient time to review invoicing issued for accuracy and completeness and allow the Terminating/Discontinuing User enough time to complete validation and disputes of invoices levied. This would also allow sufficient time for adjustments to be issued.

The proposal is intended to operate both ways, namely that as well as stopping invoices being issued, it would also prevent queries being raised by the User.

In view of the extensive periods factored in for review of the invoicing position and validation, it is believed that the vast majority of issues will be identified and resolved by both Transco and the User. Where adjustments become evident after closure, it is proposed that they would flow through the normal mechanisms for Transportation and Energy for unrecovered amounts. In this respect it should be noted that adjustments can be both debit and credit.

2. Transco's Opinion

Transco's opinion is that it does not support the Modification Proposal as, if implemented, the Shipping Community and Transco could be disadvantaged. In the event of Shipper insolvency, under the Insolvency Act Transco could continue to levy charges until the final dividend is declared. If the proposed changes to the Network Code were implemented, Transco would be forced to close out much sooner, and any charges would ultimately be borne by Transco or the Shipping Community and ultimately by Consumers. Only 1% of insolvencies are closed out within an 18 month period, and therefore Transco believes that it should continue to levy charges beyond this time as this would increase recoverable funds by way of increased dividends.

The statutory period in which to lodge a claim against an insolvent User (subject to fund dividend declaration) is six years and Transco questions why it would support a contractual change to restrict this given its role to mitigate financial exposure on behalf of the Community.

Transco is of the opinion that a distinction should be drawn between orderly exit from the market and insolvency. Transco considers that any measures that could be introduced to facilitate an orderly exit from the market (Voluntary Discontinuance) should be discussed as a topic at the Supply Point and Billing Workstream, and these discussions have now commenced.

Whilst Transco does not support any like consideration in instances of insolvency, Transco does support some of the views of the Proposer and some Shipper representatives at the Workstream in that there may be scope for development of the principles within the proposal in relation to Voluntary Discontinuance of a Solvent User.

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

Transco does not support implementation of this Modification Proposal as it considers it does not better facilitate the relevant objectives.

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

Transco is not aware of any impact to the operation of the system.

b) development and capital cost and operating cost implications:

Transco is not aware of any development or capital costs from the implementation of the 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:

Transco's costs would be treated as normal operating costs.

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

No such consequences have been identified.

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 may not be able to minimise the levels of bad debt to the Shipping Community if the proposal were implemented as it seeks to prevent the levy of some charges to an Insolvent User.

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 computer systems.

7. The implications of implementing the Modification Proposal for Users

Facilitation of market exit may be simplified for those Users electing Voluntary Discontinuance although these perceived benefits need to be assessed against the potential risks against all Users by those Users exiting the market through insolvency.

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

No such implications have been identified.

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 unaware of any change in legislative, regulatory obligations or contractual relationship of Transco, and each User or Non-Network Code Party as a consequence of implementing this Modification Proposal.

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

- The Proposer identified that an advantage of the Modification Proposal is that it provides the basis for an efficient and competitive market by players being able to enter the market, operate and leave that market.
- Transco considers that implementation of this Modification Proposal as drafted could disadvantage the Shipping Community and Transco in the event of Shipper insolvency

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 six Users, Powergen, TXU Europe Energy Trading Ltd (in Administration) ("TXU"), British Gas Trading ("BGT"), BP Gas Marketing ("BPG"), EDF Energy plc ("EDF") and Scottish and Southern Energy ("SSE"). Five Users are against implementation of the Modification Proposal with one User supporting implementation.

- 18 Month Rule

The views expressed in the representations focused on the potential risks of limiting the 18 month period to Users if this Modification Proposal were to be implemented. Powergen stated "*Powergen are not in favour of this proposal as it potentially increases the risk for shippers where Transco are*

unable to fully recover their charges". It also added that implementation would restrict the statutory 6 years during which Transco could recover charges from an insolvent User. SSE stated "We believe that if Transco were forced to close out on invoices, adjustments, queries or disputes within this timescale there would be significant risk to other Users who could be required to fund a share of any shortfall". EDF also supported this view and stated "We feel that there would be increased exposure for the community if insolvent Shippers were simply allowed to exit the industry without proper security in place after 18 months". EDF made reference to reconciliations occurring well after this period and the fact that there had been several insolvencies in recent years where shipper debt is still being smeared across the industry after 18 months. BGT also shared this view and stated "there is some risk inherent in the neutrality process that to facilitate a terminated or discontinued user to avoid this exposure could place an unacceptable risk to the remaining community if a large adjustment were to be affected".

