

CODE MODIFICATION PROPOSAL No. 0043
"Limitation on offering for sale unsold capacity"
Version 2.0

Date: 29/03/2006

Proposed Implementation Date: 19/08/2005

Urgency: Urgent

Proposer's preferred route through modification procedures and if applicable, justification for Urgency

(see the criteria at http://www.ofgem.gov.uk/temp/ofgem/cache/cmsattach/2752_Urgency_Criteria.pdf)

Modification Proposal 0037 was granted Urgent status by Ofgem on 18th July 2005 based on the following justification by Transco NTS:

"Transco NTS requests Urgent status in respect of this Proposal on the basis that the proposed revisions need to be in place and effective before invitations are issued for the next long-term auctions for quarterly system entry capacity ("the QSEC auctions"). In accordance with the provisions of the UNC, the invitation letter for these auctions must be issued by 19 August 2005. It is recognised that this could be later were Modification Proposal 0030, "Extension of the QSEC auction timetable for 2005", to be implemented, however the timetable for Modification Proposal 0030 does not allow this to happen until at the earliest 4 August 2005, which would not allow sufficient time for this Proposal to be considered.

Transco NTS believes that without these provisions being in place prior to issuing the invitations for the next QSEC auctions there could be an adverse commercial impact on Transco NTS and Users (and also, therefore, to end consumers) as a result of potentially high buy-back costs at specific Aggregate System Entry Points."

Transco NTS considers that this Proposal, which is a refinement of the initial proposal 0037 (which has now been withdrawn) to seek to accommodate User representations received through the consultation process on the proposal, should also be granted Urgent status based on the same justification as the initial proposal.

Nature and Purpose of Proposal (including consequence of non implementation)

It is proposed that Transco NTS should not be obliged under the Uniform Network Code (UNC) to make Unsold NTS Entry Capacity ("unsold capacity") available to Users at an Aggregate System Entry Point (ASEP) for each gas day within a calendar quarter which Transco NTS would otherwise release through QSEC auctions (in accordance with TPD, Section B2.2) when the following criteria are met for QSEC auctions conducted within the current formula period (ie. up to 31 March 2007):

- Transco NTS assesses there is a significant risk that it will not be able to physically deliver all or part of the unsold capacity from the capacity allocation date. This would typically be caused by the length of time required to obtain consents or construction challenges, both of which may be beyond the full control of Transco NTS; and
- Transco NTS assesses there is an expectation that previously allocated capacity at the ASEP would need to be bought back.

If such criteria are met at any ASEP for one or more calendar quarters, it is proposed that the unsold capacity is set to zero in respect of any future annual, monthly or daily capacity auctions at the ASEP for any gas day within the relevant calendar quarter(s). By way of example, this would mean that if the above criteria are met in the 2005 QSEC auction for a System Entry Point for the first 4 calendar quarters for which capacity would otherwise be made available ie. Apr 07 to Mar 08, that the unsold capacity would be set to zero for that System Entry Point in respect of the following auctions conducted during the current formula period for capacity release on any relevant gas day within the period Apr 07 to Mar 08:-

- the Annual Monthly NTS Entry Capacity (AMSEC) auction (to be conducted during Feb 06 and Feb 07);
- Rolling Monthly NTS Entry Capacity (RMSEC) auctions; and
- the Daily NTS Entry Capacity auctions

In addition

However, Transco NTS, in making its assessment as to whether to release unsold capacity in any auction in accordance with the above such criteria, would still need to ensure that it was able to meet Special Condition C8B Part 2 paragraph 14(5)(f)(ii)(a) of its Transporters Licence to “use all reasonable endeavours to offer for sale” all obligated entry capacity. Transco NTS therefore believes that the criteria proposed to be included within the UNC when considered in combination with its Licence obligations would result in unsold capacity not being released through auctions conducted this formula period only in exceptional circumstances. It is envisaged that Transco NTS would be required to seek written permission from the Authority to not release unsold capacity. Transco NTS considers that this should mitigate industry concerns regarding the amount of discretion that Transco NTS may be perceived to be granted in not releasing unsold capacity, were this Proposal to be implemented.

Under such exceptional circumstances, Transco NTS considers that the total level of buy-back costs is likely to be higher, than would otherwise be the case, if the unsold capacity is offered for sale and would be above that considered to be efficient and economic. ~~This would particularly be the case in the event that Users purchase the unsold capacity solely on the expectation that they would receive buy-back payments.~~ While Transco NTS would be partly exposed to the buy-back costs in accordance with the incentive arrangements in its Transporter’s Licence, the capacity neutrality arrangements would result in all Users funding a significant proportion of these costs, which could ultimately be passed on to consumers.

If this Proposal were to be implemented, Users would be initially notified that Transco NTS is not releasing unsold capacity for each gas day within certain calendar quarters through the annual QSEC relevant annual or rolling monthly invitation process for the long and medium auctions, or by 12:00 ahead of the gas day for daily auctions. This would then be appropriately

reflected in any future annual or monthly auction invitations relating to any gas day within such a period.

Transco NTS believes this Proposal must be implemented prior to issuing invitations for the next QSEC auction, which, in accordance with the provisions of TPD Section B2.2, must state the amount of capacity that is available for each relevant capacity year. However, if this Proposal were not implemented in the timescales identified, Transco NTS believes it and other Users could be exposed to inefficient levels of buy-back costs, which would ultimately be borne by consumers.-

Basis upon which the Proposer considers that it will better facilitate the achievement of the Relevant Objectives, specified in Standard Special Condition A11.1 & 2 of the Gas Transporters Licence

Transco NTS considers this Proposal would, if implemented, better facilitate the following Relevant Objective as set out in its Gas Transporters Licence:

- in respect of Standard Special Condition A11 paragraph 1(a), the Proposal would better facilitate the economic and efficient operation of the NTS pipeline system by avoiding the potential increase in buy-back costs incurred by both Transco NTS and Users above that which would be considered to be economic and efficient as permitted by the Authority.

Any further information (Optional), likely impact on systems, processes or procedures, Proposer's view on implementation timescales and suggested text

a. Proposed implementation timetable

Transco NTS requests that the Authority considers the following timetable:

Proposal sent to Ofgem requesting Urgency	09/08/2005
Ofgem grant Urgent status	09/08/2005
Proposal issued for consultation (2 working days)	10/08/2005
Close out of representations	12/08/2005
Urgent Modification Report issued (1 working day)	15/08/2005
Modification Panel decide upon recommendation	17/08/2005
Revised Urgent Modification Report issued to Ofgem	17/08/2005
Ofgem decision expected	18/08/2005

b. Proposed legal text

UNC Transition Document – Part IIC (Transitional Rules)

Insert the following as new paragraph 1.1, and renumber existing paragraphs accordingly:

“1.1 TPD Section B: System Use and Capacity

1.1.1 TPD Section B2.1.5 and Section B2.1.6

- (a) In respect of any invitations for Quarterly NTS Entry Capacity issued prior to 31 March 2007, then the Unsold NTS Entry Capacity which Transco NTS shall be required to offer in such invitation shall be determined as follows:

In respect of an Aggregate System Entry Point and in relation to a Day in a calendar month in a Formula Year, "Unsold NTS Entry Capacity" is the amount of Firm NTS Entry Capacity that Transco NTS has, in relation to each Day in a calendar quarter, an obligation to make available (in accordance with the procedures set out in UNC TPD Section B2) to Users pursuant to paragraph 14(5)(f) of Part 2 of Special Condition C8B of Transco NTS's Transporter's Licence as, in the case of Quarterly NTS Entry Capacity to be made available under UNC TPD Section B2.2, set out in Transco NTS's Transportation Statement; provided that:

- (i) such Unsold NTS Entry Capacity shall not include any NTS Entry Capacity which Transco NTS assesses it may be unable to physically deliver for any reason if such NTS Entry Capacity were to be allocated at a given Aggregate System Entry Point, including for example, due to the length of time required to obtain consents or construction challenges; and
- (ii) such Unsold NTS Entry Capacity for a particular Aggregate System Entry Point shall be zero where Transco NTS assesses there is an expectation that Transco NTS would be required to accept daily capacity offers pursuant to UNC TPD Section B2.10 in respect of previously allocated NTS Entry Capacity at that Aggregate System Entry Point;

and (for the avoidance of doubt) the provisions of UNC TPD Section B2.1.5 shall not apply for the purposes of UNC TPD Section B2.2 in relation to any invitations for Quarterly NTS Entry Capacity issued prior to 31 March 2007.

- (b) In respect of any allocations of Quarterly NTS Entry Capacity pursuant to an invitation issued prior to 31 March 2007, then, for the purposes of the application of UNC TPD Section B2.6, the amount of Unsold NTS Entry Capacity in existence at a particular time will, unless expressly stated otherwise, be calculated by reference to a continuing obligation to make available Firm NTS Entry Capacity through the application of paragraph 14(5) of Part 2 of Special Condition C8B of Transco NTS's Transporter's Licence prior to the time at which the amount of Unsold NTS Entry Capacity is to be ascertained; provided that:
- (i) the amount of Unsold NTS Entry Capacity in existence at a particular time shall not include any NTS Entry Capacity which Transco NTS assesses it may be unable to physically deliver for any reason if such NTS Entry

Capacity were to be allocated at a given Aggregate System Entry Point, including for example, due to the length of time required to obtain consents or construction challenges; and

(ii) the amount of Unsold NTS Entry Capacity in existence at a particular time for a particular Aggregate System Entry Point shall be zero where Transco NTS assesses there is an expectation that Transco NTS would be required to accept daily capacity offers pursuant to UNC TPD Section B2.10 in respect of previously allocated NTS Entry Capacity at that Aggregate System Entry Point;

and (for the avoidance of doubt) the provisions of UNC TPD Section B2.1.6 shall not apply in such circumstances.

(c) Where (by virtue of the provisions of paragraph 1.1.1(a) or 1.1.1(b) above) the Unsold NTS Entry Capacity for a particular Aggregate System Entry Point is zero for a particular calendar quarter, then the Unsold NTS Entry Capacity for the purposes of paragraphs 2.2 (in relation to Monthly NTS Entry Capacity only), 2.3 or 2.4 of UNC TPD Section B shall also be deemed to be zero for each calendar month or Day within such calendar quarter, and (for the avoidance of doubt) the provisions of UNC TPD Section B2.1.5 shall not apply for the purposes of UNC TPD Section B2.2 (in relation to Monthly NTS Entry Capacity only), 2.3 or 2.4 in such circumstances.

Transportation Principal Document, Section B

Amend paragraph 2.1.5 to read as follows:

~~2.1.5— In respect of an Aggregate System Entry Point and in relation to a Day in a calendar month in a Formula Year:~~

~~(a) —~~

~~(b) —~~

~~(c) —~~

~~(i) —~~

~~(ii) —~~

~~(iii) —~~

~~an obligation to make available (in accordance with the procedures set out in this paragraph 2) to Users pursuant to paragraph 14(5)(f) of Part 2 of Special Condition C8B of Transco NTS's Transporter's Licence as, in the case of NTS Entry Capacity to be made available under paragraphs 2.2, 2.3 and 2.4 but not paragraph 2.5, set out in Transco NTS's Transportation Statement; provided that:~~

- (i) ~~Unsold NTS Entry Capacity in each case shall not include any NTS Entry Capacity which Transeo NTS reasonably assesses it may be unable to physically deliver for any reason if such NTS Entry Capacity were to be allocated at a given Aggregate System Entry Point, including for example, due to the length of time required to obtain consents or construction challenges; and~~
- (ii) ~~Unsold NTS Entry Capacity in each case for a particular Aggregate System Entry Point shall be zero where Transeo NTS reasonably assesses there is an expectation that Transeo NTS would be required to accept daily capacity offers pursuant to paragraph 2.10 in respect of previously allocated NTS Entry Capacity at that Aggregate System Entry Point.~~

Amend paragraph 2.1.6 to read as follows:

~~2.1.6 For the purposes of the application of paragraph 2.6, the amount of Unsold NTS Entry Capacity in existence at a particular time will, unless expressly stated otherwise, be calculated by reference to a continuing obligation to make available Firm NTS Entry Capacity through the application of paragraph 14(5) of Part 2 of Special Condition C8B of Transeo NTS's Transporter's Licence prior to the time at which the amount of Unsold NTS Entry Capacity is to be ascertained; provided that:~~

~~(a) the amount of Unsold NTS Entry Capacity in existence at a particular time shall not include any NTS Entry Capacity which Transeo NTS reasonably assesses it may be unable to physically deliver for any reason if such NTS Entry Capacity were to be allocated at a given Aggregate System Entry Point, including for example, due to the length of time required to obtain consents or construction challenges; and~~

~~(b) the amount of Unsold NTS Entry Capacity in existence at a particular time for a particular Aggregate System Entry Point shall be zero where Transeo NTS reasonably assesses there is an expectation that Transeo NTS would be required to accept daily capacity offers pursuant to paragraph 2.10 in respect of previously allocated NTS Entry Capacity at that Aggregate System Entry Point.~~

Amend paragraph 2.4.10 to read as follows:

~~2.4.10 Where there is no Available Daily Capacity in respect of an Aggregate System Entry Point for a Day, or the amount thereof is less than the minimum eligible amount, Transeo NTS will not accept any daily capacity bids. Where, following the application of paragraph 2.3, there remains Unsold Entry Capacity in relation to an Aggregate System Entry Point in respect of a Day but, as a result of the operation of paragraph 2.1.5 or 2.1.6, the Unsold NTS Entry Capacity in relation to that Aggregate System Entry Point in respect of that Day is less than that remaining after the application of paragraph 2.3, then Transeo NTS shall notify Users of the Available Daily Capacity in relation to that~~

~~Aggregate System Entry Point not later than 12:00 hours on the Preceding Day to that for which the Daily NTS Entry Capacity is being offered.~~

c. Advantages of the Proposal

Transco NTS believes that this Proposal, if implemented, would

- avoid potentially increasing buy-back costs that are already expected to arise as a result of previously allocated capacity at an ASEP above that which would be considered to be efficient and economic and thereby reduce costs for end consumers; ~~and~~
- remove the potential for Users to seek to obtain unsold capacity solely on the expectation that it will receive buy-back payments; and
- limit the applicability of the Proposal to QSEC auctions undertaken during the current formula period. This would allow further consideration as to the amounts of capacity that it is efficient and economic for Transco NTS to release as part of the next Transmission Price Control.

d. Disadvantages of the Proposal

Transco NTS recognises that this Proposal may limit the amount of unsold capacity that is made available to Users. However, Transco NTS believes that this is necessary in the specific circumstances set out in this Proposal.

It is recognised that this Proposal relies upon Transco NTS assessment of the likelihood of capacity not being physically delivered on time and the potential for buy-back of previously allocated capacity for the affected ASEP. It is also difficult to specify an exact level of risk applicable to all ASEPs and circumstances under above which unsold capacity would not be made available. However, in the event that Transco NTS does not make unsold capacity available, were this Proposal to be implemented:

- Transco NTS would still require to ensure it was able to meet Special Condition C8B Part 2 paragraph 14(5)(f)(ii)(a) of its Transporters Licence to “use all reasonable endeavours to offer for sale” all obligated entry capacity and would be expected to require written permission from the Authority to not release unsold capacity; and
- Transco NTS would limit its opportunity to earn entry capacity investment incentive revenue under Special Condition C8B Part 2 paragraph 14(5) of its Transporters Licence, unless the incentive cap had already been met for the relevant year.

e. The implications of implementing the Modification Proposal on security of supply, operation of the Total System and industry fragmentation

Transco NTS does not believe this Proposal, if implemented, would adversely impact upon security of supply or; operation of the Total System as the Proposal would not limit the availability of capacity against which Shippers Users could flow, and instead would only prevent release of capacity that is not expected to be physically available, ~~or industry fragmentation.~~ In addition, Transco NTS does not consider that this Proposal would prevent timely system enhancements as it could only be utilized under exceptional

circumstances under which it highly unlikely to be able to physically deliver investments under shorter timescales.

Transco NTS does not consider this Proposal would impact industry fragmentation.

f. The implication for Transporters and each Transporter of implementing the Modification Proposal, including

i. implications for operation of the System

Transco NTS does not believe this Proposal, if implemented, would adversely affect the operation of the System.

ii. development and capital cost and operating cost implications

Transco NTS considers that this Proposal would reduce the potential increase in buy backs costs it may incur above that which would be considered to be economic and efficient. However, if Transco NTS did not release unsold capacity, it may limit its opportunity to earn entry capacity investment incentive revenue under Special Condition C8B Part 2 paragraph 14(5) of its Transporters Licence.

iii. extent to which it is appropriate to recover the costs, and proposal for the most appropriate way to recover the costs

Transco NTS does not believe this Proposal, if implemented, requires it to recover any additional costs.

iv. analysis of the consequences (if any) this proposal would have on price regulation

In the event that this Proposal, if implemented, restricts the release of incremental obligated entry capacity, the associated revenues would be treated under the SO Entry Capacity Investment Incentive arrangements. However, if this Proposal is used to restrict the release of NTS SO baseline capacity (as defined in Transco NTS's GT Licence), there could be a modest increase in the TO commodity charge.

~~However Transco NTS does not believe this Proposal, if implemented, would have any consequence on price regulation.~~

g. The consequence of implementing the Modification Proposal on the level of contractual risk of each Transporter under the Code as modified by the Modification Proposal

Transco NTS believes that this Proposal could reduce the contractual risk that it is exposed to by reducing the volume of capacity that it is required to offer for sale in specific circumstances. However the proportion of buy-back costs which Transco NTS would incur over the periods considered by this Proposal (ie. from Apr 2007) are still to be determined – this will be considered in establishing future Transmission Price Controls.

h. The high level indication of the areas of the UK Link System likely to be affected, together with the development implications and other implications for the UK Link Systems and related computer systems of each Transporter and Users

Transco NTS does not envisage any impact on the UK Link System if this Proposal were to be implemented.

i. The implications of implementing the Modification Proposal for Users, including administrative and operational costs and level of contractual risk

Transco NTS considers that this Proposal would reduce the potential increase in buy backs costs incurred by itself and Users above that which would be considered to be economic and efficient. The proportion of the total buy back costs incurred by Transco NTS and Users would of course be considered as part of future Transmission Price Controls. However Transco NTS considers that this is a separate issue as to whether it is appropriate to release capacity in the knowledge that it is likely to give rise to buy-back costs, which must ultimately impact end consumer costs.

Code Concerned, sections and paragraphs

UNC Transition Document, Part IIC Transitional Rules ~~UNC Transitional Document, Section B~~

Proposer's Representative

Paul Roberts (National Grid Transco - UKT)

Proposer

Richard Court (National Grid Transco - UKT)

Signature

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