However, BGT were of the opinion that a different approach was required to achieve the aim of this Modification Proposal and stated "Our preference would be to ensure that any charges which may be due are calculated and applied in a more timely manner for all Users". It further stated that this would provide greater certainty for the rest of the community by ensuring that there was no exposure to amounts due to the ceased User and eliminate the practice of significant retrospective adjustments over an extended period. In support of this approach BGT stated "It is our view that the introduction of an absolute close out of the billing position should be applied 18 months from the "event". " This would incentivise Transco to invest in processes and systems to ensure that billing was improved to a satisfactory standard".

The Proposer "TXU" in support of its proposal agreed that the detail within section one of this report 'Transco Opinion' was factually correct, in that either Transco or the Shipper Community would bear some increased costs by closing out sooner. However, it did make reference to this not being explicit as to the likely amount of the charges and stated "One would have thought that after 18 months both the probability of such charges occurring and the amount to be redistributed if such an event did arise, would be small".

TXU's clarified within its representation that the Modification Proposal was to address the administrative cost of the current open ended arrangements as it considered these outweighed the likely benefits after 18 months in respect of NDM shippers. It stated "If Transco's position is that it will accept no risk whatsoever in closing out the billing for User's who wish to withdraw from the Code then the only other alternative which would both allow User's to withdraw from the Code and for Transco to have no risk would be to close the billing for all Users on a defined timescale".

Transco's Response: Transco shares the view of those Users that consider early cessation of invoicing during the 18 month period to be inappropriate where a User is insolvent. Transco has provided information on the percentage of insolvencies closed out before this period (as detailed within this report) and considers any change to the 18 month period would impact on community exposure. SSE shared this view and stated "As only 1% of insolvencies are closed out within the 18 month period proposed it is difficult to see how this can be considered appropriate".

In response to TXU's reference to the likelihood of these charges being small amounts, Transco agrees that in some circumstances these charges may be considered as 'small' for some Users after

smearing. However, Transco would like to stress that certain charges which are raised are contingent on other Users raising queries which result in adjustments impacting on some or all Users during the 18 month period. In the sense that these charges are the result of actions by Users, they are not easy to predict.

In response to BGT's opinion that a different approach is required to incentivise Transco to ensure that any charges due are raised in a timely manner for all Users, Transco would like to confirm that it does make very effort to achieve to this currently. However, due to nature of the business, and notwithstanding the reasons as defined above, where other shipper queries may result in a revision to invoiced charges, it is very difficult to agree a finalised closeout position by a specific date without having an element of financial risk which would be borne by Transco and Users.

- Voluntary Discontinuance

Whilst the majority of representations do not support implementation of the Modification Proposal, three Users support the principle of allowing Users to exit from the market in an orderly fashion. Powergen stated "*In principle, we would support the introduction of measures to facilitate an orderly exit from the market for Voluntary Discontinuance, however a distinction does need to be drawn between voluntary exit from the market and termination*". This view was supported by BGT and it suggested that a different approach is required dependant upon the circumstances for cessation where an orderly close down of a business is being undertaken, but not in cases of insolvency. EDF also provided support for this and stated "*there is merit in designing a structure where a Shipper can exit the market in an orderly manner*". EDF also made reference to the procedure in the Electricity industry for exiting the market and whether or not elements could be adopted in the gas market.

Transco Response: Transco recognises Users concerns regarding the need to facilitate orderly exit from the market and has already commenced discussions at the Supply Point and Billing Workstream with a view to establishing whether any measures can be implemented to improve this process.

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

Transco does not believe that modification to Network Code is required in order to comply with Safety or other Legislation

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 to facilitate any such change.

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

Changes to processes, procedures and systems would be required to facilitate implementation of this proposal.

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

In view of Transco's recommendation, no implementation timetable is proposed.

16. Recommendation concerning the implementation of the Modification Proposal

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

No legal text has been provided as Transco does not support implementation of this proposal.

19. Text

Signed for and on behalf of Transco.

Signature:

Terry Grove
Service Delivery Manager

Support Services

Date: